



ECONOMIC ISSUES
ASSOCIATED WITH THE
ESTABLISHMENT OF A
SINGLE SECURITIES COMMISSION

Prepared by:
Daniel Denis
Partner

April 2010



MONTRÉAL :: NEW YORK :: PARIS :: QUÉBEC :: TORONTO :: VANCOUVER

TABLE OF CONTENTS

INTRODUCTION AND CONTEXT	2
1. THE ECONOMIC CONTRIBUTION MADE BY A DYNAMIC FINANCIAL CENTRE.....	4
Summary.....	4
Why is the financial sector important from an economic standpoint?	4
What are the key characteristics of a dynamic financial centre?.....	5
What factors favour the presence of a genuine financial centre?	6
How does regulation contribute to the financial sector's vitality?	7
2. CHANGES IN AND CHALLENGES FACING QUÉBEC AS A FINANCIAL CENTRE.....	9
Summary.....	9
What is the size of the financial sector in Québec and Montréal and how has it changed?	9
What is Québec's or Montréal's situation as a financial centre?	10
3. ECONOMIC ISSUES ASSOCIATED WITH THE ESTABLISHMENT OF A SINGLE SECURITIES COMMISSION	13
Summary.....	13
Fewer levers available to develop Québec's financial centre	13
Less sensitivity to the needs of issuers in Québec	17
A decrease in economic activity in Québec arising from the regulatory function.....	19
CONCLUSION	21

INTRODUCTION AND CONTEXT

- The question of the establishment of a single securities commission for Canada as a whole is not new. The topic has been on the federal agenda for several years. In its 2009 and 2010 budgets, the Canadian government has reasserted its determination to create a Canadian securities commission, with or without the participation of all of the provinces.
- A Transition Bureau has been set up in anticipation of the transition to a single securities regulation regime in Canada and draft legislation on the establishment of the Canada-wide agency is expected in 2010. Québec, Alberta and Manitoba have already indicated their opposition to the federal proposal. Moreover, Québec and Alberta have initiated legal proceedings to challenge the constitutionality of a federal regulatory agency in this field.
- The establishment of a single Canadian securities commission has numerous legal, financial and economic repercussions. From Québec's standpoint, in particular, the creation of such an agency would call into question certain of its regulatory responsibilities. Furthermore, certain activities of the AMF could become legally or functionally obsolete were a Canadian securities commission to be established.
- Current debate is focusing largely on the legal and constitutional dimensions. Economic aspects, especially the repercussions on the Québec financial industry, have until now received much less coverage. However, this dimension also warrants close attention, bearing in mind the role that regulatory bodies play in the functioning of financial markets and the importance of financial markets with respect to a territory's economic development.
- This note seeks to delineate the key economic issues for Québec that would be linked to the establishment of a single securities commission. Bearing in mind the numerous unknowns concerning the nature, distribution and location of the operations of such a Canada-wide commission, it is not, however, possible at this stage to conduct a quantitative evaluation of its economic repercussions on Québec. On the other hand, **we can already pinpoint several significant adverse repercussions associated with the establishment of a single commission, whether in respect of the Québec financial sector or Québec issuers.**
- This note is divided into three parts:
 - The first part focuses on the importance in respect of a territory's economic development of a strong, dynamic financial centre and the specific contribution that the presence of regulatory bodies makes to this performance.
 - The second part illustrates changes in and the challenges facing Québec as a financial centre, in particular its weaker growth in recent years and the decline in the number of its hubs of influence.
 - The third part highlights the issues linked to the establishment of a single securities commission as regards the positioning of Québec's financial industry, the financing of Québec businesses, and Québec's economic development levers.
- It should be noted from the outset that the economic issues pinpointed in this note are in no way contrary to consumer protection. It is common knowledge that weak oversight of the

financial sector is a factor that limits investment and economic development. There is no question whatsoever of reducing the quality of the regulatory framework.

- On the other hand, wanting to preserve for Québec the economic benefits stemming from the current regulatory situation in no way implies sacrificing the protection of investors. Quite the reverse is true. Canada's current regulatory structure governing securities is already acknowledged as one of the best in the industrialized nations.¹
- The protection of investors is obviously a basic component of the mission of a financial regulatory body and must remain so. While we ensure that the regulatory body can fully play this role of protecting the interests of Québec investors, it can at the same time act as a key catalyst in efficient financial markets.

¹ See, for example, A. De Serres, S. Kobayakawa, T. Slok, and L. Vartia, "Regulation of financial systems and economic growth in OECD countries: An empirical analysis," *OECD Economic Studies No. 43*, 2006/2. Canada ranks second among the major industrialized nations with respect to the protection of investors and the quality of its securities regulations, ahead of the United States, England, France, and Australia.

1. THE ECONOMIC CONTRIBUTION MADE BY A DYNAMIC FINANCIAL CENTRE

SUMMARY

- The financial sector continues to occupy an intrinsically important place in the economy, especially in the economies of the developed nations. It also plays a key role in the allocation of resources for the development of other sectors of the economy. These contributions explain the efforts made in several regions to maintain or develop this field of business.
- This sector contributes all the more to a territory's economic development when it is an integral part of an active, dynamic financial centre. Certain key characteristics are the hallmarks of the vitality and strength of a financial centre.
- The regulatory body is, in this respect, a major component in the financial sector. Regulatory bodies can enhance the vitality of a financial centre both through their own activities and how they operate.

WHY IS THE FINANCIAL SECTOR IMPORTANT FROM AN ECONOMIC STANDPOINT?

