Research Study

Regulatory Intensity in the Regulation of Capital Markets: A Preliminary Comparison of Canadian and U.S. Approaches

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July 30, 2006

Commissioned by the
Task Force to Modernize Securities Legislation in Canada

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1. Overview and Executive Summary

My work for this study breaks down into two parts: a comparison of budgets and staffing levels for securities regulations agencies in the United States and Canada; and my collection of data on enforcement intensity in Canada followed by a comparison of enforcement intensity between the United States and Canada. Each part is presented in full in a separate section. My conclusions are summarized below. I include a few thoughts on policy implications at the end of the paper.

a) Budgets and Staffing

I begin with an analysis of regulatory budgets and staffing for securities market oversight in Canada and the United States. My principal findings are:

- In terms of budgets and staffing levels, the Canadian regulatory system is comparable to the overall regulatory system in the United States.
- Adjusted for by most measures of economic scale – population, GDP, or market capitalization – Canadian budgets and staffing may actually be somewhat more intensive than those in the United States. The level of Canadian supervisory budgets and staffing do not, however, seem wildly out of line as compared to the United States once one takes into account plausible estimates of economies of scale.
- One area in which Canada does differ somewhat from the United States is regulatory budgets per staff member. For the most part, Canadian costs per staff member are lower than their counterparts in the United States. Only costs for personnel in U.S. state agencies seem to be lower than average Canadian costs; costs per staff members at RS is roughly comparable to costs per staff member at the New York Stock Exchange (NYSE). But financial support for staffing among provincial authorities and two major Self-Regulatory Organizations ("SROs"), the Investment Dealers Association ("IDA") and the Mutual Fund Dealers Association ("MFDA").seem to be lower than what exists in the United States. Although data of this sort is difficult to interpret, these differences may speak to the relative quality of – or at least support for – Canadian supervisory personnel.

b) Enforcement Actions in Canada

The next section of my analysis focuses on enforcement activity of both provincial authorities and self regulatory agencies. My major findings are:

- Whether measured in terms of actions brought or monetary sanctions imposed, provincial authorities are the most important *public* enforcers of securities regulation in Canada. In recent years, these agencies have averaged 124 actions a year and are imposing monetary sanctions at a rate of US$219 million a year.
- Taken together, the Canadian SROs also undertake substantial enforcement efforts, bringing about 40 per cent of total public actions and imposing a substantially smaller share of sanctions (11 per cent).
- On average, provincial sanctions are a good deal larger than SRO sanctions, and the very largest provincial sanctions are also very much larger than the biggest SRO sanctions.
- Although the range of data I have collected differs for each agency, for most agencies there has been a substantial increase in enforcement activity, particularly towards the latter periods (2004 and some of 2005). While these increases are easily observable in IDA and RS data, they are most pronounced in data on provincial authorities, which have become increasingly dominant figures of Canadian securities enforcement in the time frame of my analysis, though the level of provincial enforcement activity has dropped off a good deal towards the end of my period of analysis.
- At both the provincial and SRO level, the increase in aggregate monetary sanctions is driven by a very small number of actions in which large penalties have been imposed. While these cases do not explain all of the growth in Canadian enforcement activity, they contribute the lion's share of that growth.

c) Comparison to U.S. Enforcement Levels

The primary goal of my study – comparing Canadian and U.S. enforcement levels – was complicated by the fact that Canadian enforcement activity appears to have been in the process of dramatic change during the period of analysis, including a precipitous spike of activity in 2004 and early 2005. To some degree, therefore, my conclusions depend heavily on the period of comparison. But, in summary form, my conclusions are as follows:

- In certain areas, the evidence is quite clear that Canadian enforcement activity is less intensive than U.S. enforcement activity. Although not the primary focus of my study because comprehensive Canadian data was not available, private enforcement (both arbitration and class action litigation) is much less common in Canada than in the United States. Criminal prosecutions also appear to be much less common.

- Public enforcement activity presents a more interesting case. If one focuses at the earliest periods for which I obtained data for each public Canadian agency (ranging from 2002 to 2004 depending on the agency), the level of public enforcement activity in Canada was much lower than that of the United States and the differences are so huge that they swamp any possible scaling adjustment. So, it seems that public enforcement activity in Canadian securities markets used to be much less intensive than U.S. enforcement activity.
- If one focuses instead on the full period of my data, enforcement activity in Canada has jumped up considerably, at both the level of provincial authorities and SROs, particularly if one focuses on monetary sanctions imposed. Comparisons based solely on public enforcement sanctions in these latter periods show Canadian public enforcement activity as still lower than U.S. public enforcement activity, taking in effect plausible scaling factors, but not of an entirely different magnitude. (Note, however, that private enforcement is still much lower.)
- Comparability in aggregate public sanctions at one point in time does not, however, imply equivalence in efficacy of enforcement. The increase in Canadian sanctions is driven by a very small number of large sanctions, both by provincial authorities and by SROs. In addition, these heightened sanction levels have persisted for only a short period of time, creating uncertainty as to whether they are a temporary phenomenon or permanent. U.S. regulatory officials, in contrast, have maintained a multi-year commitment to an extensive enforcement apparatus with broadly based sanctions as well as numerous large awards, particularly in recent years.
- Another interesting difference between Canadian and U.S. public enforcement activities is the relatively lower level of enforcement actions brought with respect to issuers. Whereas the preponderance of SEC enforcement actions involved issuers – either involving defective public offerings or financial misstatements, Canadian provincial authorities seem to focus more of their attention on broker-dealers, in a large degree overlapping with the jurisdiction of Canadian SROs.

2. Introductory Reservation

Before turning to the analysis, I begin with a series of reservations. International comparisons of the sort presented in this paper, that is, comparing regulatory budgets and formal enforcement actions ("regulatory intensity"), are problematic in many ways. I have discussed these problems at length in my academic work on the subject, but let me emphasize several basic points:

- First, different jurisdictions set different goals for their financial regulators. Some seek only minimal protections from systemic risk; others aspire to elaborate consumer safeguards. Some countries use their financial regulatory apparatus to effect political decisions such as detecting financial crimes or the effecting of social programs (such as income redistribution) through the financial system. Some countries choose decentralized regulatory structures to advance political goals, perhaps at the expense of efficiency. To the extent that jurisdictions set different goals for their financial regulators, one might reasonably expect variations in regulatory budgets and staffing or even enforcement activities.
- Second, even if two countries set exactly the same regulatory goals for their financial regulators, one would not necessarily expect to see identical levels of regulatory intensity. For one thing, the lawfulness of local populations may vary. Moreover, jurisdictions may pursue different approaches to regulation, one relying more on private ordering and another on public oversight. Even public oversight may be structured in substantially different ways, with a different balance of ex ante examination and inspection as opposed to ex post sanctioning and litigation. In other words, even if two countries are seeking the same regulatory ends, they may choose different regulatory means.
- Third, even if we were to conclude that two countries, say, Canada and the United States, had set the same goals for their oversight of capital markets and had decided to achieve those goals through substantially similar means, it does not follow that Canada should emulate U.S. regulatory intensity for the simple reason that the United States may not be pursuing an optimal policy in this area. Cost benefit analysis in the area of financial regulation is notoriously difficult, and there is no compelling evidence that the United States is currently striking the correct balance. Indeed, our academic journals are full of articles claiming that U.S. regulation is profoundly out of balance. (Unfortunately, there is no consensus as to whether we are doing too much or too little.)

Practical difficulties also complicate comparisons of regulatory intensity between jurisdictions. Pulling together comprehensive data about regulatory costs and enforcement actions is painstaking work. Data invariably comes from many sources and in many forms. It is difficult to be comprehensive but it is also easy to double-count as the same actions are often reported in multiple places and at multiple times. Researchers such as myself are also particularly challenged when collecting data from foreign jurisdictions. Without substantial local assistance it is difficult to be confident one has covered all the relevant bases and interpreted foreign information correctly. Finally, there are often questions whether foreign data has the same meaning as data from one's own jurisdiction. Prison sentences are a good case in point, as there is substantial variation in parole practices across jurisdictions. But even monetary sanctions and administrative orders may have different effects in different jurisdictions.

- For these and related reasons, one must treat inter-jurisdictional comparisons of regulatory intensity with considerable caution. Marginal differences, in my view, are likely to be of little significance. Only when substantial variations emerge are findings likely to suggest meaningful differences. And even then, one must be cautious in drawing inferences and making policy recommendations.
- Notwithstanding the foregoing reservations, I do think that comparing Canadian and U.S. regulatory intensity is an interesting and potentially valuable exercise. For a host of reasons, the regulatory philosophies in our two jurisdictions are quite similar. Geographic proximity coupled with substantially integrated capital markets and cooperatives arrangements, including the North American Securities Administrators Association ("NASAA") and the Multi Jurisdictional Disclosure System (MJDS) have brought our two countries to remarkably similar systems of financial regulation. Both countries have a federal system of oversight and also rely extensively on self-regulatory organizations. In addition, there are a host of other cross-border connections that links our markets and professional practices. While important differences persist – most notably in civil litigation traditions and criminal sanctions – securities regulation in the two countries has important and deep similarities. Regulatory goals are substantially comparable, and regulatory means are not too dissimilar, with the major exception being Canadian reliance on provincial regulatory agencies as opposed to our centralized Securities Exchange Commission.
- I have also found it easier to collect information on Canadian regulatory structures and enforcement activities than has been my experience with other jurisdictions. In part, this ease is the result of the considerable assistance I have received from the Task Force staff and, in particular, Professor Poonam Puri. But the amount of data available on the websites of Canadian provincial authorities and SROs is also quite high and complete by international standards (again, excepting data on civil litigation and criminal sanctions). I have also benefited from a number of

prior studies of Canadian securities markets and especially the work of Charles River Associates, Inc., which was kind enough to provide me with data on provincial and state budgets. As a result of all this cooperation, the data presented in this study draws principally on the following sources:

- An extensive survey of Canadian Securities Market Oversight completed under the auspices of the Task Force staff.
- Detailed data on enforcement activity of Market Regulation Services Inc. ("RS"), submitted by Doug Harris, Director of Policy, Research and Strategy, Market Policy.
- Enforcement data available online for Canadian provincial authorities, the Investment Dealers Association ("IDA"), and the Mutual Fund Dealers Association ("MFDA").
- Telephone interviews with several corporate practitioners – representing both plaintiffs and defendants – as well as a number of regulatory officials.

With the assistance of several research assistants at Harvard Law School, I have organized this data to permit comparison with data that I am in the process of developing for U.S. securities markets. While the comparisons are not perfect, and I note the major deficiencies below, I believe that the data I have assembled on Canadian regulatory intensity is sufficiently complete to justify the analysis presented in this paper.

I do, however, also want to stress that the current paper remains only a preliminary study, pulled together on what is a very tight time schedule for empirical work. Though prior drafts have been reviewed by several Canadian experts, I have not yet had a chance to present the paper to academic audiences or received the kind of rigorous vetting that would take place in such contexts. Thus, the policy recommendations I suggest below should all be regarded as preliminary and provisional.

3. Regulatory Budgets and Staffing Levels

One of the most straightforward ways to measure regulatory intensity in financial markets is to compare regulatory budgets and staffing levels across jurisdictions. To be sure, the size of regulatory budgets and staffing is not a perfect proxy for enforcement activity, but a reasonable level of regulatory staffing is perhaps a necessary condition for effective enforcement in financial markets. Accordingly, as an initial matter, I have attempted to compare the size of regulatory budgets and staffing across regulatory jurisdictions.

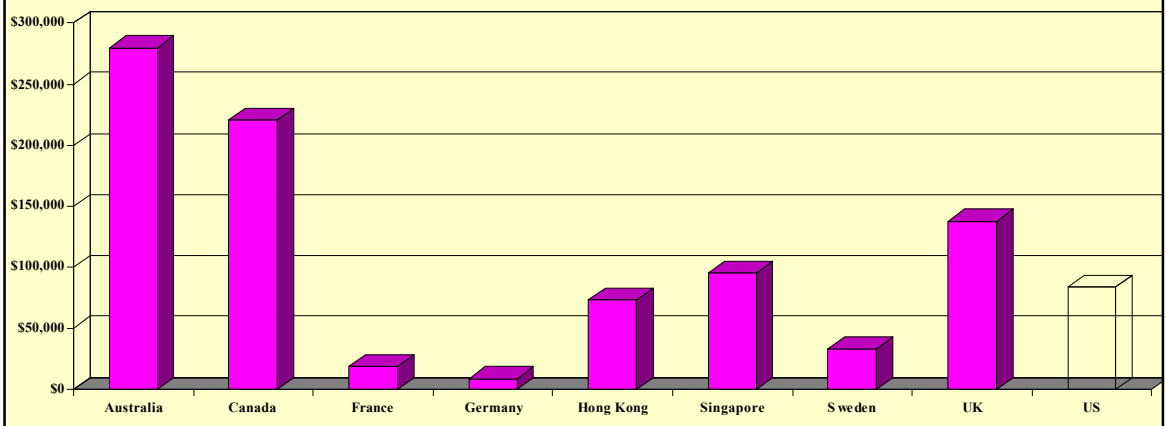
As it happens, this is an issue that I have considered in passing in prior writings on the subject of comparative regulatory intensity. In a working paper circulated last year, I presented the following chart on securities regulation in capital markets in a number of jurisdictions.[1] Figure 3 below is based on data assembled for a 2004 annual report by the Financial Services Authority of the United Kingdom ("FSA"). According to these FSA estimates, the Canadian securities regulation budget in 2004 was US$195.3 million with a staffing level estimated at 1,684 personnel.

