IIAC ACCVM

Investment Industry Association of Canada Association canadienne du commerce des valeurs mobilières

October 9, 2024

Submitted via Email

Attention:

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, Ontario M5H 3S8
E-mail: comments@osc.gov.on.ca

Dear Sir/Madame:

RE: RESPONSE TO ONTARIO SECURITY COMMISSION'S REQUEST FOR COMMENTS ON: PROPOSED OSC RULE 11-502 DISTRIBUTION OF AMOUNTS PAID TO THE OSC UNDER DISGORGEMENT ORDERS (THE "RULE"); PROPOSED COMPANION POLICY 11-502 DISTRIBUTION OF AMOUNTS PAID TO THE OSC UNDER DISGORGEMENT ORDERS (THE "CP"); PROPOSED OSC RULE 11-503 (COMMODITY FUTURES ACT) DISTRIBUTION OF AMOUNTS PAID TO THE OSC UNDER DISGORGEMENT ORDERS (COLLECTIVELY, WITH THE RULE, THE "PROPOSED RULE"); PROPOSED COMPANION POLICY 11-503 (COMMODITY FUTURES ACT) DISTRIBUTION OF AMOUNTS PAID TO THE OSC UNDER DISGORGEMENT ORDERS (COLLECTIVELY, WITH THE CP, THE "PROPOSED COMPANION POLICY") - MODERNIZE THE PROCESS TO DISTRIBUTE DISGORGED AMOUNTS TO HARMED INVESTORS.

The Investment Industry Association of Canada ("**IIAC**") is the national association representing investment firms that provide products and services to Canadian retail and institutional investors. The IIAC appreciates the opportunity to respond to the Commission's Request for Comments on the Proposed Rule and Companion Policy.

OVERVIEW OF POSITION:

The IIAC generally supports the objectives of the Proposed Rule, which include defining the circumstances in which the Commission is *required* to compensate harmed investors using funds that the Commission has received in payment of disgorgement orders. We appreciate the Commission's efforts to establish a framework for the timely and effective distribution of funds to investors who have suffered a direct financial loss as a result of a contravention of Ontario securities law in accordance with s. 128.1 of the Ontario *Securities Act*, R.S.O. 1990, c.S.5 (the "***Act***").

However, we have concerns with respect to the limited scope of the Commission's proposed distribution framework. Our concerns and recommendations are detailed below.

SUMMARY OF CONCERNS:

The IIAC is concerned that the distribution framework contemplated in s. 128.1 of the Act, the Proposed Rule, and Proposed Companion Policy, is limited to disgorgement orders and does not apply to payments received by the Commission in respect of settlement agreements and/or administrative penalties. The proposed framework will only allow harmed investors to recover in the limited circumstances in which a respondent is ordered to disgorge ill-gotten gains, the respondent complies with the disgorgement order, and the amount of the disgorgement order is sufficient to compensate the direct financial losses that investors have incurred as a result of the respondent's misconduct. We are concerned that the limited scope of this proposed framework will negatively impact its effectiveness as a tool for investor redress.

DETAILS OF CONCERNS:

Settlement Payments

From our review of the Proposed Rule and Companion Policy, it is not clear whether the proposed definition of "disgorgement order" includes disgorgement orders that are made as part of approved settlement agreements. We note that the Proposed Rule and Companion Policy draw a distinction between funds received in respect of disgorgement orders and funds received for the payment of settlements. The Commission's Request for Comments also:

- Draws a distinction between the Commission's proposed framework and the Commission's existing tools to return money to investors, which include the use of receiverships and "no contest settlements"; and
- Notes that settlement payments will continue to be dealt with in accordance with subsection 19(2) of the *Securities Commission Act*, S.O. 2021, c. 8, Sched. 9 (the "***SCA***").

In our review of recent proceedings before the Financial Services Tribunal (and its predecessor), we found that a disproportionate number of proceedings continue to be resolved by way of approved settlement as opposed to a decision on the merits and, therefore, account for a significant proportion of the funds that are paid to the Commission. As such, the issue of whether settlement payments are included or excluded from the Proposed Rule will necessarily affect the scope and effectiveness of s. 128.1 of the *Act*.

We therefore ask that the Proposed Rule be clarified to include settlement payments.

Administrative Penalties

We are also concerned that the framework that is being contemplated by the Commission will place an arbitrary restriction on the amount of funds that are made available to harmed investors by limiting the scope of this framework to disgorgement orders and excluding amounts paid to the Commission in respect of administrative penalties.

As the Commission acknowledges, disgorgement orders are focused on depriving respondents of amounts received in breach of securities law rather than compensating aggrieved investors. Disgorgement orders do not reflect and are not calculated on the basis of third-party loss. As such, it is unclear why the Commission's proposed framework applies to disgorgement orders but does not apply to administrative penalties.

We note that the United States Securities Exchange Commission has adopted a framework for the distribution of funds to harmed investors that includes monetary penalties.[1] We also note that the recommendations made by the Auditor General of Ontario, which informed the Commission's proposed framework, included the distribution of administrative penalties to harmed investors.[2]

In our review, we have found that the amount and frequency of disgorgement orders is highly variable from year to year and a significant portion of the payments made to the Commission relate to administrative penalties. Despite this, the Commission's Request for Comments states that the Commission will continue to deal with administrative penalties in accordance with s. 19(2) of the *SCA,* which means that the distribution of those funds to harmed invests will remain subject to the Commission's discretion. As noted in the Request for Comments, there is no statutory framework for the distribution of administrative penalties, however, the Commission's practice is to allocate these funds to investors "if practicable in the circumstances".

We appreciate that s. 128.1 of the *Act* is limited to disgorgement orders and that the inclusion of administrative penalties in the proposed framework would likely require legislative amendments which the Commission may pursue. Pending legislative amendments, the Commission has the ability to create rules to better define the circumstances in which the Commission will exercise its discretion to distribute administrative penalties to harmed investors and set the parameters for such distributions.

RECOMMENDATIONS:

The IIAC recommends that the Commission amend the Proposed Companion Policy to include disgorgement orders made in connection with approved settlement agreements.

Pending further legislative amendment, the IIAC also recommends that Commission establish rules, subject to public comment, to clearly define the circumstances in which the Commission will exercise its discretion to distribute funds received in respect of of administrative penalties to harmed investors under s. 19(2) of the *SCA*. It is our view additional guidance and transparency on the Commission's use of the funds paid to the commission for administrative penalties will allow for a more effective system of investor redress.

We are happy to discuss the issues raised in this letter in further detail.

Respectfully submitted,

Investment Industry Association of Canada

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[1] The SEC is empowered to create "Fair Funds" to distribute disgorged funds and administrative penalties to defrauded investors. *Sarbanes-Oxley Act of 2002*, Pub. L, 107-204, 116 Stat. 745 at s. 308(a).

[2] See Recommendation No. 12 of the Auditor General of Ontario. Office of the Auditor General of Ontario, *Value-for-Money Audit: The Ontario Securities Commission* (December, 2021) at p. 34.