- The financial sector is a very fertile business area as regards a territory's or a region's industrial fabric.
- First, the financial sector is a **major direct employer**. It generally accounts for 5% or more of jobs in metropolitan areas and its relative importance may exceed 10% in regions where this sector is more dynamic. The financial sector also offers a high proportion of quality jobs with salaries that are above the average in other industrial sectors. In 2008, average yearly earnings in all industrial sectors in Canada stood at \$42 824, compared with \$53 914 for the finance and insurance sector, i.e. 25.9% higher.²
- The financial sector also makes an **important indirect contribution to the economy of a territory**. In fact, financial firms are major purchasers of goods and services for other strategic industries. For example, this sector is one of the biggest consumers of information and communications technologies (ICT). In 2008, the six biggest Canadian banks allocated \$5.9 billion to ICT. The financial sector is also a major purchaser of accounting, legal and tax services. Moreover, the financial sector is one of the main occupants of rental space in city centres. It also contributes significantly to charity. All told, each direct job in the financial sector helps to support an additional job in a wide array of industrial sectors, a high proportion of them in the value-added professional services sector.³
- The financial sector also **gives considerable impetus to economic development**. Its main role is obviously to provide financial intermediation and, *ipso facto*, it is a supplier of capital, savings products, services and advice aimed at businesses and individuals. The more effective and efficient this intermediation is, the more economic growth will be facilitated in the territory. The financial sector is also

² Statistics Canada, *Survey of Employment, Payrolls and Hours*. CANSIM table 281-0027, All industries compared with finance and insurance, 2009.

³ The ratio of indirect and direct jobs is drawn from the Statistics Canada input-output models and from the Institut de la Statistique du Québec (2009 version).

a field whose impact can largely extend beyond the immediate territory of its operations and even be felt at the international level. This impact can take several forms, e.g. the organization of conferences, meetings and events that assemble foreign experts, international networking, its visibility or power of attraction among foreign investors, and so on.

- Given the financial sector's economic importance, it is hardly surprising that **a number of regions are making a significant effort to maintain or develop their activities**. Numerous regions have, in recent years, adopted strategies and guidelines to foster the development of their financial sector, including London, New York, Geneva, Paris, Dubai, Singapore, Sydney, Dublin, Seoul, Toronto, Vancouver, Edinburgh, Munich, and so on.
- These strategies focus on **the establishment of conditions that promote the existence of a genuine financial centre**. The financial sector is, in fact, sensitive to neighbourhood effects and the presence or absence of such effects has significant repercussions on the size and vitality of a territory's financial sector.

WHAT ARE THE KEY CHARACTERISTICS OF A DYNAMIC FINANCIAL CENTRE?

- Despite the development of information technologies and more widespread digitization of data, financial operations are highly sensitive to neighbourhood effects, which explains the maintenance of a **geographic concentration of this industry in certain territories and the establishment of financial centres**. Financial centres “ensure the assembly of numerous stakeholders who participate in the smooth operation of financial markets with ecosystems that generate significant synergy.”⁴ [TRANSLATION] The presence of numerous stakeholders and the existence of synergy between them are the hallmarks of an active, dynamic financial centre.
- A dynamic financial centre is recognizable through the **depth of its pool of stakeholders and its resources**:
 - The community of stakeholders in a financial centre obviously encompasses issuing bodies, investors and intermediaries. These stakeholders are at the centre of financial transactions. However, a financial centre is not confined to these functions and must also rely on logistical support operations. The community of stakeholders in a financial centre includes *ipso facto* a broad range of experts in highly specialized fields with high added value, i.e. risk analysts, jurists, lawyers, accountants, computer specialists, tax experts, and so on.
 - Dynamic financial centres also offer these stakeholders architectures such as efficient technical infrastructure and modern regulatory environments that facilitate exchanges. The regulatory body represents *ipso facto* a component of the ecosystem of a dynamic financial centre.
 - A financial centre can exist without being fully integrated and maintain on site all of these functions, but its size and vitality will be affected accordingly. For example, an organized banking system cannot alone spur the establishment and vitality of a financial centre, even it is an essential breeding ground. A broader, fuller range of experts in varied fields is essential to more extensive development.

⁴ Banque de France, “Places financières et banques centrales,” 2nd quarter 2000, *Revue d'économie financière* n° 57.

The presence of this additional expertise ensures that a financial centre can have a much broader impact.

- A dynamic financial centre is also recognizable through the **extent of the impact of its operations:**
 - A financial centre may only have an impact at the regional level. Its functions will be confined essentially to basic financial operations and the local services offered to customers. The size and expansion of the regional economy will determine its importance and scope.
 - A financial centre can also have a much greater impact by carrying out specialized operations on behalf of customers outside the region. These operations are usually linked to more specialized or less common services and to operations that require a critical mass of expertise or favourable localization conditions. These operations are part of the exporting of services and thus contribute to increasing the region's economic wealth, not to mention that such operations often have added value and are conducted by highly skilled workers.
 - Moreover, a financial centre's wider impact can enhance a region's attractiveness. It can attract the operations centres of financial enterprises active in the same field that wish to avail themselves of the expertise developed and available in the region. It can also attract the decision-making centres of non-financial enterprises since the latter are the main consumers of elaborate financial services.
- A dynamic financial centre is also recognizable through **its ability to adapt and innovate:**
 - A financial centre is an essential means to mobilize domestic investment and the financing of local businesses. It must provide a level of quality service to the entire financial sector and to the non-financial sector. The quality of this service is closely linked to the financial centre's ability to adapt to changing needs and the business context of its clients or users.
 - A financial centre that is innovative from the standpoint of its products and services or its business methods will more readily adapt to changing needs and the business context. It should be noted that an innovative financial centre does not imply less protection for savers or investors. To the contrary, innovation can bolster this protection and enhance the functioning of financial intermediation.
 - The existence of an innovative financial centre contributes to the better allocation of resources and to brisker economic growth. An innovative financial centre also reflects on the territory overall through the image that it projects outside the territory.

WHAT FACTORS FAVOUR THE PRESENCE OF A GENUINE FINANCIAL CENTRE?

- Beyond the size of the regional or national economy, there are factors that favour the presence of a financial centre with greater depth and that has more impact and the ability to innovate more extensively. The **factors that underpin the strength and attractiveness of a financial centre** can be divided into four main groups:
 - *The presence of a pool of financial skills:* Human capital is the main resource of financial operations. A financial centre is all the more attractive when it possesses abundant workers with a broad range of financial skills.

