U.S. – Canadian Mutual Recognition

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Last week, the SEC announced that the Chairman of four Canadian securities regulators and Christopher Cox, the Chairman of the SEC, had agreed on a schedule for the completion of a process agreement for discussion of a potential U.S. – Canada mutual recognition arrangement. The process agreement is expected to be concluded in mid-June 2008.

Before considering the implications of this announcement, we should be clear about is happening here. The five regulators have agreed to agree to a schedule. Nothing is going to happen mid-June, other than making a plan for further discussions. Just what the world needs now – another roadmap.

Canadian securities regulation is at the provincial level; there is no federal regulation of securities in Canada. It is as if the blue sky laws were the only means by which securities are regulated in the United States. There are 13 provinces in Canada, and 13 independent securities regulators. The scheduling agreement will be with 5 out of 13. The release does not identify which five. For it to mean anything, Ontario, British Columbia and Quebec should be among the five. At best, this means that the scheduling agreement would resemble an agreement that Great Britain would form with the securities commissioners of New York, California, Massachusetts, Kansas and Texas. A useful enterprise perhaps, but not the significant global step forward touted by the SEC and the Canadian Securities Administrators.

The announcement is even more curious because the SEC already has a mutual recognition agreement with Canadian regulators. In 1988, Canadian regulators and the SEC agreed to assist each other in enforcement investigations. A quick scan of the SEC's recent enforcement docket suggests that our securities law enforcement folks play quite well with the Mounties. In 1990, the SEC and Canada's securities regulators put together a Multi-Jurisdictional Disclosure System or "MJDS." The MJDS permits U.S. issuers to sell securities in Canada using U.S. prospectuses and Canadian issuers to sell securities in the U.S. using Canadian prospectuses. Canadian issuers are permitted to provide annual and semi-annual disclosure to U.S. investors using Canadian forms, rather than Form 10-K, 10-Q and 8-K. MJDS went through some perturbations with the advent of Sarbanes-Oxley because Canadian issuers selling securities in the U.S. became subject to the same hated internal audit provisions that have been the subject of so much criticism by U.S. issuers and the financial press.

Setting aside the Sarbanes-Oxley kerfuffle, the fact remains that Canada and the United States successfully implemented a mutual recognition scheme almost two decades ago. This early success has not been repeated with any other jurisdiction.

The current process schedule will consist of a plan to hold discussions between the SEC and the four participating Canadian securities regulators. It is hoped by all and sundry that these discussions will result in a mutual recognition agreement that will permit Canadian brokers to sell securities to U.S. persons and U.S. brokers to sell securities to Canadian persons. The press release optimistically expresses the hope that "dual regulation, redundancy, and regulatory overlap could be eliminated."

Similar goals are often cited by the adherents of a one world government, one of those themes that emerged from the cruel ashes of World War II. The United Nations is the iconic symbol of that creed. But, it is a massive understatement to point out that the United Nations has been something of a disappointment to those who hoped the institution would forever end war and oppression on our planet.

I would submit that the United Nations has failed to achieve many of its most exalted aims because many people, and perhaps a majority of people, are fond of their own governments. I suppose this is just another way of saying that the populace generally is happy, or at least content, with dual regulation, redundancy and regulatory overlap. For one thing, dual regulation bears most heavily on outsiders, as it tends to protect the locals from competition. Moreover, local government, for all of its faults, is more responsive to citizen input that its larger cousins. There has never been a majority of the people of any nation that have seen enough of an advantage to one world government to support the abolition of their own national regimes. Even less ambitious efforts at unified regulation – the European Union, WTO and NAFTA – have faced strenuous opposition from many quarters. As a result, one world government is the stuff of fiction, of the futuristic kind.

For these reasons, it is difficult to understand what the SEC hopes to accomplish with the highly-touted Canadian mutual recognition regime. U.S. persons have no difficulty purchasing or selling Canadian securities. U.S. brokers can easily arrange these transactions. Due to our close relationship with Canada, it is not difficult for U.S. persons to open Canadian brokerage accounts. From time to time, U.S. brokerage firms have established a presence in Canada, sometimes profitably, sometimes not. But, I have never heard the expense of dual regulation cited as a reason for failure. I think most securities professionals think the Canadian securities regulators to be quite practical folk.

So, why are we doing this?