Given the FSA's estimate of the size the Canadian equity markets at the time (US$885 billion), this analysis suggests that the supervisory budget of Canadian securities markets, once normalized for equity market size, was fairly intensive when compared with other jurisdictions included in this analysis. For example, the Canadian securities regulation budget per billion dollars of market capitalization in this analysis was US$220,515, whereas the U.S. regulatory costs per billion of market capitalization were estimated as US$83,943 in the UK's FSA analysis and the United Kingdom's own securities enforcement budget was estimated at US$138,159 per billion of stock market capitalization.

[1] See Howell E. Jackson, Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications (Aug. 2005) (Harvard Law and Economics Discussion Paper No. 521) (available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=839250).

Figure Three

Securities Regulation Costs Per Billion Dollars of Stock Market Capitalization

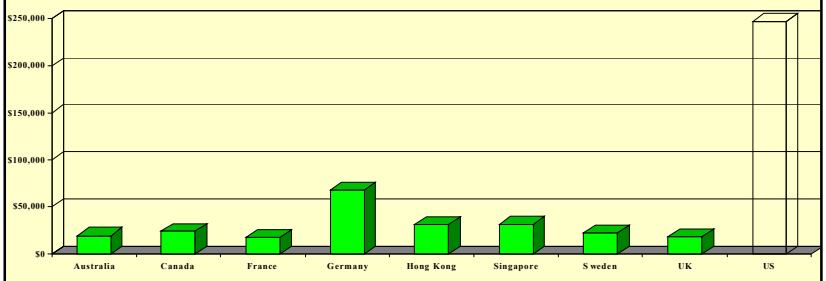


Source: FSA 2003/2004 Annual Report Appendix 5..

Another interesting aspect of this preliminary data about Canadian securities market oversight is the relatively different position of Canadian banking and insurance oversight budgets and staffing as compared to the level of insurance and banking oversight found in other jurisdictions covered in the FSA dataset. In both sectors of the financial services industry, Canadian oversight levels do not appear to be out of line with those of other jurisdictions. (Indeed, in terms of U.S. versus Canadian comparison, the level of Canadian banking oversight seems quite modest; this is, however, an artifact of the highly fragmented nature of the U.S. banking industry and the equally fragmented structure of banking supervision in the United States.) Graphs of banking and insurance regulatory budgets normalized for total bank assets and insurance premia in respective jurisdictions are set forth below (Figures One & Two).

Figure One

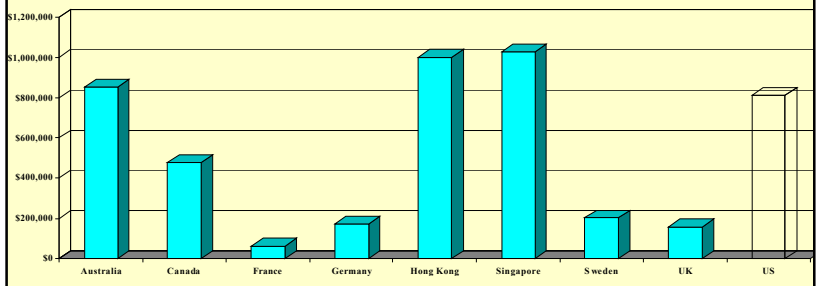
Bank Regulation Costs Per Billion Dollars of Banking Assets



Source: FSA 2003/2004 Annual Report Appendix 5..

Figure Two

Insurance Regulation Costs Per Billion Dollars of Insurance Premia



Source: FSA 2003/2004 Annual Report Appendix 5..

As this preliminary data with respect to Canadian securities regulation oversight was striking, I have attempted to construct a more comprehensive database of both Canadian and U.S. securities regulation budgets and staffing levels than was available in the FSA dataset from 2004. In comparing U.S. and Canadian regulatory apparatus, I have included a number of different methods of normalization, beyond the regulatory budget per billion dollars of market capitalization employed in my prior work. I have also attempted to give some thought to the question of whether differentials in regulatory budgets in the United States and Canada could, in large part, be reflective of differences in economies of scale.

a) Estimating the Regulatory Budget and Staffing Levels for the Canadian Securities Industry

An initial challenge is developing a more accurate estimate of the total Canadian regulatory budget for securities market oversight. As Canada maintains a federal system of securities market oversight and also makes use of a number of self-regulatory organization, this is a non-trivial task, and the information I have pulled together so far should be regarded as preliminary. As a starting point, I worked off a study undertaken by Charles River Associates International ("CRAI") in 2004. That report estimates the 2004 regulatory budget of Canadian provincial securities regulators as C$128.2 million. Working and updating the original data supplied to CRAI, I estimate that the current budget for Canadian provincial securities regulators is approximately US$127.7 million (or Cdn$143.3) and includes approximately 1,035 staff. Elements of this estimate are based on extrapolations of partial data, utilizing assumptions about average costs per staff member, and other estimates. The summary data is presented in Table 1.[2]

Table One

Provincial Budgets and Staffing for Securities Regulation

(Canadian Dollars)

	Budget	*Staff*
Alberta	$16,700,000	120
British Columbia*	$27,923,520	208
Manitoba	$3,300,000	34
New Brunswick	$837,085	7
Newfoundland	$837,085	7
Nova Scotia	$787,917	6
Nunavut	$250,000	2
NW Territories	$358,751	3
Ontario*	$61,929,237	376
PEI	$607,883	5
Quebec*	$28,248,000	249
Saskatchewan	$1,250,000	16
Yukon	$239,167	2
Totals:	$143,268,646	1035
US Dollars (5/23/05)	$127,677,898	

* Indicates author's adjustments to CRAI Data.

Shaded cells have been extrapolated in some way.

[2] Highlighted entries in Table 1 have been extrapolated. Most commonly, these extrapolations occur when I have obtained staff data but not budget data for an agency or visa versa. The extrapolations are based on an estimate of budgets per staff for the agency in question or comparable agencies.

In addition to provincial regulatory authorities, Canadian self-regulatory organizations, such as RS, the IDA and the MFDA also play an important role in regulatory oversight of Canadian capital markets. Table 2 summarizes my estimates of regulatory budgets and staffing levels for these organizations. Roughly speaking, these SROs have collective budgets and staffing equal to 50 per cent of all provincial authorities, or a total collective budgets of US$60.6 million (Cdn$68.0 million) with roughly 470 in staff. RS has another US$16.2 million supervisory budget (Cdn$18.1) with 71 staff. Thus, in total Canadian SROs have budgets of US$60.6 million with a staff of 470.

Table Two
Canadian SRO Budgets and Staffing
(Canadian Dollars unless otherwise indicated))

	Budget	*Staff*
Investment Dealers Association	$37,407,387	299
MFDA	$12,500,000	100
Subtotal	$49,907,387	399
US Dollars (5/23/06)	$44,476,377	
Market Regulation Services, Inc	$18,110,000	71
US Dollars (5/23/06)	$16,139,238	
Total SROs	$68,017,387	470
US Dollars (5/23/06)	$60,615,614	

When the data presented in Tables 1 and 2 are assembled, I estimate the current regulatory budget of Canadian securities regulation to be approximately US$188.3 billion with approximately 1,506 staff. As it turns out, this estimate is remarkably similar to estimates included in the FSA 2004 Annual Report (total budget of US$195.3 million with a staff of 1,684). This similarity, however, is something of a coincidence, as the components of my estimate differ in several respects from the FSA estimate, and also the U.S. Canadian exchange rate used in my analysis (1:1.12211 as of May 23, 2006) reflects a weaker U.S. dollar than existed in 2004. There are, however, enough similarities in several sources—the FSA estimates, the earlier work of CRAI, and my own analysis—to suggest that the estimates generated in my analysis here are not widely off the mark.

b) Estimating U.S. Regulatory Budget and Staffing Levels

I turn now to providing an estimate of securities regulation budgets and staff in the United States. The largest single source of regulatory oversight in the United States is the SEC with a budget of over US$917.6 million in 2005 and a staff of 3,865. The second most important source of supervisory oversight comes from state regulators. Unfortunately, data on state regulators is quite difficult to obtain, so I had to estimate total U.S. state budgets and staffing levels drawing on a combination of data collected by CRAI and my own research. For a number of states, no data was available and so I had to estimate budgets and staffing based on a regression analysis of states on which data was available.[3] The assumptions underlying this estimate are, I think, reasonable, but the result should, nevertheless, be viewed with some caution. According to my analysis, the total state budgets are estimated at roughly US$171.9 million a year with an estimated supervisory staff of 1,981. Aggregated with SEC data, these estimates suggest that public U.S. securities regulation budgets are in the order of US$1.1 billion and consist of some 5,843 staff. Adding in the NASD, the total staffing levels of U.S. securities regulators go up to 7,933 with an annual operating budget on the order of US$1.6 billion. Add in further the operations of NYSE Regulation, with a reported budget of US$150 million in 2004 and staffing of 650 personnel.[4] The total U.S. enforcement budget reaches nearly US$1.8 billion with a staff on the order of 8,586. Table 3 summarizes these results.

[3] To derive these estimates, I collected actual budget and staffing data from 27 states for 2004. In some instances, the data related to consolidated supervisory agencies, so I had to reduce these budgets and staffing levels somewhat. Using these figures, I then determined the ratio of budgets and staffing to state GDP levels and population levels, using log transformations and a linear regression model. I then employed these regression results to predict budgets and staffing levels in the states for which I did not have actual data.

[4] These NYSE Regulation estimates come from press releases in early 2004. More recent NYSE Group annual reports indicated that the NYSE Regulation staff had grown to 745 by year-end 2005 and the merger of NYSE and Archipelago. As I could not find reliable estimates of 2005 budgets, I have employed the 2004 figures here. Current, NYSE Regulation budgets and staffing are, however, likely somewhat higher than those reported in the text.

Table Three

U.S. Securities Regulation Staffs and Budgets

(US Dollars)

	Budget	*Staff*
Securities & Exchange Comm'n	$917,650,000	3,865
State Agency Estimate*	$171,933,198	1,981
Subtotal	$1,089,583,198	5,846
NASD	$498,865,500	2087
NYSE Regulation	$150,000,000	650
Subtotal	$648,865,500	2,737
T otal	$1,738,448,698	8,583

* This estimate is based on several extrapolations.

c) Comparing U.S. and Canadian Budgets and Staffing Levels

The next step in our analysis is to compare the staffing levels between the two jurisdictions. Again, the task is not simple. In Canada, public oversight takes place at the provincial level, whereas U.S. public oversight is divided between federal and state authorities, with the lion's share of budgets and staffing being located at the SEC. Both countries make use of SRO supervision, but the structure of this supervision differs in each jurisdiction, with market oversight in Canada being pushed out into RS, whereas a major portion of U.S. market regulation remains inside the NYSE Group. Recognizing that there is no single correct method of comparing budget and staffing levels in Canada and the United States, I have attempted to construct a series of comparisons, which are summarized in Table 4. Across a number of dimensions, I present the ratio of U.S. regulatory intensity to Canadian regulatory intensive. First, consider the size of U.S. state regulatory agencies as compared to Canadian provincial authorities. These two groups are of roughly comparable size, with my estimate of total U.S. state budgets being 1.35 times the total Canadian provincial budgets and U.S. state staffing being some 1.91 higher than Canadian provincial staffing. Of course, once one factors in the SEC, the primary U.S. public oversight body, the scale of U.S. supervisory capacity moves far ahead of Canadian oversight: with ratios of 8.53 on budgets and 5.65 on staff. If one's focus is just on the NASD on the U.S. side, and the IDA and MFDA on the Canadian side, and they are added into the comparisons, the ratios move to 11.22 for budgets and 5.23 for

staffing. If one compares just the NYSE Regulation to RS, one sees ratios of 9.29 for budgets and 9.15 for staffing. Finally, if one adds together all public and SRO entities on both sides, the ratios go to 9.23 for budgets and 5.7 on staffing. Details of these ratios appear in Table 4.

Table Four
Comparisons of US & Canadian Staffing Levels

	Ratio of Budgets	*Ratio of Staffing*
US State Agencies to Canadian Provincial Agencies	1.35	1.91
Total US Public Agencies to Canadian Provincial Agencies	8.53	5.65
NASD to Canadian IDA and MFDA	11.22	5.23
NYSE Regulation to Canadian RS	9.29	9.15
Total US versus Total Canadian	9.23	5.70

Although the ratios presented in Table 4 are based on some rough estimates, I think they do present a crude estimate of the relative scale of regulatory oversight in the two jurisdictions. Comparing the U.S. state agency versus the Canadian provincial authority ratio, which is not particularly useful given the relatively small role that state regulators play in supervision in the United States, I would interpret Table 4 to suggest that U.S. supervisory budgets are in the range of 9 times larger than Canadian budgets, whereas staffing levels are in the range of 5 to 6 times larger. In the next section, I will discuss the implications of these differences in scale in light of the relative sizes of the U.S. and Canadian markets. But before turning to that larger question, I want to pause for a moment to consider the relatively higher ratios of budgets as compared to staffing.