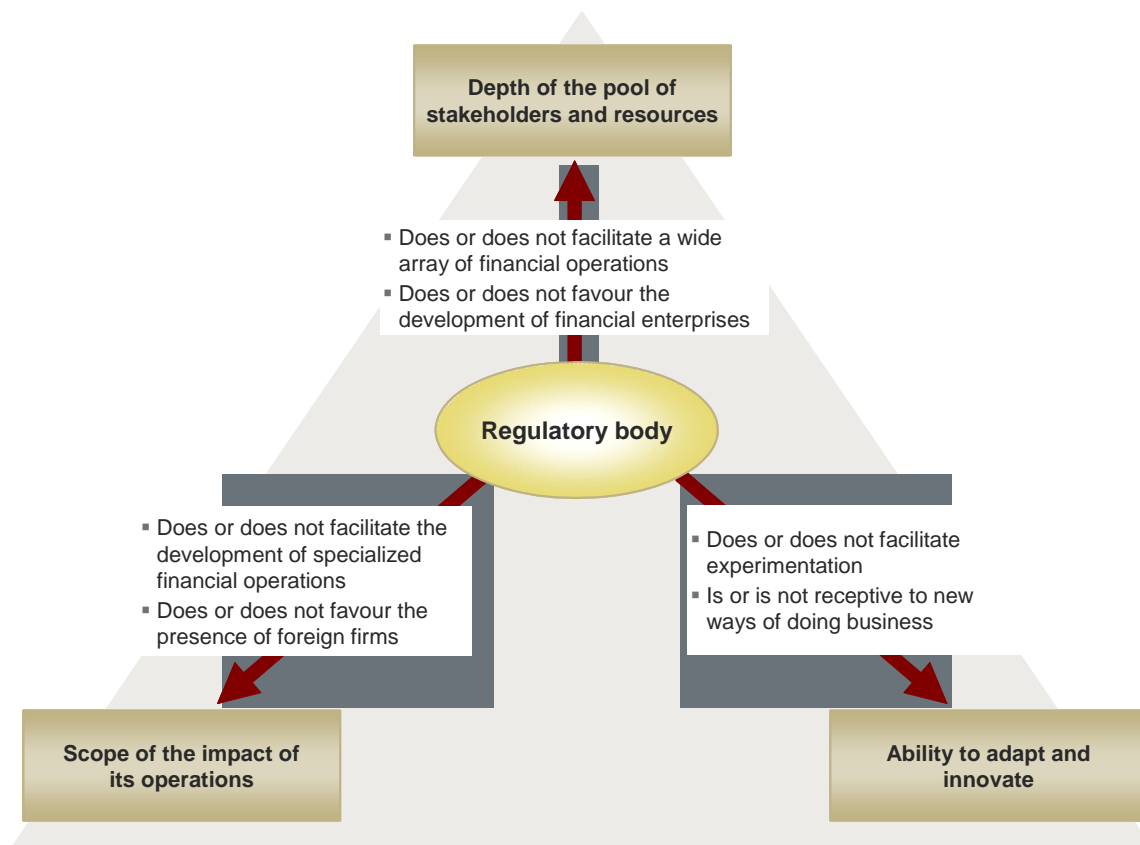
- *The ability to generate external economies:* The more synergy there is between the stakeholders, the stronger and more attractive a financial centre will be. Such synergy can stem from the proximity and circulation of information between stakeholders in the centre, or the presence of a platform that satisfies common needs, e.g. top-notch training, specialized support services, a research institute, and so on.
- *A favourable business environment:* Financial operations are highly sensitive to the overall business environment, in particular from the standpoint of taxation, legislation, costs, and the quality of certain physical infrastructure.
- *A quality regulatory framework:* The regulatory framework is a key factor in a financial centre's strength and attractiveness. The next section focuses more specifically on this factor.

HOW DOES REGULATION CONTRIBUTE TO THE FINANCIAL SECTOR'S VITALITY?

- **Regulatory bodies are in themselves an integral, active part of a financial centre.** Like financial institutions, they assemble a significant number of specialized individuals in several highly qualified fields. They also purchase strategic products and services, in particular professional services.
- A number of experts regard the regulatory function as **an intrinsic component of the financial sector.** For example, the Z/Yen Group, which conducts a review of major financial centres, considers separately government and regulatory bodies as an important sub-sector of the financial industry. Government and regulatory bodies are one of five main sub-sectors in the industry, along with the banking sector, the insurance sector, asset management, and specialized professional services.⁵
- Beyond the economic activities stemming from their operating expenditures, regulatory bodies contribute to economic development through the regulation of financial markets. **In fact, regulatory oversight plays a key role in a financial centre's vitality or lack of it.** This dimension is included in the key critical factors named by all observers, studies and analyses focusing on the conditions on which a financial centre's success hinges.
- **The quality of regulatory oversight** is usually associated with the following characteristics:
 - compliance with legal principles;
 - the relative stability of the body of regulations;
 - guarantees concerning the protection of investors;
 - the simplicity of compliance measures;
 - the regulatory body's receptiveness and collaboration.
- Regulatory oversight also affects each of the three main dimensions of an active, dynamic financial centre (see the diagram below). Regulatory bodies can thus contribute or not contribute to this vitality depending on the quality of their oversight. In return, the quality of oversight is linked to the regulatory body's levels of collaboration and expertise.

⁵ The Z/Yen Group produces the *Global Financial Centres Index*, which classifies financial centres according to their level of competitiveness and attractiveness. See also Part 2.

THE THREE KEY CHARACTERISTICS OF A DYNAMIC FINANCIAL CENTRE AND THE CONTRIBUTION MADE BY REGULATORY BODIES



- Regulation must obviously satisfy stakeholders' needs from the standpoint of transparency and security, but it must also allow the latter sufficient flexibility to innovate and develop.
- **The quality of regulatory oversight is important for all financial centres, but it is even more important for those that do not serve a big domestic market.** This situation applies, in particular, to Québec and to Montréal's financial centre.

2. CHANGES IN AND CHALLENGES FACING QUÉBEC AS A FINANCIAL CENTRE

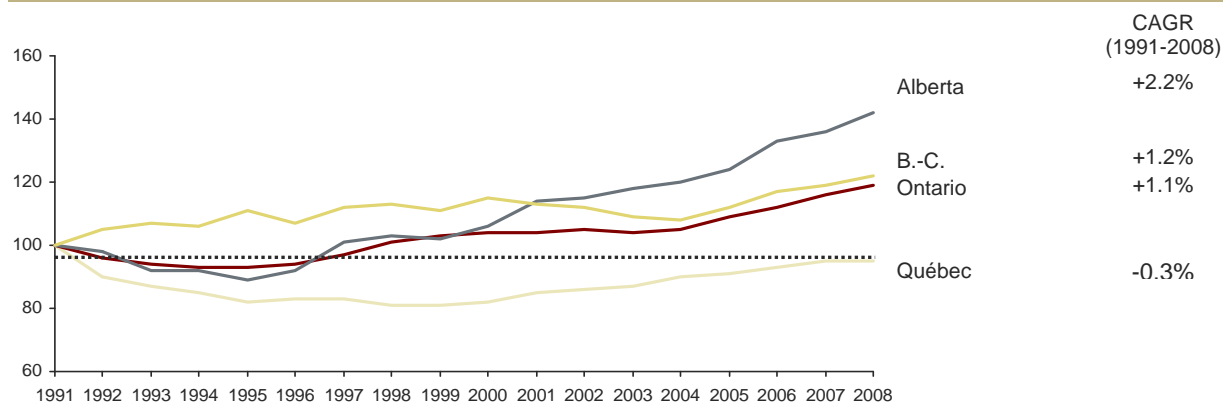
SUMMARY

- The financial sector is very important to Québec's and Montréal's economic fabric. On the other hand, the financial sector in Québec and Montréal is shrinking compared with the other provinces. Québec's impact as a financial centre has also dwindled and the region has few specialized activity centres.
- Moreover, Toronto, which already benefits from natural attraction, is making a greater effort to accelerate its development. Such effort risks further increasing Québec's fragility as a financial centre.
- Montréal's financial centre still enjoys certain advantages and can become even more competitive in Canada and, indeed, at the international level. It is important to grasp the changes in and challenges facing Québec as a financial centre to fully understand certain negative economic repercussions of a single securities commission.

WHAT IS THE SIZE OF THE FINANCIAL SECTOR IN QUÉBEC AND MONTRÉAL AND HOW HAS IT CHANGED?

- **In 2008, the financial industry directly employed more than 97 000 people in the Montréal area.** This number excludes support services jobs and those in public organizations devoted to financial monitoring and regulation. When account is taken of jobs in the financial ecosystem overall, including the regulatory function, it is estimated that nearly 150 000 people in the Montréal area have jobs that depend directly or indirectly on this activity, i.e. nearly 7.5% of jobs in the territory.
- **In Québec as a whole, there were 155 000 direct jobs in the financial sector in 2008.** Bearing in mind the ecosystem overall and the jobs maintained in the supply chain, the jobs of nearly 300 000 Quebecers are linked to this field of activity.
- **However, the Québec financial sector has declined in recent years compared with the changes noted in the other big Canadian provinces.** Québec lost 8 000 jobs in the financial sector between 1991 and 2008, while the number of jobs increased by 52 000 in Ontario, 20 000 in Alberta and 15 000 in British Columbia (see the diagram below). The proportion of GDP that the financial sector in Montréal represents has also grown more slowly than in other big Canadian cities since 1988, i.e. 2.6% a year in Montréal as against over 4.0% a year in Toronto, Calgary and Vancouver. It should be noted that this discrepancy is more marked than that of the overall GDP of the provinces in which each of the cities is located. This denotes that Montréal as a financial centre has experienced a relative loss of impact since 1988.

LEVEL OF EMPLOYMENT IN THE FINANCIAL SECTOR (FINANCE/INSURANCE/LEASING) – PRINCIPAL CANADIAN PROVINCES
(1991 to 2008; 1991 = 100)



Sources : ISQ ; Statistics Canada (Statistics Canada (SEPH method))

- **Montréal’s position at the international level is also declining.** Overall, Montréal ranked 32nd on the worldwide scale of financial centres in the Global Financial Centres Index (GFCI) published in September 2009.⁶ Since March 2007, Montréal has fallen from 21st to 32nd place. Vancouver overtook Montréal in September 2008 and Toronto has remained in 13th place.
- The GFCI report also classifies financial centres according to five industry sub-sectors: (i) asset management; (ii) banking operations; (iii) government and regulation; (iv) insurance operations; and (v) professional services. **Montréal ranks in the top 20 solely in respect of the “government and regulation” sub-sector** (19th place) and it surpasses Vancouver in only two sub-sectors, i.e. government and regulation, and professional services.
- Moreover, **Ontario and Toronto continue to organize themselves to increase the size and influence of their financial sector.** Toronto does not merely make do with the natural factors that foster its development, since it recently adopted a strategic plan to accelerate such development. In November 2009, the Toronto Financial Services Alliance (TFSA) pinpointed strategic opportunities that could create between 25 000 and 40 000 new jobs and add between \$4 billion and \$5 billion to the region’s GDP within five years. As we will see later, the Ontario government and Toronto are also bringing pressure to bear to have the headquarters of the federal securities commission located in Toronto, thus recognizing the importance of the regulatory body’s presence from the standpoint of the vitality and the development of the financial sector.

WHAT IS QUÉBEC’S OR MONTRÉAL’S SITUATION AS A FINANCIAL CENTRE?

- In the last two decades, Montréal has sought in various ways to offset Toronto’s centralizing force, in particular by relying formally on certain niches:

 - the development of derivative products (it is recognized as the Canadian centre of expertise);
 - the NASDAQ initiative, which proved fruitless;

⁶ Index compiled and published regularly by the Z/Yen Group.