The difference between U.S. and Canadian budgets is generally greater than the difference between U.S. and Canadian staffing levels. In other words, U.S. regulatory authorities are spending more per staff member than their Canadian counterparts. This differential would have been even more pronounced a few years ago when the U.S. dollar was stronger with respect to the Canadian dollar. In Table 5, I have presented estimates of budgets per staff by various categories. In only a comparison of U.S. state agencies versus Canadian provincial authorities is the budget per staff in Canada higher than the budget per staff in the U.S. counterpart. The differentials are fairly significant once SEC budgets and staffing are

added into the public agency comparisons. There are even greater differences in the budget per staff figures if one focuses on just the NASD versus the IDA and MFDA. Here, U.S. budgets per staff are more than twice as high as their Canadian counterparts. On the other hand, the budget per staff between the NYSE Regulation and RS seems roughly comparable.[5] Nevertheless, on average, regulatory budgets per staff members are over 60 per cent higher than those in Canada.

Table Five

Estimated Budget Per Staffing Level

(US Dollars)

	U.S. Cost	*Canadian Cost*	*Differential*
US State Agencies versus Canadian Provincial Agencies	$86,789	$123,308	70.38%
Total US Public Agencies Versus Canadian Provincial Agencies	$186,379	$123,308	151.15%
NASD versus IDA & MFDA	$239,035	$111,397	214.58%
NYSE Regulation versus RS	$230,769	$227,313	101.52%
Total US versus Total Canadian	$202,544	$125,054	161.97%

* Based on 5/23/06 Exchange Rate of 1.12211

The interpretation of budget per staff data is complicated, as there are differences in labour markets across jurisdictions and also in costs of living (particularly in major financial centers). These differentials can, however, be suggestive of differences in staff quality. These figures may also suggest differences within staff quality within regulatory departments. So, for example, the budget per staff of the SEC is a good deal higher than the budget per staff of U.S. state agencies, which accords with the prevailing wisdom that the quality of the SEC staff is higher than that of the state agencies. Going over the Canadian data presented in Table 5, one is struck by the lack of a differential between IDA and MFDA budgets per staff as compared with the budgets per staff of provincial authorities. In the United States., by contrast, the

[5] Additional investigation is needed to understand more fully the source of higher RS budgets per staff. According to agency experts, high IT costs may push up RS budgets per staff. In addition, RS personnel currently undertake on a contract basis certain supervisory functions for the Canadian exchanges that are not comparable to activities of the IDA or MFDA. Accordingly the differentials noted in the text should be regarded as preliminary findings, requiring additional investigation before policy conclusions are formulated.

NASD budget per staff is a good deal higher than the budget per staff of public agencies. On the other hand, the budget per staff of RS is roughly comparable to the budget per staff of the NYSE Regulation.[6]

d) Scaling U.S. and Canadian Markets

To evaluate the estimated differences between budgets and staffing levels in the United States and Canada, one must take into account the relative size of the two countries' economies. Again, no single measure captures all dimensions of scale, and I have assembled in Table 6 a number of potential measures. The first two, population and GDP, are gross measures of the scale, by which the United States appears to be 9.2 and 13.04 times bigger than Canada. (The latter figure would be somewhat lower if adjusted for current exchange rates.) Differentials in market capitalization (based on 2005 exchange rates) are roughly comparable with the United States being 11.46 or 12.03 times larger than Canada depending on which public companies are included in the measure.[7]

Table Six
The Relative Size of U.S. and Canadian Markets
(US Dollars)

	US	*Canada*	*Ratio*
Population (2003)	291,044,000	31,630,000	9.20
GDP (2003)	$10,881,609,000,000	$834,390,000,000	13.04
Market Capitalization (2005)			
Major Exchanges	$17,000,863,000,000	$1,483,658,000,000	11.46
All Public Companies*	$17,846,863,000,000	$1,483,658,000,000	12.03
Number of Listing Firms (2005)			
Major Exchanges	6,407	3,610	1.77
All Public Companies*	13,028	3,610	3.61
Without Dual Listed Firms (2005)			
Market Capitalization	$17,846,863,000,000	$617,293,000,000	28.91
All Public Companies*	13,028	3,393	3.84
Average Daily Turnover (2005)	$96,078,000,000	$2,678,000,000	26.78

* Including on US side, OTC Bulletin Board and PInk Sheets.

[6] See supra note 5.

[7] The market capitalization of a stock exchange is defined to be the total number of issued shares of domestic companies, including their several classes, multiplied by their respective prices at the end of the year. This figure reflects the comprehensive value of the market at that time. The measure does not include investment funds, various rights and options, or listed foreign shares. These figures are from the World Federation of Exchanges. See http://www.world-exchanges.org/

These gross measures of scale, which peg the U.S. market as at least 10 times larger than Canada, suggest that the crude measures presented earlier and derived from UK's FSA data from 2004 remain accurate. U.S. regulatory budgets and staffing are in the range of 5 to 9 times larger than Canadian budgets and staffing, but the U.S. market is more than 10 times greater. It therefore follows that Canadian regulatory budgets and staffing, when normalized for population, GDP, or market capitalization, will come out as more intensive than that of the United States.

One can, however, get a somewhat different perspective on these measures of relative intensity if one considers the ratio of listed firms in the two jurisdictions. As indicated in Table 6, the number of firms listed on the major U.S. exchanges is only 1.77 times the number of firms listed on the two major Canadian stock exchanges. Even if one expands the U.S. side of the ledger to include all public companies – perhaps a better point of comparison given the very small size of companies listed on the TSX Venture Exchange – the ratio only rises to 3.61 per cent. Using either of these measures as a method of normalization, Canadian regulatory budgets and staffing per listed firm would be lower than the comparable ratio in the United States.

Another potentially interesting benchmark is to exclude from the Canadian side all Canadian firms that are listed on U.S. exchanges, on the theory that Canadian authorities can free ride off of U.S. oversight. As the cross-listed Canadian companies tend to have relatively large market capitalizations, this adjustment has a more pronounced effect on the ratio of U.S. to Canadian market capitalization, moving the ratio up to 28.91. The ratio of all listed U.S. public companies to Canadian listed firms without cross-listings also increases to 3.84.

Finally, one might compare the trading volume of U.S. and Canadian securities markets. Here the ratios for 2005 jump to 26.78 per cent, reflecting the greater liquidity of U.S. markets as compared with Canadian markets.

e) Concluding Comments

Drawing back a bit from the foregoing analysis, let me conclude this section with some additional general assessments of the data presented. In answering the overarching question -- how large is the Canadian apparatus for overseeing securities markets as compared to the U.S. system? —the answer seems fairly clear. By the most plausible means of normalized comparison, the Canadian system appears to be larger than the U.S. system. To be sure, if one normalizes budgets and staffing for the number of listed

companies, U.S. budgets and staffing levels push ahead of Canada's to some degree, but the levels are fairly close.

Rather than agonizing further as to which method of comparison is the most salient, I think it is useful here to return to Figure 1 drawn from the FSA's data of 2004. A telling feature of this figure is not so much the relatively high intensity of securities oversight in Canada (and Australia) but the very low level of oversight in many other jurisdictions, especially in Germany and France. If one were to expand the analysis presented in this section to include not just Canada and the United States, the most striking result would not be the marginal differences in intensity between the North American jurisdictions, but rather the huge differentials between civil law jurisdictions and common law jurisdictions. In the greater scheme of things, what is truly noteworthy is the similarity between the regulatory intensities of securities market oversight between Canada and the United States, not their differences. And, again from a broader perspective, this similarity is not surprising given the proximity of the two jurisdictions, the coordinating effect of organizations such as the NASAA, and the history of regulatory collaboration exemplified by the MJDS.

Finally, to the extent that the foregoing analysis implies that Canadian authorities are over-regulating their securities as compared with their U.S. counterparts, I would emphasize that mechanisms of normalization present here do not incorporate any adjustments of economies for scale. Using back of the envelope calculations,[8] the observed differences in regulatory budgets and staffing are mostly consistent with quite plausible estimates of economies of scale in the delivery of financial services regulation. Certainly, this is the case when one considers budgets for public regulators or public regulators combined with the NASD and Canadian SROs. Accordingly, even though the evidence presented in these data suggests that Canadian regulation is more costly than U.S. regulation when normalized for general economic measures, such as GDP or market capitalization, I do not believe the data necessarily imply that Canadian regulatory is excessive as compared to the United States', if one were to make appropriate adjustments of scale economies. Rather, I think the clear message of the foregoing analysis is that Canadian budgets and staffing for capital market oversight are grossly comparable to those in the United States.

[8] In various other research efforts, I have attempted to estimate plausible ranges of economies of scale in securities market oversight. While I have yet to settle on a precise estimate and, indeed, the scale effects may not be uniform across market sizes, there is fairly strong evidence of some degree of scale effects in this area.

4. Enforcement Intensity

I now turn to the question of enforcement intensity, which is the frequency and severity with which a country's legal regime imposes sanctions on capital market participants. I am currently undertaking a research on this subject regarding U.S. enforcement activities, including both public enforcement efforts and private litigation. While much work remains to be done, my data on U.S. enforcement activities is, at this point, reasonably comprehensive, covering most sources of legal sanctions with data over a five-year time frame. The information that I have collected on Canadian enforcement activities is a good deal less complete. My Canadian information is mostly limited to public enforcement activities, although I have managed to collect some summary data on arbitration proceedings. I do not have any systematic data about private securities litigation or criminal sanctions in Canada, although I have conducted several interviews with knowledgeable practitioners and government officials on this aspect of Canadian enforcement. I summarize these interviews below.

The analysis in this section is organized as follows. First, I present the statistical data that I have collected on Canadian enforcement efforts. Next, I compare these data to comparable data from the United States, emphasizing the relative size of enforcement activity in Canada as compared to enforcement activity in the United States, differences in the relative importance of different regulatory bodies, that is public officials versus self-regulatory organizations, in both jurisdictions and, finally, differences in the allocation of enforcement activities with the jurisdiction of public authorities and SROs in Canada and the United States. I conclude with a short discussion of the areas of Canadian enforcement activity where I lack quantitative data, relying chiefly on interviews with practitioners.

a) An Overview of Enforcement Activities by Canadian Regulators and SROs

This section presents data on Canadian enforcement activities in the recent past. I focus on the quantitative information with particular attention on tracking levels of actions and the composition of the data over time. My analysis generally covers the years 2002 through 2004, although the data is less complete for the earlier years of this range and, in some instances, I include some data on 2005. To date, this analysis is limited to public enforcement actions initiated by provincial authorities, as compiled by the Canadian Securities Administrators,[9] and self-regulatory organizations such as the IDA, RS, and

[9] The Canadian Securities Administrators (CSA) coordinates regulatory issues for the 13 securities regulators of Canada's provinces and territories. See http://www.csa-acvm.ca/html_CSA/about.html

MFDA. Eventually, I hope to extend this analysis to include additional information on arbitration proceedings, civil litigation, and criminal sanctions in Canada. For current purposes, my analysis of civil litigation and criminal sanctions is limited to qualitative information drawn from a series of telephone interviews with Canadian practitioners.

In each area, my goal is to identify the number of formal sanctions imposed in each venue and to collect information on the total amount of monetary sanctions imposed on wrong-doers each year. To the extent possible, I have also attempted to develop data on the distribution of sanctions, by monetary amount, category of defendant, and type of violation. In concluding this section I present an assessment of the relative importance of each source of formal sanction within the Canadian regulatory structure. The data has been structured so as to make it as comparable as possible to a pre-existing database on U.S. securities enforcement activities. The comparisons with U.S. enforcement activity appear in the next section.

i. Canadian Provincial Authorities

The data presented below comes from enforcement reports published at the Canadian Securities Administrators home page, http://www.csa-acvm.ca/home.html. Since the organization first began furnishing enforcement statistics, on April 1, 2004, it had released three six-month reports by the time my data were compiled.[10] I have not been able to obtain data on provincial enforcement activity before this time. The CSA reports include settlements and decisions from multiple agencies. To avoid double-counting, I omitted data for agencies from which we had collected data independently. Thus, this section does not include CSA reports of IDA, MFDA, or RS decisions or settlements. CSA's handling of the data from these agencies did cause some concern: CSA only included a smattering of these agencies' actions, and they seemed to only include the highest-value actions. According to Ontario Securities Commission ("OSC") personnel, provincial authorities committed to make a comprehensive reporting of their enforcement actions in these filings. That said, other readers of a preliminary draft of this report expressed surprise at the relatively low level of actions reported by Quebec authorities. Accordingly, it is possible that the data reported below understate the enforcement activities of provincial authorities. It does, however, seem likely that the most important actions are included and so data regarding aggregate sanctions from provincial authorities should be reasonably accurate.

[10] Subsequently, a fourth report, covering Oct. 1, 2005, through Mar. 31, 2006, was released. Data from this fourth report are not included in my analysis, though I do allude to that report below.