- attempts to attract foreign financial institutions through the IFC Montréal and the IFC program, a measure that has led to the development of 115 International Financial Centres involving 1 500 individuals, but which has stagnated in recent years.
- At the same time, certain forces have also come into play more informally to attract or maintain the support functions of financial institutions, in particular:
 - the influence of the Caisse de dépôt et placement du Québec, the Mouvement Desjardins and National Bank;
 - the presence of substantial retirement funds;
 - the strength of electronic data processing services in Montréal;
 - the quality and recognition of Québec’s actuarial expertise.
- More recently, the latest Québec Budget supported the establishment of a steering committee for the development and advancement of the financial sector and amended the rules of the IFC program to revitalize this type of activity.⁷ These measures seek to foster the emergence of a concerted strategy to make Montréal a strong financial centre in North America.
- The following table presents a high-level evaluation grid of Montréal’s and Québec’s situation as a financial centre. The factors in bold type are aspects that have a direct or indirect link with Québec regulations.

Strengths	Weaknesses
<ul style="list-style-type: none"> ▪ A highly attractive environment with respect to several basic factors: <ul style="list-style-type: none"> • costs, the quality of infrastructure, the university and Cegep network, the proximity of major centres, and the regulatory framework ▪ A stable, secure socio-political environment ▪ A bicultural society ▪ Numerous head offices of big regional, national and foreign financial institutions are located there ▪ The derivatives centre of Canada (the Montreal Exchange) 	<ul style="list-style-type: none"> ▪ Montréal is a small financial centre ▪ Economic growth in Québec is moderate ▪ Growth in employment in the sector is below that in other Canadian cities ▪ Key private-sector and institutional stakeholders are of a regional nature ▪ There is little cooperation and collaboration between stakeholders in the sector and a shared concern to promote Montréal as a financial centre is lacking ▪ There are few tools devoted to promotion and external impact
Opportunities	Threats
<ul style="list-style-type: none"> ▪ Take advantage of the repositioning initiated by financial institutions in response to the crisis (in addition to the usual factors, Montréal's safe environment makes it a legitimate alternative for the relocation of a number of operations) ▪ Broaden cooperation and collaboration between public and private stakeholders in the sector to enhance Montréal's competitiveness and promote it abroad ▪ Make Montréal a strong regional player focusing on national and international niches such as derivatives 	<ul style="list-style-type: none"> ▪ The factors that foster globalization are hampering Montréal's development ▪ Several other financial centres, including Toronto, are organizing themselves on the international scene ▪ The merging of stock exchanges in Canada and the establishment of a single securities commission ▪ Inadequate promotion of Montréal as a financial centre ▪ Follow-up and coordination are required to ensure the implementation of development initiatives

⁷ See Ministère des Finances du Québec, *2010-11 Budget, Additional Information on the Budgetary Measures*, March 30, 2010, page 188.

- From the standpoint of basic factors, Montréal has what is necessary as a financial centre:
 - sound basic **infrastructure**;
 - qualified **workers** and a flexible **regulatory framework**;
 - a centre that facilitates **interaction** between stakeholders in the sector and the sharing of **information**;
 - a centre that is surrounded by activities that allow for **networking**.
- Montréal can reasonably aspire to being recognized as an important regional financial centre. Moreover, **Montréal and Québec could distinguish themselves in certain fields**. To this end, it is important to consider three dimensions in respect of which “small” financial centres can compete:
 - effective cooperation and coordination of public and private initiatives to promote and develop the financial sector;
 - initiatives to foster the establishment and development of enterprises in targeted niches;
 - promote Montréal as a credible financial centre that possesses solid expertise in specific niches.
- Such a strategy could resolve the twofold problem that Montréal is facing, i.e. contribute to the development of existing financial enterprises, attract new firms and create new jobs; and position Montréal as a niche financial centre on the national and international scene.
- The challenges are daunting but can be faced and met successfully. **As we will see in the section below, the presence of a single federal securities commission could, however, prejudice the desired changes.**

3. ECONOMIC ISSUES ASSOCIATED WITH THE ESTABLISHMENT OF A SINGLE SECURITIES COMMISSION

SUMMARY

- The establishment of a single securities commission could have a negative economic impact on three levels: i) fewer levers available to foster the development of Montréal as a financial centre or of Québec; ii) less sensitivity to the specific characteristics, concerns and problems of Québec companies and institutions iii) a decrease in regulatory activities carried out in Québec and, hence, in economic activities generated in Québec by the regulatory function.
- It is not possible at this stage to quantify these impacts given the many unknowns as to the nature, distribution and location of the activities of a Canada-wide securities commission. However, we can identify some significant negative impacts associated with such a development, whether for Québec's financial sector or Québec issuing companies. These negative economic impacts arise from the loss of regulatory decision-making authority.

FEWER LEVERS AVAILABLE TO DEVELOP QUÉBEC'S FINANCIAL CENTRE

- An active and dynamic financial centre ensures the creation of highly-skilled jobs that by the very fact participate in the development of high value-added activities. In addition, successful and innovative financial markets contribute to economic growth of non-financial enterprises by facilitating the allocation of capital. As mentioned earlier, this vitality is fed by the activities and decisions of many different stakeholders, as well as their interactions. Among these stakeholders, regulatory organizations have an important role to play.
- The regulator is an important component of the financial sector. **Regulatory bodies can contribute to the dynamism of a financial centre through their own activities and their methods.** This last aspect is important because harmonization of legislation and the associated regulations has increased in recent years. Such harmonization provides investors with a platform that minimizes the risk of adverse effects of regulatory competition among jurisdictions. However, despite this desirable underlying trend, it is important to emphasize three major advantages of the existing framework:

For harmonized rules, the provinces and territories put forward their views and **influence the development of common regulations.** Québec has not only asserted its interests at the “roundtable of provincial regulators”, but has taken a real leadership role in the establishment of common rules. For example, the Québec regulator has initiated or provided the model for many rules for the registration of intermediaries, including the system of handling complaints, the concept of permanent registration, and registration according to the exercise of activity rather than the nature of transactions. Québec has also provided leadership in chairing two important pan-Canadian committees of regulators

dedicated to harmonization, namely the “Passport Steering Committee” and the “Intermediary Regulation Committee”. In another realm, Québec led the work on governance of controlled companies. It has also provided leadership in respect of derivatives, following Québec’s adoption of modern legislation for these instruments.

- However, if a province wants to have a particular measure, **there is room for local conditions**. Despite the high degree of regulatory harmonization in Canada there are still some differences among regions reflecting the peculiarities of the territories concerned. Accordingly, the provinces and territories continue to innovate and adopt “local” measures. For example, under instrument 31-103 on the registration requirements of representatives, Québec has chosen to retain the obligation to participate in the Fonds d’indemnisation des services financiers and maintain the requirement that representatives and firms purchase liability insurance, in particular given the desire to maintain a similar framework for representatives also engaged in insurance. Québec has also chosen to recognize as a self-regulatory organization in group savings the Chambre de la sécurité financière (CSF) rather than the Mutual Fund Dealers Association of Canada (MFDA) as was the case in the rest of Canada.

In addition, **the methods, approaches or cultures of regulatory organizations can sometimes differ significantly** and thereby be more or less favorable to certain types of development or experimentation. For example, Alberta’s regulatory approach is based largely on the needs of issuers and the market. It seeks to respond to requests made by issuers. British Columbia seeks to intervene as little as possible, particularly in governance and public offerings, and broadly promotes a principles-based approach. Ontario is very sensitive to the needs of banks and large financial institutions and seeks to adjust its proposals in terms of their potential response or requests. Québec seeks a balance between investor protection and market efficiency. Indeed, in 2004 the AMF decided to prioritize its activities to counter financial crimes. It is the only province that no longer favours administrative arrangements in order to send a clear enforcement message.

- These benefits underscore the importance of keeping the decision-making power of the regulator in Québec; this decision-making authority is directly related to economic issues in Québec, particularly when considering the vulnerability of Québec’s financial centre and the strengths that remain. Québec City and Montréal can currently count on but a small number of influential hubs and major institutions. However, **the AMF has paid great attention to the specific characteristics of Québec financial institutions and the development of financial activities in Québec**.
- **Sensitivity to the development of derivatives** is probably one of the best examples in this regard. It is important to bear in mind that this sub-sector is one of the niches of Montréal’s financial sector. Over 90% of the clientele of Montréal’s derivatives market is located outside Québec, with almost 70% in the U.S. and Europe. This reach is attributable to its products, its effectiveness and the recognized excellence of its operational platform. At the same time, the derivatives sector represents nearly 500 highly skilled jobs in the Montréal region, not counting the many others among the various suppliers of this sub-sector. Québec has also developed a high level of expertise in the management of payment and clearing systems in the field. This

activity also shows a high level of integration on site with intermediaries, customers, analysts, experts in support ... **And the Québec regulator was one of the key contributors to the development and dynamism of derivatives in the region:**

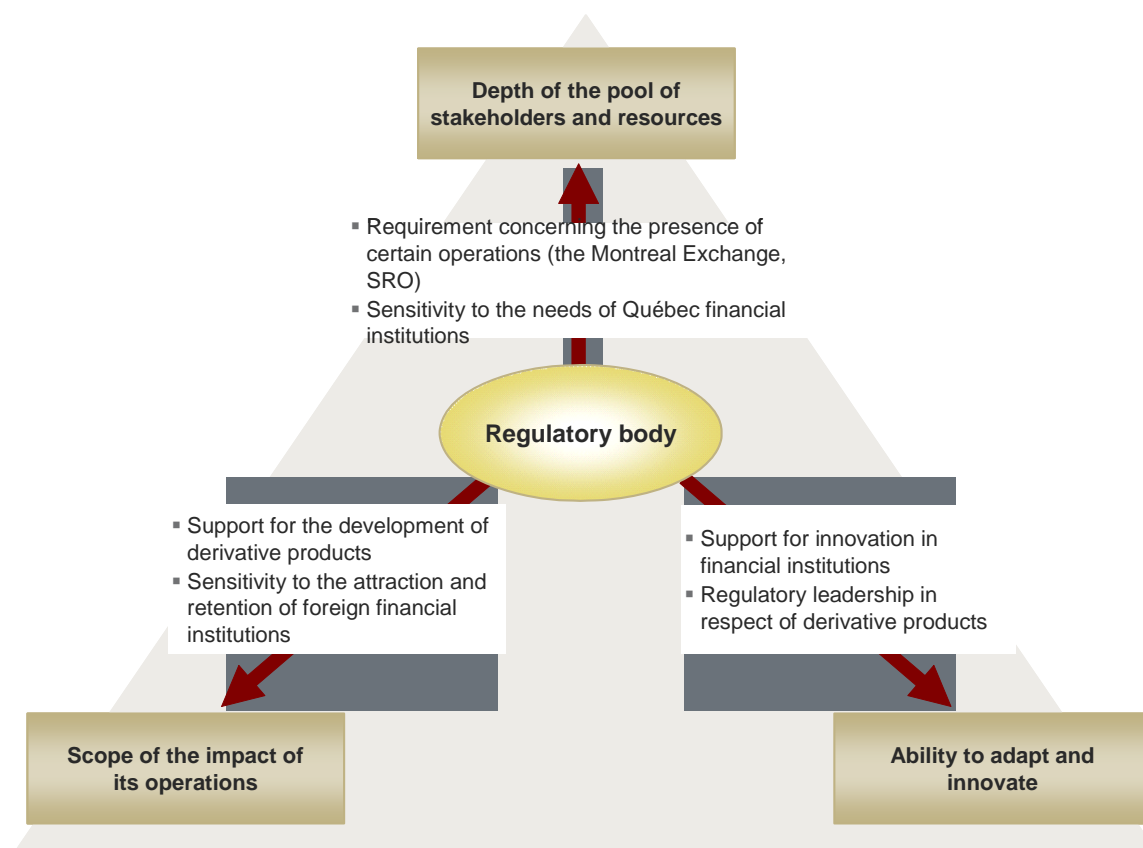
- First, Québec modernized its legislation and regulations faster than elsewhere and notably faster than the rest of Canada. Québec’s legislative and regulatory leadership has supported the development of the derivatives market while protecting stakeholders and ensuring competition among players. The quality and expertise of Québec’s regulator in this field is also acknowledged across Canada and even outside the country. The development and establishment in Montréal of companies specializing in derivatives would not have been as great without the leadership and expertise of Québec’s regulator.
- The AMF’s support for the development of derivatives, however, extended beyond mere legislation. Imposing certain conditions on the Toronto Stock Exchange in its merger with the Montreal Exchange helped bolster the sustainability of activities located in Montréal. These actions and decisions have been fundamental to Québec’s financial centre and its strategy of developing niches.
- **Sensitivity to the needs and specific characteristics of Québec financial institutions** is another example. This sensitivity can take different forms. For example,
 - The AMF adopted an approach that enabled Desjardins to efficiently access financing to recapitalize the group. As a result, over 450 credit unions were able to invest in permanent shares within a short period of time.
 - Development capital investment funds also benefited, in Québec, from greater openness to their concerns in the overhaul of their continuous disclosure obligations. In formulating the *Regulation respecting development capital investment fund continuous disclosure*, the Québec regulator has taken a different position than the rest of Canada to better reflect the reality of these funds.
- **Sensitivity to the attraction and retention of foreign financial institutions in Québec** is a third example.
 - In this regard, the AMF has guided foreign institutions so that they have a better understanding of Québec and Canadian regulatory matters, which was instrumental in bringing them to Québec. In particular, it has enabled the London Stock Exchange and Eurex to carry out activities here.
 - Québec is among the first jurisdictions to have proposed the deregulation of financial institutions to foster multidisciplinary and implementation of the concept of “integrated financial services”.
- The **requirements regarding the presence of certain activities in Québec** constitute a fourth example.
 - The AMF requires certain organizations to locate functions in Québec. For example, concerning these responsibilities with regard to self-regulatory organizations (SROs), the