Table Seven					
Provincial Authorities' Disciplinary Actions and Results					
	April 2004 to Sept. 2004 (Canadian Dollars)	Oct. 2004 to Mar. 2005 (Canadian Dollars)	April 2005 to Sept. 2005 (Canadian Dollars)	April 2004 to Sept. 2005 (Canadian Dollars)	Annualized Data in US Dollars
Number of Disciplinary Actions resolved	56	68	61	**185**	**123**
Firms Expelled (not including failure to pay a fine)	1	4	11	**16**	**11**
Firms Suspended	28	6	16	**50**	**33**
Individuals Barred	39	33	37	**109**	**73**
Individuals Suspended	5	15	15	**35**	**23**
Number of Fines	30	56	31	**117**	**78**
Amount of Fines levied	$2,400,055	$367,946,850	$3,648,339	**$373,995,244**	**$206,947,346**
Disgorgement	$360,000	$19,200,000	$1,474,622	**$21,034,622**	**$11,639,344**
Reimbursement for CSA costs	$633,751	$293,018	$391,500	**$1,318,269**	**$729,454**
Total Monetary Punishment (including reimbursement)	$3,393,806	$387,439,868	$5,514,461	**$396,348,135**	**$219,316,143**

As shown in the shaded column of Table 7, CSA reports that over the 18-month period beginning April 1, 2004, provincial securities regulators levied nearly Cdn$400 million in monetary punishment, of which over 94 per cent of this total punishment is due to fines. Some 63 per cent of actions resulting in discipline were given fines, while 109 individuals were barred in 86 actions; 16 firms were expelled in 11 actions. Fifty firms were suspended in some form in 26 actions, and provincial authorities suspended 35 individuals in 23 actions. While a roughly equal number of enforcement actions occurred in each six-month period, the severity of monetary penalties, particularly fines, was much higher in the second period than in the first and third periods, suggesting perhaps a spiking of enforcement intensity among provincial authorities in late 2004 and early 2005. The final column of Table 7 shows an annualized level of enforcement activities averaging the previous three columns and then converting monetary items into U.S. dollars at the 12/31/04 exchange rate. (In subsequent analyses, I present alternative annualized estimates using the lower levels of sanctions imposed in the first six-month period and in the third six-month period.)

Looking at the distribution of the actions across provinces (Table 8), we see that the majority of actions resulting in discipline concentrated in several provinces. Fifty-six per cent of such actions in Canada split evenly between Ontario and British Colombia. Add in Alberta and the percentage of total actions increases to 74 per cent. (Note: Some readers have questioned whether Quebec enforcement actions might not have been under-reported in this analysis.)

When it comes to the type of disposition that brings about a fine, disgorgement, costs imposed, or injunctive relief, Table 9 shows that the majority of the disciplinary actions end in settlement agreements.

Table Eight	
Number of Provincial Actions by Province	
Province	**Actions resulting in disciplinary action**
Ontario	51
British Columbia	52
Alberta	34
Manitoba	16
Québec	10
Nova Scotia	7
New Brunswick	6
Saskatchewan	4
Bureau de Décision et de Révision en Valeurs Mobiliéres	4
Joint actions	1

Table Nine	
Number of Actions by Type of Disposition	
Type of disposition	**Actions resulting in disciplinary action**
Settlement agreement	105
Regulatory tribunal decision	0
Court ruling	22
Appeal	4

As is true of disciplinary actions in the United States, the distribution of fines and disgorgement for provincial authorities is skewed towards smaller sanctions. Forty-two per cent of the fines were $10,000 or less. Thirty per cent of all fines were over $100,000. Meanwhile, the "middle" of the curve is pretty slim. As to disgorgement, there were very few orders made, reflecting the fact that only 3.4 per cent of the total monetary awards were made through disgorgement. While the accompanying graph reveals a relatively small number of large sanctions, the monetary significance of these sanctions is great. Indeed, one provincial actions --the one involving Franklin Templeton Investments and a number of other firms found to have been engaged in market timing activities- involved sanctions in excess of Cdn$200 million. This single action accounted for the bulk of the increase in monetary sanctions imposed by provincial authorities during the second six-month reporting period of CSA data. Without this action, enforcement sanctions would still have increased in the second period, but the spike would not have been nearly as dramatic.

ii. IDA Enforcement Actions

The data on IDA enforcement actions comes from individually published Disciplinary Bulletins, which report both settlements and administrative decisions and were downloaded individually from www.ida.ca/Enforcement/DisciplinaryBulletins_en.asp. The bulletins were generally comprehensive, but where we found information missing, we obtained supplemental information from the "Related Documents" link on the same page. Typically what was missing in the bulletins was information related to the type of party or violation; the outcome of the settlement, or decision that was always reported.

Table 10 reports our compiled data for IDA disciplinary actions. The number of actions resulting in discipline stayed steady for two years, then increased sharply in 2004, from 48 to 71. The number of fines stayed relatively consistent with the number of actions, except that a slightly higher proportion of actions ended in fines in 2004 as compared with 2002 and 2003, rising from 77 per cent to 88 per cent. Meanwhile, the total monetary punishment moves erratically over the three years, first dropping more than 50 per cent, then climbing by a factor of 14. The most striking feature of this data is the sharp upward movement of both the number of sanctions and the amount of monetary sanctions in 2004. As with the data on provincial enforcement actions, there seems to be a substantial upward movement in sanctions imposed. Also similar to the CSA data, the bulk of the increase in sanctions came from a small number of proceedings, two involving TD Waterhouse and Dominion Securities. Taken together, these two IDA actions accounted for nearly 80 per cent of the IDA's total monetary sanctions in 2004. Without

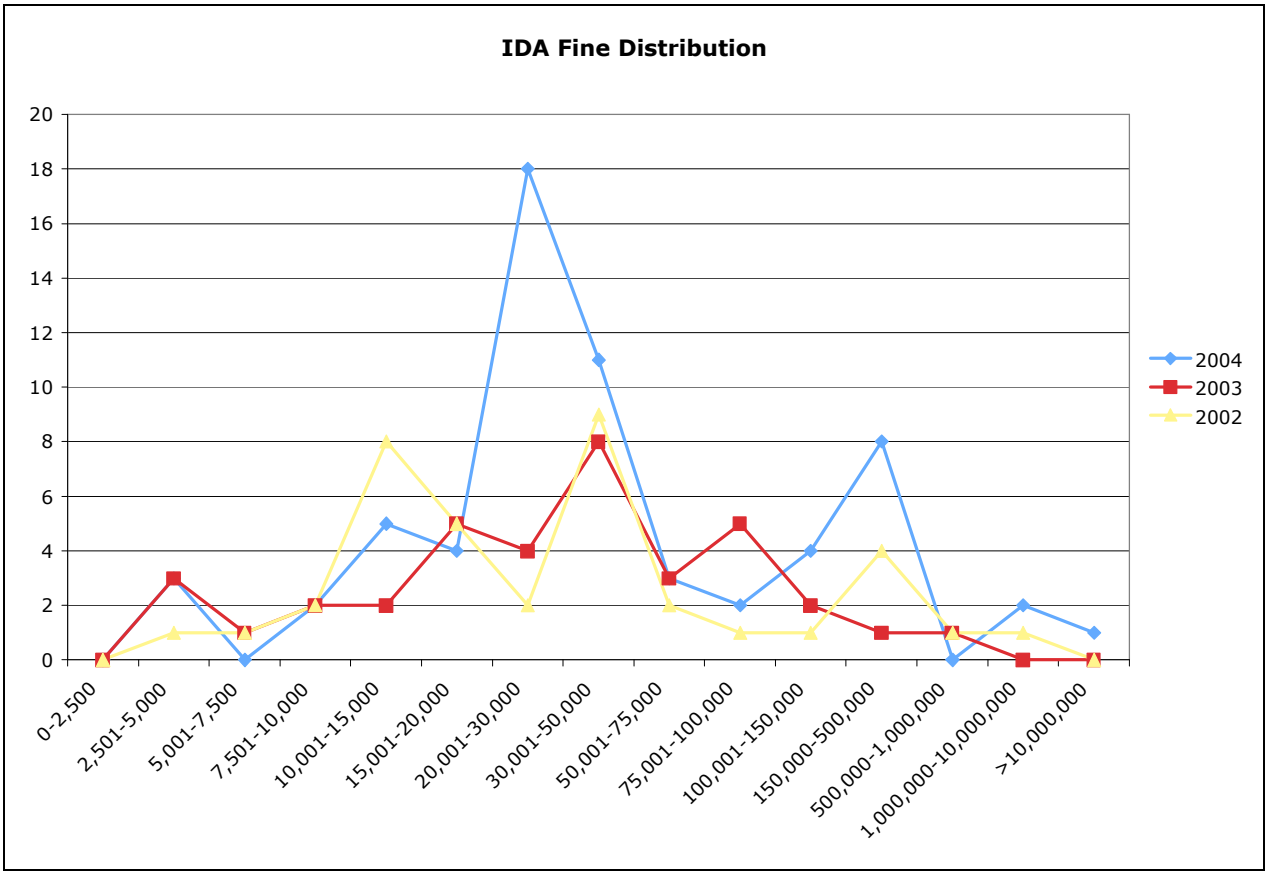
those actions, the IDA sanction level in 2004 would have been only modestly higher than in 2002 and 2003.

In terms of the nature of penalties, the data suggest that IDA more commonly suspends individuals rather than barring them permanently from practice. The number of individuals suspended is never less than one-and-a-half the number of those expelled. As to the monetary punishments, there also seems to be no strong trend, but there are several noteworthy features of the IDA data. First, for 2002 and 2003, the total disgorgement is less than 4 per cent of the total fines. In 2004, two massive disgorgements (again, the TD Waterhouse and Dominion Securities actions) drive the number up so that disgorgement is 78 per cent as large as fines. Removing those actions makes disgorgement 2.45 per cent as large as fines, a number more consistent with earlier years. (The IDA and most other Canadian enforcement agents usually order parties to reimburse the enforcer for costs. We have included these reimbursement amounts in "amount of fine.")

Table Ten				
IDA Disciplinary Actions and Results				
	2002	2003	2004	Average 2003-2004 in US Dollars
Number of Disciplinary Actions resolved	48	48	71	**56**
Firms Expelled (not including failure to pay a fine)	2	0	0	**1**
Firms Suspended	0	1	0	**0**
Individuals Barred	6	6	17	**10**
Individuals Suspended	24	12	27	**21**
Number of Fines	38	37	63	**46**
Amount of Fines levied	$5,841,500.00	$2,477,250.00	$24,787,822.97	**$9,159,632**
Disgorgement	$26,848.89	$78,395.76	$19,394,165.42	**$5,394,923**
Reimbursement for IDA costs	$607,379.00	$579,031.86	$3,166,630.85	**$1,204,361**
Total Monetary Punishment	$6,475,727.89	$3,134,677.62	$47,348,619.24	**$15,758,916**

Figure 4 shows how the concentration of IDA fines tends to centre around $20,000 to $75,000 values, with each year's distribution represented by a single line. Again, this tendency is more or less consistent over three years. It is interesting that the higher number of actions in 2004 did not result in fines evenly distributed across the range. Rather, as the chart shows, they clumped in the $20,000 to $50,000 range. This bunching of relatively higher sanctions explains some of the increase in total 2004 IDA sanctions (aside from the major actions against TD Waterhouse and Dominion Securities).

Figure 4



iii. Enforcement Data for Mutual Fund Dealers Association

All data for the MFDA come from the organization's enforcement page at www.mfda.ca/enforcement/hearingscomplete.html. Though the raw data seem to give a complete picture of MFDA's enforcement activity for the reporting years, the oldest action reported is from mid-2005. The data thus do not line up against the other agencies' data. Between mid-2005 and early 2006, the MFDA ordered 12 fines in 12 cases against 13 securities violators, all brokers. Half the violations were business conduct violations, and one quarter was market misbehaviour violations. The rest, slightly more than one quarter of the violations, were for miscellaneous violations. No firms were suspended or expelled. While nine individuals were barred, only one was suspended. Disgorgement made up less than one quarter of total money payments ordered. And compared to fines and disgorgement ordered, costs due for reimbursement were low: only 1 per cent total pay-outs ordered.

Table Eleven		
MFDA Disciplinary Actions and Results		
	2005-2006 Data Canadian Dollars	*Annualized Data US Dollars*
Number of Disciplinary Actions resolved	12	12
Firms Expelled (not including failure to pay a fine)	0	0
Firms Suspended	0	0
Individuals Barred	9	9
Individuals Suspended	1	1
Number of Fines	12	12
Amount of Fines levied	$8,505,000	$7,059,263
Disgorgement	$2,650,000	$2,199,535
Reimbursement for CSA costs	$119,500	$99,187
Total Monetary Punishment (not including reimbursement)	$11,274,500	$9,357,985

iv. Enforcement Data for Market Regulation Services, Inc (RS)

The data presented are from data submitted through email by Doug Harris, RS Director of Policy, Research and Strategy. For the most part, the data appear to be comprehensive, although they do not include any injunctive relief, rather only fines, disgorgement, and cost reimbursement.

Table Twelve RS Disciplinary Actions and Results				
	2002 Canadian Dollars	*2003 Canadian Dollars*	*2004 Canadian Dollars*	*Annualized US Dollars*
Number of Disciplinary Actions resolved	14	20	20	18
Number of Fines	13	18	14	15
Persons expelled	0	0	1	0
Persons suspended	0	5	0	2
Amount of Fines levied	$205,500.00	$736,215.67	$4,962,220.00	$1,633,448
Disgorgement	$26,848.89	$43,997.59	$29,925.00	$27,881
Reimbursement for FS costs	$39,300.00	$189,500.00	$434,000.00	$183,378
Total Monetary Punishment	$271,648.89	$969,713.26	$5,426,145.00	$1,844,706

Table 12 shows summary data for RS. Throughout the period, the number of annual reactions remains roughly constant, rising from 14 in 2002 to 20 in both 2003 and 2004. The big change comes in the level of monetary sanctions. The total amount of fines and costs assessed against violators increased 240 per cent fold from 2002 to 2003, and then spike up even more in 2004 when sanctions were 18 times greater than that in 2002. Meanwhile, disgorgement first increased 64 per cent from 2002 to 2003, and then dropped 32 per cent in 2004. On balance, particularly if one focuses on total sanctions imposed, the intensity of RS enforcement actions seems to have increased between 2002 and 2004, consistent with the increases found in the CSA and IDA data.

v. Overview of Public Securities Enforcement in Canada

In this subsection, I attempt to pull together all foregoing data on public enforcement actions in Canadian securities markets. My results are summarized in Table 13, and include both information on the number of enforcement actions and the level of monetary sanctions for each agency. The first two columns of

data present annualized data, averaging all years for which information is reported above.[11] Because there may be substantial changes in the level of enforcement intensity over the period of observation, I also included annualized monetary sanctions for the first period in which data is available and the last. Admittedly, there is a bit of apples to oranges quality in this presentation as the first periods are not the same for each agency; but the approach is, I hope, useful in highlighting trends. Monetary sanctions are expressed in terms of U.S. dollars, using the 12/31/04 exchange rate.

Table Thirteen

Summary of Canadian Enforcement Actions

	Actions		**Monetary Sanctions**					
	Number of Enforcement Actions		*Annualized Data (US Dollars)*		*Annualized Last Period (US Dollars)*		*Annualized First Period (US Dollars)*	
Agency	*(annualized)*	*Percentage*		*Percentage*		*Percentage*		*Percentage*
Provincial Authorities*	124	59.0%	$219,316,143	89.1%	$9,154,152	14.7%	$5,633,807	27.4%
IDA	56	26.7%	$15,758,916	6.4%	$39,299,983	63.1%	$5,374,940	26.1%
MFDA * **	12	5.7%	$9,357,985	3.8%	$9,357,985	15.0%	$9,357,985	45.4%
Subtotal	68	32.4%	$25,116,900	10.2%	$48,657,967	78.1%	$14,732,925	71.5%
RS	18	8.6%	$1,844,706	0.7%	$4,503,772	7.2%	$225,472	1.1%
Total	210	100.0%	$246,277,750	100.0%	$62,315,892	100.0%	$20,592,204	100.0%

* Data from 2004-2005. ** MFDA data is available for only a single period.

Focusing first on the number of actions, Canadian provincial authorities accounted for nearly 60 per cent of all formal enforcement actions in Canada, with the IDA (26.7 per cent) being the next most important source of enforcement actions, and RS, the third (8.6 per cent). If we look over to annualized monetary sanctions, the rank orderings shift somewhat, with MFDA edging out RS for third place in sanctions imposed. But the most striking feature of the table is the dominance of provincial authorities in terms of sanctions imposed (some 89.1 per cent of the total). What this table suggests to me is that while enforcement authority is decentralized in Canada, by far the largest stick remains in the hands of provincial authorities. Not only is this true in the aggregate, but it is true if one examines the size of the very largest penalties that provincial authorities impose, as compared with the Canadian SROs.

If one shifts over to the last period" and "first period" annualized data on monetary sanctions presented in Table 13, some interesting nuances emerge. If one focused only the first period for which data is available, 2002 for IDA data and mid-2004 for provincial authorities, the total level of sanctions imposed

[11] As noted in the table, for CSA and MFDA data, the period of coverage is 2004-2005, whereas for the IDA and RS, the period is from 2002 to 2004.

in Canada was only a fraction of the average sanction level for the full period, only US$20.6 million in the first period versus nearly US$250 million annualized sanction level for all periods. In addition, during the first period columns, the total amount of IDA sanctions was roughly equal to that of all provincial authorities. So, the preeminence of provincial enforcement actions seen in the overall data does not appear to be present in the first period analysis. Moreover, if one looks to the last period analysis, the relative importance of provincial enforcement actions again drops down and through this lens, at least, the SROs emerge as the dominant forces of regulatory sanctioning in Canada. One should, I think, not be too quick to conclusion that SROs have actually eclipsed provincial authorities as the primary source of capital market oversight in Canada. The misalignment of periods of observation may be skewing this data. The CSA data runs into 2005 when enforcement activity may be dropping off for all authorities, whereas the SRO data, at least for the IDA and RS, end in 2004, which may be a high-water mark for all agencies. Accordingly, I think the lessons that one can draw from Table 13 are a bit more modest. First and most clearly, there has been a fair amount of volatility in Canadian sanctioning practices in the past few years. Quite clearly, the level of enforcement activity has been on an upward trend. While the very high levels of sanction observed in 2004 dominate the analysis presented in this study, the rate of increase, perhaps a 10-fold increase in sanctioning, may not reflect long-term trends. The three-fold increase between the first period and the last period analysis shown in Table 13 (total sanctions of US$62 million as compared with US$20 million) may be more plausible indicators of long term trends.[12]

In the course of my investigations, I came across a number of different explanations as to why the level of enforcement activities in Canada has risen over the past few years. These include investor losses as a result of stock market reversals in 2000 and beyond; heightened enforcement activity in the United States following the passage of the Sarbanes-Oxley Act of 2002; and criticisms of enforcement efforts leveled against provincial authorities in the Wise Persons Committee Report of 2003. All of these explanations are consistent with the data, which shows a spike of enforcement activity in 2004 and early 2005. The origin of these explanations, all arising out of events in the early years of this decade, would also be consistent with a decline in enforcement intensity over time. The data shows a falling-off of provincial enforcement agents towards the end of 2005 and beyond; anecdotal evidence suggests some further drop-

[12] It is extremely difficult to make confident predictions about long-term trends in this area. The most recent CSA data, mentioned above in note 10, suggest that provincial authorities have not returned to the very high levels of sanctioning seen in late 2004 and early 2005. Informal conversations with SRO authorities suggest also that their average rate of sanctioning may decline somewhat from earlier highs. Further research into actual practices would be important to gain a fuller picture of the longer-term trends.

off of SRO actions, though I have not seen any data on more recent SRO enforcement actions.

While data limitations make it difficult for me to be fully confident of the foregoing analysis of aggregate trends, I do think that there is strong evidence that the overall level of enforcement intensity has risen in Canada over the past few years. Much of the movement appears to have occurred at the level of provincial authorities, although the SROs have also increased their enforcement intensity too. As the SRO data end in either 2004 or mid-2005, I cannot determine whether the increases in enforcement intensity during this period have been maintained or whether the level of enforcement intensity has retreated in the past 18 months. As explained below, this variation in the level of Canadian enforcement intensity makes it somewhat difficult to compare Canadian and U.S. enforcement activity.

b) Comparing U.S. and Canadian Enforcement Intensity

I now turn to the enforcement of securities laws in the United States and attempt to compare enforcement intensity in the two jurisdictions. As noted earlier, I am currently engaged in an extensive study of U.S. enforcement activity. The information presented in this section are drawn from that research. I include both public enforcement actions, of the sort compiled above for Canada, and also private enforcement activity, including class action litigation and arbitration proceedings for both the NASD and NYSE. (My NYSE arbitration data do not include monetary sanctions.) In my opinion, the quality of my U.S. data is relatively high, certainly higher than that of my Canadian data. I have had more time to develop this information and also most of that data are drawn from a full three-year period. The one element of my U.S. data is that the information is suspect regarding U.S. state regulators. Only a limited amount of information is available on this subject, drawn chiefly from a confidential study undertaken by the NASA for 2001 and 2002. That study did not cover all the states and the information was reported only at an aggregate level. Because no better source of information on this subject was available, I have had to rely on this NASAA study to extrapolate estimates of state-level regulation. To the extent that the period covered in the study was atypical in some respect, this aspect of my data may be incomplete. On balance, I think my data presented on U.S. enforcement activity is a reasonable estimate of the true level of enforcement intensity in the jurisdiction.

i. Overview of U.S. Securities Enforcement Activity and Some Preliminary Observations

I begin in Table 14 with an overview of U.S. enforcement activity. Like Table 13 for Canada, I include information on both enforcement actions and monetary sanctions. With respect to monetary sanctions, I include both annual averages for 2002 through 2004 as well as the 2004 data (which includes wholly extrapolated estimates for state agencies). Although Table 14includes information on private actions, that is, both litigation and arbitration, my discussion in this subsection will be limited only to public enforcement activity. Accordingly, when I speak in terms of percentages, readers should refer to the columns marked as "Percentage of Total Public Actions" and not the columns entitled "Percentage of Grand Total," which also include private actions.

Table Fourteen
Summary of US Enforcement Actions in Securities Regulations

	Actions			Monetary Sanctions				
	Annualized Data: 2002-2004			*Annualized Data:2002-2004 (US Dollars)*			*2004 Data (US Dollars)*	
	Average Number Enforcenment Actions	*Percentage of Grand Total*	*Percentage of Total Public Actions*	*Total Monetary Sanctions*	*Percentage of Grand Total*	*Percentage of Total Public Actions*	*Total Monetary Sanctions*	*Percentage of Grand Total*
Public Actions:								
SEC	639	9.7%	17.6%	$2,164,666,667	24.6%	40.9%	$3,100,000,000	29.8%
DOJ	112	1.7%	3.1%	$766,525,000	8.7%	14.5%	$16,850,000	0.2%
State Agencies (estimated)	1,482	22.6%	40.8%	$1,114,949,985	12.7%	21.1%	$931,212,489	9.0%
Subtotal	2,233	34.1%	61.5%	$4,046,141,652	46.1%	76.5%	$4,048,062,489	39.0%
NASD	1,170	17.9%	32.2%	$1,078,282,572	12.3%	20.4%	$232,024,058	2.2%
NYSE	227	3.5%	6.3%	$163,059,260	1.9%	3.1%	$464,834,281	4.5%
Subtotal	1,397	21.3%	38.5%	$1,241,341,833	14.1%	23.5%	$696,858,339	6.7%
Total Public Actions	3,630	55.4%	100.0%	$5,287,483,485	60.2%	100.0%	$4,744,920,828	45.7%
Private Actions:								
Class Actions	210	3.2%	n.a.	$3,336,333,333	38.0%	n.a.	$5,456,000,000	52.5%
NASD Arbitrations	1,720	26.2%	n.a.	$162,333,333	1.8%	n.a.	$186,000,000	1.8%
NYSE Arbitrations	994	15.2%	n.a.	missing	n.a.	n.a.	missing	n.a.
Total Private Actions	2,924	44.6%	n.a.	$3,498,666,667	39.8%	n.a.	$5,642,000,000	54.3%
Grand Total -- Private & Public	6,554	100.0%	n.a.	$8,786,150,151	100.0%	n.a.	$10,386,920,828	100.0%
Adjusted Grand Total*	n.a.	n.a.	n.a.	$8,176,733,485	93.1%	n.a.	$8,616,920,828	83.0%

* Adjusted to deduct sanctions reported under two or more agencies.

Starting with actions imposed, an interesting place to begin is the distribution of public actions between government agencies (SEC, DOJ, and state agencies) with 61.5 of public actions and the balance (or 38.5 per cent) with our two major SROs, the NASD and NYSE. This allocation is quite similar to the Canadian distribution of average annual actions between provincial authorities and SROs. The major difference is that government enforcement is distributed between both federal authorities (most importantly the SEC) and state agencies in the United States. Also, like Canada, the dealers association (NASD) brings many more actions than our principal market-oversight SRO, which is the NYSE.

On the monetary sanction side, there is also a rough comparability between the U.S. and Canadian enforcement patterns. As in Canada, the most important public enforcement agencies are government agencies, which together accounted for more than three quarters of average annualized monetary sanctions during the 2002-2004 period and over 85 per cent in 2004. Over the longer period, the NASD is the next most important source of public monetary sanctions, averaging more than US$1 billion of penalties a year or more than one-fifth of total public sanctions. In 2004, however, the NYSE increased its relative importance in monetary sanctions, though it is not clear whether this rise was episodic or permanent as controversies over specialist practices and other well-publicized problems at the Exchange may have prompted NYSE officials to increase enforcement activity in recent years. While the SEC emerges in all presentations as the major source of public sanctions in U.S. capital markets, the states retain a substantial role assuming, of course, that my extrapolations of state data are accurate.

Another interesting point of comparison between the U.S. data presented here and the Canadian data presented earlier is the absence of strong upward trend lines. While the level of SEC monetary sanctions is higher in 2004 than the 2002-2004 average, NASD sanctions seem to have come down a bit as has the DOJ activity. Aggregate public monetary sanctions in 2004 of US$4.7 billion are roughly the same as those for the period average, that is, US$5.2 billion. While there was, undoubtedly, an upward swing in U.S. enforcement activity between the late 1990s and 2002,[13] the rise in sanctions seems to have plateau'd in the United States and may have even started to subside.[14] In contrast, it seems that the trend in the overall level of enforcement activity in Canada was still moving upward in 2004.

ii. Comparing the Overall Scale of Public Enforcement Activity Between Canada and the United States

I next consider the overall scale of public enforcement activity in the United States and Canada. This again returns us to the question of how to factor in the quite different sizes of U.S. and Canadian capital

[13] So, for example, average SEC monetary sanctions during 1999 to 2001 was US$617 million as opposed to US$2.2 billion during 2002 to 2004, almost a four-fold increase. While substantial, this pales in comparison to the growth rate of Canadian public sanctions in recent years. Of course, as mentioned in the text, Canadian growth is driven by a very small number of actions, while the increase in U.S. sanctions has been more broadly based.