AMF has asked that certain operating activities be carried out in Québec, whereas some SROs wanted to move them out of Québec.

Lastly, the **AMF works regularly with certain financial companies and their advisors**. Such regular exchanges are particularly important when these companies consider innovative structures or products. The AMF can better support innovation by the financial institutions it serves, in particular by setting out the regulatory issues ahead of time.

- For example, the AMF was the first Canadian securities regulatory authority to examine the question of market-linked notes. The AMF also broke new ground in Canada in its study of issues of covered bonds. In the latter case, the AMF not only managed to meet the issuer's requested timeframe, but also educated other Canadian securities regulatory authorities on important elements of covered bond issuance.
- The AMF maintains an ongoing dialogue with industry as part of formal meetings such as the *Rendez-vous with the AMF*. Moreover, as part of major reforms, including the implementation of regulation 31-103 respecting the registration reform, the AMF held several meetings to explain to industry representatives the implications of this new regulation. It also held consultations specific in Québec during the development phase of the regulation in view of certain specific Québec features (presence of the *Chambre de la sécurité financière*, the *Fonds d'indemnisation des services financiers*, complaint handling system).
- The following diagram summarizes some of the levers that have been used in recent years by the AMF to support Québec's financial sector; levers that are closely related to its influence and decision-making power.

THE THREE KEY DIMENSIONS OF A DYNAMIC FINANCIAL CENTRE AND EXAMPLES OF AMF CONTRIBUTIONS



- **The creation of a single commission will lead to a different attitude on the part of the regulator in relation to the development of Québec's financial centre.** On the one hand, distance will result in less sensitivity to Québec's needs and specific characteristics. The discussions that have taken place over the last few years on the harmonization of certain rules (for example, the *Regulation respecting development capital investment fund continuous disclosure*) are an initial indication of this. More fundamentally, a single securities commission may not favour one site over another, which in turn favors the one with the greatest natural attraction, i.e. Toronto.

LESS SENSITIVITY TO THE NEEDS OF ISSUERS IN QUÉBEC

- First, it is important to qualify strongly, and even to reject the major financial benefits for issuing companies that are often attributed to the establishment of a federal securities commission. The argument in favour of the single commission regularly posits that centralization of this authority will lead to:
 - increased access by Canadian and Québec companies to the securities market;
 - lower cost of capital for corporate issuers;

- reduced issuance costs for companies.
- This note does not address these items as they are covered in other recent studies. Nonetheless, we can mention the main findings:
 - Canada has performed very well in recent years in terms of new public offerings compared to other industrialized countries, whether for initial public offerings as a whole⁸ or offerings of “junior” companies.⁹ Access does not appear more restricted in Canada, quite the contrary.
 - The cost of capital in Canada is comparable to the United States when one considers the differences between the two countries in terms of the risk-free rate and the outlook for inflation.¹⁰
 - Canada compares favourably with the U.S. in terms of financial costs for initial public offerings.¹¹ Canada does not impose a heavier burden in terms of its costs of issues.
- Sensitivity to Québec’s special characteristics and needs applies not only to financial institutions but also to corporate issuers. On many occasions, the AMF has demonstrated an **ability to listen and collaborate in cases involving Québec corporate issuers**.
- Many of these cases required dealing with the regulator’s ultimate decision-makers and went beyond routine discussions with a regional branch. These examples include cases where:
 - **The speed of decision-making** was important to take advantage of available financing opportunities.
 - **The impact of certain rules** on groups of companies with particular characteristics. For example, the AMF has been sensitive to the situation of large family companies established in Québec in the current Canadian context.
- In some of these cases, the AMF **uses its decision-making flexibility** to better meet the needs of Québec businesses. In other cases, it **uses its influence** with other regulatory bodies to ensure that the real problems of Québec issuers are better taken into account in common rules.
- It should be noted that **Québec is not the only province where the regulator has tried to be responsive to the special needs** of companies within its territory. For example, Alberta and British Columbia in the past have also adjusted their regulations, made use of exemptions or excluded themselves from certain rules, such as Instrument 61-101 *Protection of Minority Shareholders in Special Transactions*.