[14] This subsidence is even more pronounced when one adjusts enforcement actions for the double-counting that occurs when two agencies report the same settlement. Table 14 corrects for this effect in the last row. As there was more double counting in 2004 than during the 2002–2004 period, the real decline in public sanctions at the end of the period was more pronounced than reported in the text. One further source of double-counting that may still affect some of my U.S. data arises when regulators report the same enforcement action at several times, for example, each time a party settles or each time the sanction is upheld on appeal.

markets. I will not repeat the analysis here, but in section 3, I reviewed a number of different metrics for evaluating the ratio of budgets and staffing levels between the two jurisdictions and concluded that U.S. supervisory budgets are in the range of 9 times larger than Canadian budgets, whereas staffing levels are in the range of 5 to 6 times larger. (See supra Table4.) I also noted that U.S. capital markets, by most plausible measures, are a larger multiple of Canadian markets if compared on the basis of market capitalization (on the order of 11 or 12 times), even more if measured by trading volume (perhaps 28 times) but not as large a multiple if measured by number of listed companies (only 2 or 4 times). See supra Table 6.

Unfortunately, it is not entirely clear how to apply all of these ratios in comparing Canadian to U.S. enforcement activities. If one wants to ask the question, "Are Canadian regulatory personnel as efficient in bringing enforcement actions as their U.S. counterparts?", one might focus on the ratio of Canadian budgets and staffing to U.S. budgets and staffing to see whether Canadian regulators achieve the same relative number of enforcement actions and sanctions as their U.S. counterparts. This approach would imply that Canadian officials should be expected to bring one action for every 5 to 9 U.S. actions. On the other hand, if one thought the right question to ask is whether Canadian authorities are bringing as many actions as U.S. regulators per billion dollars of market capitalization or annual turnover, one might focus on those ratios, suggesting that Canadians might only need to impose Cdn$1 dollar of sanction for every US$11 to US$30 dollars imposed in the United States. Or if one thought that enforcement activity enjoys some sort of economies of scale because, arguably, many potential violators learn from the instigation of a single action, one might think that regulators with smaller markets (like Canada) should bring proportionately more actions than regulators from larger jurisdictions and a ratio of one to 11 or 12 would be too high. Or one might ask the question in terms of listed companies, perhaps the ratio of U.S. to Canadian enforcement actions should be more in the range of about three to one to be roughly equivalent.[15]

While the absence of any strong theoretical structures for comparing regulatory intensity is unfortunate, I think the suggested ratios with a wide breadth but a center of gravity in the area of 10 to 1 as a plausible starting point is helpful, particularly when one looks at the data presented in Table 15. In this table, I

[15] Another perspective, suggested by a Canadian regulatory official who reviewed an early draft of this paper, would be on the relative size of market participants in the United States as compared with Canadian market participants. To the extent that U.S. securities firms are much bigger than their Canadian counterparts, one might think that U.S. sanction levels should be correspondingly higher. While I have not collected data on size of market participant, one might use the ratio of trading volumes, approximately 27 to 1, as a proxy for the size of market participants.

have calculated the ratios of actions and monetary sanctions on a variety of dimensions. As before, I start with the number of actions brought by various public agencies in both jurisdictions. First, I compare the ratio of average SEC actions to average provincial actions (5.2 to 1) and then add in ratios that include other U.S. government authorities, most notably the states. With all of these other U.S. government agencies included, the ratio of U.S. actions to Canadian actions jumps to 18 to 1, a good deal above the modal ratio of comparison (10 to 1) suggested above. The relatively high ratio of U.S. to Canadian enforcement actions is consistent with the common understanding that companies are a good deal more likely to be subject to enforcement actions in the United States than in Canada and the differential would still exist if we normalized for market capitalization (but not for trading volume). It also suggests that U.S. regulatory officials, on a per person or per budget dollar, are more enforcement-oriented than their Canadian counterparts. And comparable ratios exist for SRO enforcement actions, where I compare the NASD to the IDA and MFDA (17.2 to 1) and the RS to NYSE Regulation (12.6 to 1).

The ratios of monetary sanctions presented in Table 15 present a more complicated picture. Start with the column comparing the annualized first period of Canadian data with SEC averages. Here the ratios of monetary sanctions between the two jurisdictions are huge, with orders of magnitude larger than other benchmarks. The SEC alone imposed 384 times as many sanctions as Canadian provincial authorities by this measure, and total sanctions from U.S. governmental agencies were 718 times as large as provincial sanctions. Although one would need to do more work to draw firm conclusions here, my interpretation of this column is that it represents the old way of doing things in Canada when enforcement activity was very, very light, compared to U.S. enforcement practices.[16] The differences in enforcement activity by this measure are particularly striking when one recalls the relatively heavier degree of regulatory staffing in Canada as compared to the United States. Even with relatively robust regulatory staffing, Canadian authorities were bringing only a small fraction of U.S. enforcement actions, measured in terms of sanctions imposed.

[16] Even if one compares first period Canadian sanctions to pre-2002 U.S. enforcement levels (see supra note 9), the differential will still be very large.

Table Fifteen

Ratios of US and Canadian Public Actions and Monetary Sanctions

	Actions	Monetary Sanctions		
	Ratio of US to Canada for Annualized First Period to US 2002-2004 Average	*Ratio of US to Canada for Annualized First Period to US 2002-2004 Average*	*Ratio of US to Canada for Annualized Data (Full) to US 2002-2004 Average*	*Ratio of US to Canada for Annualized Last Period to US 2004 Data*
Provincial Agencies:				
to SEC	5.2	384.2	9.9	338.6
to SEC & DOJ	6.1	520.3	13.4	340.5
to SEC, DOJ & States	18.0	718.2	18.4	442.2
IDA & MFA				
to NASD	17.2	73.2	42.9	4.8
RS				
to NYSE	12.6	723.2	88.4	103.2
IDA, MFA & RS				
to NASD & NYSE	16.2	83.0	46.0	13.1
Total Canadian Public Agencies				
to Total US Public Agencies	17.3	256.8	21.5	76.1
Adjusted Total Canadian Public Agencies				
to Total US Public Agencies	n.a.	227.2	19.0	47.7

What's particularly interesting about Table 15 is how these ratios have changed over the period of analysis. Look first at the third column of data, which compares the full period of Canadian data to 2002-2004 U.S. data. While Canadian enforcement activity is still less intensive than the benchmark 10:1 ratio suggested above, provincial authorities were imposing sanctions in this period that had a ratio of 18.1:1 to U.S. governmental agencies, arguably in the same general ballpark of U.S. governmental sanctions. Canadian SROs had also showed substantial increases relative to their U.S. counterparts. In the last period analysis, provincial authorities have dropped back down, though not as low as they had been in the first period, whereas SROs show further improvement. (The different end points of Canadian provincial authorities and SROs likely reflect different time periods of analysis, with the last period provincial authority data coming from 2005 whereas the last period SRO data come from 2004.)

While Table 15 reveals some interesting and potentially important trends, I should hasten to emphasize that one should not interpret the developments as suggesting that Canadian enforcement activity even at the height of enforcement intensity in 2004 was then comparable to U.S. enforcement activity. To begin with, the estimates are extrapolated from a very small period of time and may not persist. Moreover, as explained below, there are a number of reasons to question the deterrent effect of recent Canadian enforcement activity, particularly its reliance on large sanctions in a very small number of cases. Moreover, the data presented in Table 15 are limited to public sanctions and do not include either civil litigation or criminal sanctions, areas in which U.S. enforcement activity substantially exceeds Canada. Still, the data in Table 15 suggest that changes are afoot in Canadian enforcement activity and the trend is worthy of further study.

iii. Other Observed Differences in Public Enforcement Strategies

In the course of my work on this study, I noticed a number of other differences in Canadian and U.S. enforcement strategies, some of which may be relevant to the work of the Task Force and their interpretation of the data presented in this paper.

The first difference concerns potential differences in the meaning of monetary sanctions. In the course of a telephone interview with an official from the Ontario Securities Commission (OSC), I was informed that Canadian authorities will not accept settlements involving monetary sanctions unless the agency is assured that the fine will actually be paid. Thus, for example, a bond might be required or the monetary sanction must be paid into an escrow account of some sort. According to this same official, U.S. regulators routinely announce fines that are not ultimately collected. The implication of this comment is that the levels of monetary sanctions in Canada may have a greater impact on private parties than comparable levels of sanctions in the United States. I have not attempted to verify the accuracy of this claim, although I did raise the issue with several other interviewees. At least one lawyer, who represents private parties in enforcement actions, agreed that provincial authorities do require assurances of payments before accepting settlements in enforcement actions but indicated as well that the policy was not always followed with respect to individual defendants (as opposed to corporate defendants) and that the IDA and other SROs did not follow similar policies. The same private practitioner did, however, note that, unlike U.S. authorities, Canadian officials generally required private parties to admit violations of law as part of settlement actions.[17] According to the practitioner, this requirement could potentially expose parties to Canadian settlements to civil liability in a way that does not threaten parties to U.S. settlements.[18] Again, I did not explore this issue in detail, but it introduces another dimension on which sanctions in Canada may differ from sanctions in the United States.

Another interesting dimension of comparison between Canadian and U.S. enforcement authorities pertains to the differences in the kinds of cases various agencies choose to proceed. While there is a general similarity between the cases of the U.S. SROs --that is, the NASD and NYSE and their Canadian counterparts, which are the IDA and RS, government agencies in the two jurisdictions do seem to be

[17] Interestingly, the practitioner emphasized the risk that Canadian settlements with admission of fault could create liability in U.S. litigation. It is unclear as to which jurisdiction one should assign such deterrent effects.

[18] While a theoretical concern, I suppose, the limited amount of civil litigation in Canada would lead me to doubt whether this difference is substantial in terms of overall deterrence. Indeed, there is fairly compelling evidence that public enforcement activity by the SEC is apt to stimulate private litigation in the United States notwithstanding the capacity of settling parties to avoid admissions of violations of law in SEC settlements. See James D. Cox et al., SEC Enforcement Heuristics: An Empirical Inquiry, 53 Duke Law Journal 737 (2004).

emphasizing different kinds of cases. I have reproduced below two different figures drawn from my work on SEC enforcement actions. The first, labelled as Figure 5, shows trends in the kind of SEC enforcement actions based on types of violations. The key point to note here is that much of the SEC's activities is focused on issuer-related actions: either actions related to offerings or related to issuer misstatements in financial reports. The second chart, focusing on the targets of SEC actions in 2004, conveys a similar message. The most frequent target of SEC actions is an issuer for some kind of misstatement.

Next, I present a comparable chart (Figure 7) for actions of the Canadian provincial authorities, presenting the full 18 months of data available on the CSA website. While Canadian authorities also bring actions against issuers, their enforcement activities are much more widely distributed than the SEC's and much more of their time is spent on market related activities, either market manipulation cases or broker-dealer misconduct. From this preliminary analysis, it seems that provincial authorities in Canada have a greater degree of overlap with SRO enforcement action compared to the SEC and U.S. self-regulatory organizations.[19] The NASD and NYSE Regulation specialize in broker-dealer oversight, where the SEC focuses on issuers. While I have not had the opportunity to pursue this issue further, one hypothesis is that the relatively lower level of enforcement activity of Canadian SROs has caused provincial authorities to maintain a wider regulatory agenda than the SEC, which has been able to focus the lion's share of its enforcement activities on corporate issuers. Whatever the cause of this difference in allocation of enforcement resources, it means that gross comparisons between Canadian and U.S. levels of enforcement intensity may be masking important information about the distribution of enforcement efforts.

[19] In reviewing a preliminary draft of this report, a representative of provincial authorities took issue with my characterization of these differences. The official suggested that provincial authorities are engaging in appropriate oversight of Canadian issuers, but that their investigations sometimes lead them to bring enforcement actions against broker-dealers. The official also disagreed with my speculation that there may be some overlap in the enforcement activities of provincial authorities and SRO's in Canada.

Figure 5

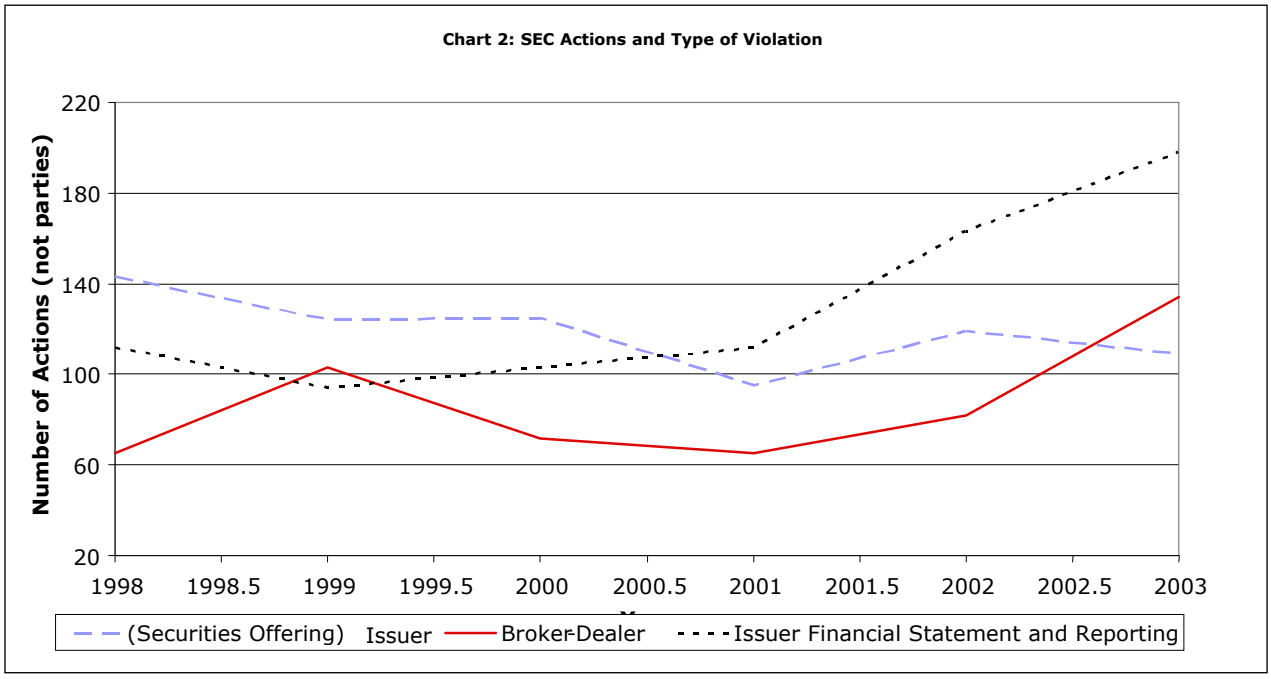


Figure 6

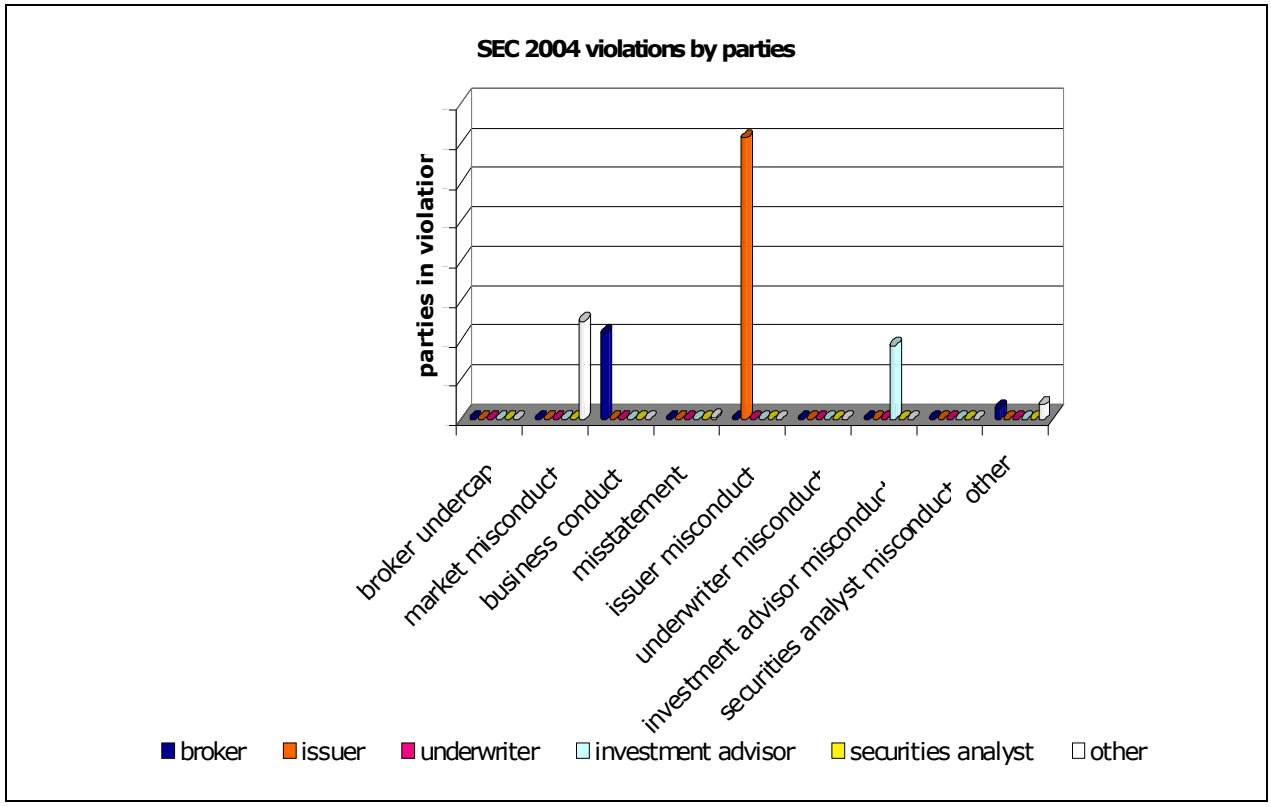
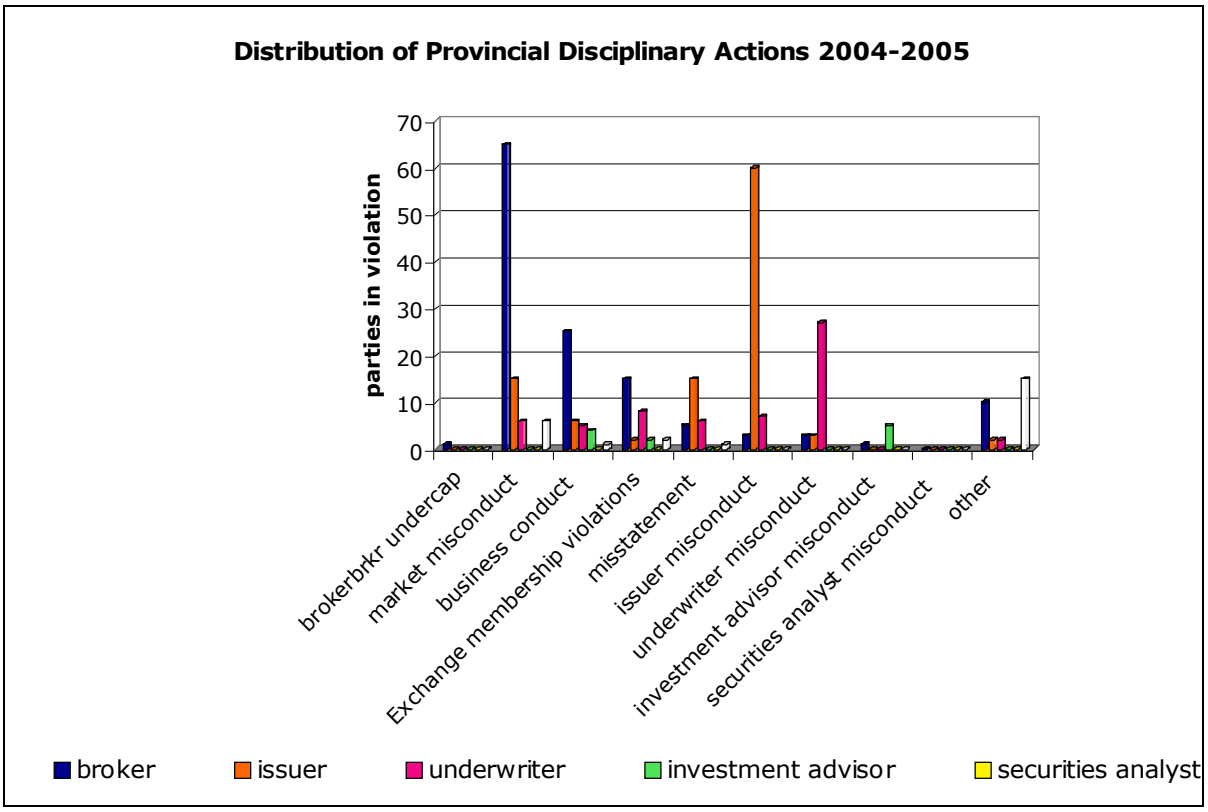


Figure 7

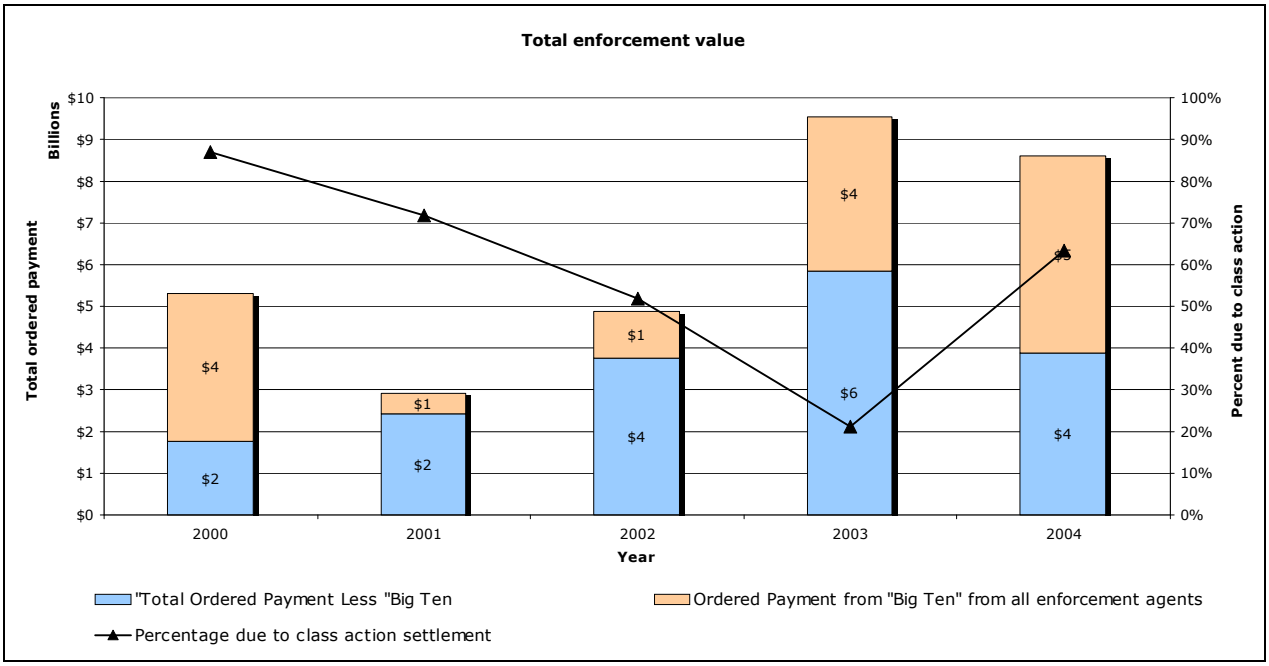


A final point of comparison concerns the role of large cases in the two jurisdictions. As recounted above, a large fraction of monetary sanctions for Canadian provincial authorities and the IDA in recent years has come from a handful of cases. Indeed, these cases, which represent 1 per cent or two of enforcement activity, contribute between two-thirds and four-fifths of monetary sanctions in recent years. While the intensity of the remaining enforcement activity of both provincial authorities and the IDA has also increased, the picture that emerges in Canada is one in which much of the enforcement punch is coming from a very small number of cases.

In the United States, big cases are important, too, and high profile public enforcement actions, concerning the analysts' conflict and other major cases such as Worldcom and Enron, have dominated the headlines. But the overall role of big cases is not as large in the United States as it has become in Canada. Again, data from my ongoing research into U.S. enforcement activity is instructive. The following chart presents data on all enforcement activity in the United States (public and private) over a multi-year period. The chart distinguishes monetary sanctions from the "top ten" awards from each area and the monetary sanctions from other actions. While big awards are important, so, too, is the collective impact of the remaining activities. Looking closely at the data, one might reasonably conclude that, in most years, the

total monetary effect of the smaller cases in the United States equals or outweighs the effect of the bigger cases.