⁸ See, for example, N. Cetorelli and S. Peristriani, “Prestigious Stock Exchanges: A Network Analysis of International Financial Centers”, Staff Report no. 384, Federal Reserve Bank of New York, August 2009.

⁹ See, for example, Carpentier, C. and J.M. Suret, “Proposal for a Single Securities Commission: Comments and Discussion”, CIRANO, Septembre 2009.

¹⁰ See, for example, Witmer, J. and L. Zorn, “Estimating and Comparing the Implied Cost of Equity for Canadian and U.S. Firms”, Bank of Canada Working Paper, No. 2007-48. As well as Zorn, L., “Estimating the Cost of Equity for Canadian and U.S. Firms”, Bank of Canada Review, Autumn 2007.

¹¹ See, for example, Koolie, M and J.M. Suret, “How Cost-Effective are Canadian IPO markets”, Canadian Investment Review 61 (1), 2003.

- To be able to react quickly or grasp certain peculiarities requires openness to dialogue and exchange, whether with leaders of regulated companies or their advisors. These exchanges can be ad hoc, as part of specific cases, or more systematic, with a view to improvement and sharing concerns. In this latter respect, the **AMF has developed formal communication channels that foster relations with key intermediaries in the industry**. It has three advisory committees: accounting, legal and investment funds. These committees help intermediaries better understand the regulator and better serve their customers.

A DECREASE IN ECONOMIC ACTIVITY IN QUÉBEC ARISING FROM THE REGULATORY FUNCTION

- The establishment of a single securities commission **would not mean the disappearance of all the activities currently conducted in Québec** by the Autorité des marchés financiers (AMF). On the one hand, some AMF activities are not affected by the regulatory responsibilities the pan-Canadian commission would be expected to assume. On the other, some local services would be needed, not to mention the need to offer services in French, which would maintain a basic level of activities in Québec. Beyond these local services, the more specific impact would depend on the type of organization implemented. Among single regulators in other countries, there are highly centralized models as well as more decentralized organizations.
- However, it can be assumed that **the commission's head office will not be in Montréal**. In fact, Toronto and the Ontario government are making significant efforts to secure this head office,¹² which confirms the strategic nature of the activities related to it. Moreover, we can assume that the more strategic major decisions will be made at head office, thus outside Québec. Indeed, this is the situation in all other single regulatory bodies.
- The establishment of a single securities commission to replace the equivalent functions of the AMF **would, at a minimum, mean the loss of head office activities** and even more if complete efficiency is sought for activities where the presence of economies of scale and critical mass exists.
- One can glimpse the initial level of economic impact because head office activities and those that must be near the seat of decision-making authority (i.e. head office support activities, regulatory activities and activities associated with compliance and prosecution) **in turn help stimulate many high-level professional services**. Over the past two years, the AMF has spent an average of \$10 million per year for professional services (legal, accounting, forensic accounting, computer ...). This item alone represents nearly 140 jobs, most of them highly skilled. And it does not take into account other operating expenses related to head office activities.
- Obviously, we are not talking of several hundred jobs. They are, however, well-paid and value-added jobs. **But also and above all, they are decision-making positions**. This latter notion is fundamental and is not unrelated to many of the economic issues arising from the establishment of a single securities commission.

¹² See, for example, the last Speech from the Throne in Ontario, March 2010.

- A head office or decision-making centre is a magnet of activity in itself. Proximity to decision-making centres is often a requirement for certain products or services purchased by head office. **This attraction effect is even greater for head offices of regulatory bodies.** Historically and still today, a broad range of stakeholders who are directly concerned by the regulated fields of activity are located close to the head offices of regulatory bodies. This is just as valid for regulatory bodies in the telecommunications and health fields as for finance.
- The stakeholders located near decision-making centres are not limited to suppliers of services to the regulatory body, but also include those representing the interests of organizations or businesses subject to regulation. **Choosing not to have a physical presence at the location of the headquarters of the regulatory body means running the risk of being deprived of essential relationships,** whence the regulatory centre's power of attraction.
- The creation of a single securities commission whose decision-making headquarters would be located outside Québec could **lead to a shift of these activities outside Québec, the departure of high value-added activities and ultimately the loss of expertise in Québec.**
- The loss of the decision-making headquarters clearly raises other even more fundamental economic issues that are related to decisions taken, which was covered in the previous two sections.

CONCLUSION

- The financial sector continues to occupy an intrinsically important place in the economy, especially in the economies of the developed nations. It also plays a key role in the allocation of resources for the development of other sectors of the economy. These contributions explain the efforts made in several regions to maintain or develop this field of business.
- However, Montréal's financial sector has been declining for a number of years. This decline has major consequences in terms of economic development. Yet Montréal's financial sector still enjoys a number of advantages and could become even more competitive both in Canada and internationally
- The presence of a financial regulator contributes to the financial sector's vitality and to the development of activities by implementing regulations that effectively balance consumer protection with the competitiveness of the businesses within its territory. Indeed, Québec's regulator has contributed to the expansion of some large Québec financial institutions and the growth of activities involving derivatives in Québec.
- A single securities commission would therefore harm Québec to the extent that Québec authorities would lose their decision-making power and influence over financial regulatory matters. Accordingly, a single commission
 - would not necessarily be as open and most definitely would not be as sensitive to the problems of Québec financial institutions or the challenges facing Québec's financial sector;
 - would not necessarily act as quickly and directly in support of Québec corporate issuers;
 - would mean a shift of expertise out of Québec, expertise concerning not just resources employed by the regulator, but also the external experts attracted by the presence of decision-making headquarters;
 - would represent a net loss of high-level jobs for Québec.