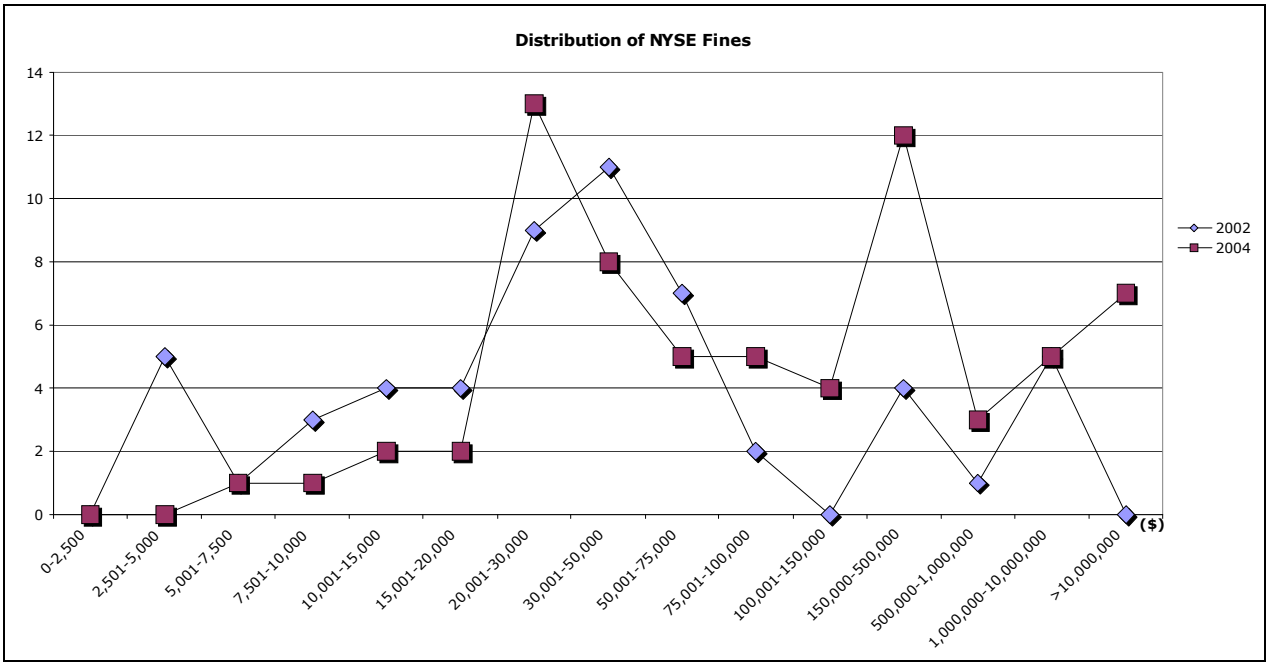
Figure 8



As is true of much of the data presented in this paper, one cannot be sure what to make of this additional distinction between U.S. and Canadian enforcement activity. To me, it seems to suggest that the enforcement impact of recent Canadian efforts, though the size of several actions pushes up the country's aggregate sanctions, may have less deterrent effect than more evenly distributed sanctions, with more of the penalties coming from a larger number of enforcement actions. Such a broader distribution of sanctions increases the likelihood that any particular firm will be subject to an enforcement action. Moreover, since only a handful of actions make up such a large share of the overall Canadian enforcement effort, the possibility that authorities may not bring similar actions in future years may serve to loosen their deterrent effect going forward. In contrast, in the United States, a multi-year commitment to a large number of reasonable serious monetary sanctions seems like a more credible commitment to ongoing enforcement activity, even if the importance of large cases falls off.

Another way to make a similar point is to consider the distribution of sanctions from the SROs in the United States as compared with their counterparts in Canada. I have reproduced below a chart of the distribution of NYSE sanctions for 2002 and 2004. The percentage of NYSE sanctions, which is approximately at the $50,000 and $100,000 levels, is higher than that of their Canadian counterpart RS. Thus, one might infer, that the deterrence effect of NYSE actions will be greater than that of RS.

Figure 9



iv. A Few Words on Private Enforcement Activities

So far in my analysis, I have not considered the private enforcement of securities laws. This omission is material, as private enforcement plays an important role in the United States. As indicated in Table 14, during the 2002 -- 2004 period, private enforcement actions accounted for nearly 45 per cent of all securities enforcement actions. These private actions accounted for at least 40 per cent of all monetary sanctions, most likely more since I was unable to collect data on monetary sanctions from NYSE arbitration proceedings. In 2004, a series of very large class action settlements pushed the share of private sanction to more than half of the total. So, in the United States at least, private enforcement actions represent a substantial multiplier to public enforcement in the field of securities regulation. In terms of number of actions, the vast majority of private cases are arbitration proceedings, typically involving customer disputes with broker-dealers and held in NASD and NYSE venues. These cases average more than 2,700 a year during 2002 to 2004. A much smaller number of class action cases are

settled each year, which is about 210, but the monetary awards in these cases are larger.[20] Indeed, class actions represent the single most important source of monetary sanctions in U.S. capital market oversight, exceeding even SEC monetary sanctions. Class actions can be brought against a variety of parties, but issuers and underwriters would be the most common target of these proceedings.

While I have not been able to collect analogous data on private enforcement actions in Canadian securities markets, there is little doubt that private enforcement plays a much less important role in Canada than it does in the United States. My confidence on this point comes from several sources. First, in one case where data are available on numbers of IDA arbitration proceedings, the total number of reported cases a year is quite small (at most less than 70), and of these cases only a fraction end in awards for plaintiffs (at most, 16 a year).[21] Compared to the thousands of arbitration cases brought in the United States, the level of Canadian arbitration proceedings seems trivial. Even if one adds in the hundred or so securities investigations conducted each year by the Ombudsman for Banking Services and Investments,[22] the level of private actions through dispute resolution mechanisms does not seem close to U.S. levels.

Further confirmation of the relatively low levels of Canadian private enforcement actions came through a series of telephone interviews I conducted with Canadian practitioners. When asked to compare sources of potential liability in the two jurisdictions, one practitioner noted that, in Canadian cases, the chief concern for defendants is the authority of provincial agencies (including potential referrals to the Integrated Market Enforcement Team ("IMET")) with the threat of civil liability typically not much of an issue. With matters involving U.S. listed companies, the same practitioner noted, the hierarchy of enforcement concern is inverted: civil litigation is seen as the most serious threat, followed by concern over SEC enforcement actions. If one goes back to the data presented in Table 14, this practitioner's evaluation of U.S. enforcement threats is (on average) accurate. Private litigation is the largest monetary threat, followed by SEC enforcement actions. I have no independent way to confirm the practitioner's ranking of Canadian enforcement risks, but the implication is that the projected risk from Canadian litigation is much lower than the risk of provincial enforcement activity. Again, this observation supports the view that overall enforcement activity in Canada is a good deal less intensive than overall U.S. enforcement intensity.

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[20] My U.S. data does not yet include litigated securities class actions cases, but the omission is probably not material as the overwhelming majority of class action damage awards come through settlements.

[21] For details, see http://www.ida.ca/Investors/Arbitration_en.asp.

[22] Information on the Ombudsman's work appears in annual reports, which are available at http://www.obsi.ca/obsi/pages_english/annrep_home.php3. One of interviewees suggested that recoveries obtained through the Ombudsman's office was roughly of the same magnitude as those obtained through arbitration, although I have not been able to obtain data on this point.

Another clue to inter-jurisdictional differences concerns practitioner commentary about class action litigation in Canada. In another practitioner interview, I was told that the relative paucity of individual claims against Canadian securities firms was generally consistent with general differences in U.S. and Canadian rates of litigation. That is, in this practitioner's view, the differences in litigation were the function of societal differences, including a general aversion to litigation in Canada as well as differences in fee-paying rules. Securities class action, in contrast, were further suppressed in Canada as a result of specific doctrinal limitations, including stiff reliance requirements and other procedural impediments, some judicially constructed, according to this interviewee. While I gather recent legislation may improve the prospects of class action plaintiffs in future case,[23] all of my interviewees suggested that relatively few Canadian securities class actions have generated substantial awards in the past and many cases had failed to achieve any benefits for class members, even when parallel class actions were sometimes able to proceed in the United States. Indeed, I was told of only one truly successful Canadian securities class action—the YBM Magnus International litigation—in which I heard various estimates of the settlement amount, but the highest being an award pf Cdn$100 million. When one compares this single reported award with the average annual $3.5 billion of securities class action settlements in the United States (as reported in Table 14), it is clear, as one interviewee put it, that "the United States is in a world of its own" when it comes to securities litigation.[24]

So if one accepts, as I think reasonable, that private litigation in Canada is substantially less intensive than in the United States, what are the implications for the foregoing analysis? Inasmuch as Canadian public enforcement activity has traditionally been lower than U.S. public enforcement, the gap in overall enforcement activity must become larger when one adds in private actions. Moreover, to the extent that recent increases in Canadian public enforcement action is largely based on a relatively small number of cases, the absence of robust private enforcement mechanisms means that the chances of Canadian issuers being subject to some sort of enforcement action in Canada is even lower than in the United States. Recall that issuers were one area in which provincial authorities appear to be spending less effort than the SEC. So the absence of private enforcement with respect to issuers in Canada may be further evidence that enforcement oversight of Canadian issuers is less stringent than that facing U.S. issuers.

[23] In many respects, Bill 198 does seem to offer important improvements in the ability of plaintiffs to bring actions for relief in securities market cases in Ontario, particularly involving secondary market transactions. I have not, however, attempted to assess the importance of this legislation on private enforcement activity in Canada.

[24] Further support for this proposition comes in the form of my preliminary surveys of Canadian supervision. All respondents indicated that class actions play a relatively small role in Canadian oversight of capital markets.

An implication that I would not necessarily draw is to conclude that Canada should necessarily move dramatically towards to the U.S. system of class actions, as there are many reasons to believe that our litigation system in this area is inefficient and inequitable. In addition, there is some evidence that much U.S. private class action litigation largely piggy-backs off of public investigations and may, in some sense, be redundant of public oversight. Accordingly, a possible response to the absence of strong class action traditions in Canada might be the expansion of public enforcement apparatus, especially with respect to issuers, and not the introduction of a new class of judicial proceeding. While there are also those who are critical of the level of individual arbitration rates in the United States, I would be more inclined to investigate this area to ensure that adequate mechanisms exist for redress of individual injuries caused by securities firms or other intermediaries. Of course, offering prescriptions of this sort is subject to the caveat with which I began: There are no strong theoretical reasons to suppose that the level of enforcement intensity in the United States is an appropriate benchmark for fine-tuning Canadian policy.

v. Criminal Prosecutions

Yet another area in which I have been unable to collect comprehensive data concerns criminal prosecutions. Again, this is an area in which the United States excels. According to my research, federal authorities in the United States imposed an average of 4,100 months of prison sentences on securities law violators during the 2002–2004 period. According to NASAA analysis, even more months of prison terms, supposedly 8,600 months, were handed out at the state level during a 2001–2002 study period. While vagaries of sentencing guidelines and parole rules make these numbers somewhat difficult to interpret, one can safely conclude that criminal prosecutions are a real and credible component of U.S. securities enforcement. Prosecutions in high-profile cases garner considerable media attention, and industry participants are well aware of the threat of criminal sanctions.

According to my interviewees, the threat of criminal sanctions for securities law violations remains more a possibility than a reality in Canada today. Several explanations were provided: a lack of expertise and resources on the part of the Royal Canadian Mounted Police in the past; poor judicial management of the criminal docket; and the unconstrained capacity of defense counsel to delay trials for many years in the hope that evidence will become stale or that the prosecution will lose interest in the case. While several interviewees expressed the view that criminal referrals to the IMET would soon result in multiple prosecutions, indeed, one interview expressed a concern that too many routine cases were being referred to the IMET. The prosecutions have not yet taken place in large number. Accordingly, as an historical matter, one can simply note that criminal prosecutions, like civil litigation, is an area in which Canadian regulatory intensity trails the United States by a good margin.

5. Conclusions & Recommendations

In an academic setting, I would not ordinarily conclude a paper of this sort with detailed policy recommendations since the data are still fragmentary and the paper addresses only one facet of regulatory policy. However, as the Task Force has requested my views on policy implications, I would suggest the following issues for further study.

Recommendation #1:: **In terms of the overall size of Canada's regulatory apparatus, I do not see strong evidence for suspecting that more personnel is needed. Indeed, by international levels, total Canadian staffing and budgets seem to be on the high end. I do, however, think that some attention might be given to budgetary levels (mostly salaries) for Canadian regulators. My analysis suggests that, at least in the United States, the allocation of budgetary resources to staff is higher.**

Recommendation #2: **In terms of sanctioning policy, I think more work needs to be done to understand whether the trends noted in my paper are permanent or temporary. To the extent that Canadian public sanctions, particularly monetary sanctions, fall back to the level suggested in some of my first period analyses, I would be concerned that enforcement oversight would be too lax. While I recognize that I lack strong normative foundations for this claim, I do think that common sense suggests that Canadian sanctioning efforts should not be set at a small fraction of the sanctions imposed in its large neighbor to the South. If nothing else, such a disparity would encourage fraud to migrate across the 49th parallel.**

Recommendation #3: **To the extent that enforcement activity stabilizes at levels suggested by my full period analyses, the policy implications are less clear. My preliminary review of the distribution of Canadian sanctions suggests that a more even distribution of sanctioning, rather than a very few large sanctions, could enhance deterrence. Also, I think more attention should perhaps be given to the oversight of issuers, as that area of enforcement activity seems to be shortchanged in Canada, at least with respect to the United States. Some more careful consideration of supervisory specialization between provincial authorities and SROs may also be useful. (See footnote 19 above for an alternative perspective on this recommendation.)**

Recommendation #4: **The more difficult issues concern private litigation in Canada. One fairly straightforward policy recommendation would be for Canadian authorities to do a better job collecting data on private litigation such as arbitration, ombudsman actions and, also, class action**

suits. (Though I didn't touch upon the issue in my analysis, I think it would also be useful to have data on enforcement actions, both public and private, against Canadian issuers in other jurisdictions.) If, as I suspect, the data confirm that private enforcement activity in Canada is quite low compared to the United States, the Task Force has several choices: 1) Recommend the enhancement of private enforcement (either individual arbitration or judicial class action) to more closely approximate the U.S. model; 2) Recommend the enhancement of public enforcement (perhaps with greater reliance on providing private compensation) in order to match U.S. oversight efforts without replicating U.S. litigation; or 3) Accept that Canada will not attempt to replicate the effect of U.S.-style private enforcement activity.

<u>Recommendation #5:</u> Improving the efficacy of criminal prosecution seems also an important issue of reform for Canadian securities markets. Again, having access to better data on criminal prosecutions would be useful. And most of what I heard from my interviewees suggest that further improvements at the IMET is needed, although I also was led to believe that this process may already be underway.

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