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A National Securities Regulator? – No way! says the Alberta Court of Appeal

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Cases Considered:
Reference Re Securities Act (Canada), 2011 ABCA 77

Can the federal government pass legislation to establish and empower a national securities regulator?

Essentially, this is the question referred by the Alberta Cabinet to the Alberta Court of Appeal. Specifically, the question relates to the draft *National Securities Act*, Sessional Paper No. 8 525-403-10. The *National Securities Act* would mean federal regulation of participants in the Canadian securities industry, federal disclosure rules and limits for raising money from the public, federal regulation of the trading of securities, and federal monitoring and enforcement of these rules to protect the public.

This question, the Alberta Court of Appeal answered with a resounding "No".

The Court's reasoning (per Justice Frans Slatter, with Justices Jean Côté, Carole Conrad, Keith Ritter, and Clifton O'Brien concurring) can be described in a word – OK, two words – "constitutional balance". It honed in on the idea that the proposed legislation would regulate exactly what provincial securities legislation regulates now and has traditionally regulated, with no evidence of fundamental problems. To permit this federal move into overall regulation of the Canadian securities industry would be an unprecedented expansion of federal constitutional jurisdiction over economic matters. It would be a tectonic shift in the essential constitutional division of legislative powers.

Why was this so obvious to the Court of Appeal? In this age of globalization, we are accustomed to hearing about the national economy and about investment and investment trends. Particularly since the financial markets crisis of 2008, we have been aware of the potential for broad disruption of capital markets – the risk of system meltdown. Indeed, this was how the federal government framed its argument in this *Reference*. Canada argued that a *National Securities Act* is fundamentally about addressing this "systemic risk" (at para. 7).

The problem with this, said the Court, is that the draft federal act contains nothing "concrete" about systemic risk (at para. 21). It does not focus primarily on dubious and irresponsible investment decisions that can create this kind of risk. Nor, the Court noted, does it "do anything that is not already being done (in a coordinated and cooperative way) at the provincial level" (at

para. 23). Securities regulation is not something that can only be done effectively at the national level (at para. 40). Nor does the legislation seek to regulate capital flows (at para. 25). The latter is done by the Bank of Canada – authorized specifically by federal jurisdiction over "Banking and Bills of Exchange".

What these systemic risk issues come down to, cautioned the Court, is regulating specific investment contracts. This is on-the-ground local activity that is the essence of provincial constitutional jurisdiction over "Property and Civil Rights in the Province", and not federal jurisdiction over "Regulation of Trade and Commerce".

The parties purported to agree that the pith and substance or leading feature of the proposed *National Securities Act* was regulation of participants in public capital markets and of transactions for the raising of capital. But they really did not agree. Each put a different spin on the *Act* that amounted to a different pith and substance. For the federal government it was "comprehensive national securities regulation" – investment risk and capital flows (at para. 17). The province saw the pith and substance as concerning investment transactions – fundraising and trading that occurs locally (at para. 19). The Court's implicit conclusion was that true pith and substance was closer to the provincial formulation (at para. 24).

The next step in the federalism analysis under the *Constitution Act 1867* is classification of the law in its pith and substance to the most appropriate federal or provincial power. Here, the Court concluded that the core of regulating the raising of investment funds is regulation of particular investment contracts. The securities traded are a form of property. In constitutional language, "civil rights" created by investment contracts and "property" represented by securities is involved – matters of property and civil rights that fit the exclusive provincial power over "Property and Civil Rights in the Province" (at para. 19).

This may involve some regulatory offences, in themselves classifiable as criminal law. But, said the Court, as a whole, the legislation is a response to economic, not criminal concerns. To support the pith and substance of the entire securities regime proposed as criminal l aw would be "constitutional bootstrapping" (at para. 32).

The federal government argued forcefully that the legislation is in relation to Regulation of Trade and Commerce. But the problem here is that this federal power has, since the Privy Council's decision in *Citizens' Insurance v. Parsons*, [1881] 7 App. Cas. 96, been interpreted as not extending to regulating contracts of a particular business or trade. This criterion was carried forward as one of the Supreme Court of Canada's five "indicia" in *General Motors v. City National Leasing*, [1989] 1 S.C.R. 641, of a matter coming within the "general" trade and commerce branch of the power.

The Court of Appeal concluded that the proposed national securities legislation does not meet three of these indicia: (1) It does not concern trade as a whole, but rather a particular industry – one involving a small number of businesses that raise money from the general public (at para. 40). (2) Nor are the provinces incapable of regulating this industry. They have, as the Court pointed out, been regulating it successfully for decades. The vehicle of general regulation is the "Passport" system that the provincial regulators have developed and agreed upon (at paras. 12,

40). (3) Exclusion of some provinces from the overall regime does not jeopardize its operation in other provinces. The fact that the proposed federal legislation involves provinces opting into the scheme supports this conclusion (at para. 40).

The Court's value laden phrases leap off the page: "long occupied by the provinces"; "does not meet the traditional tests"; "intrusion" of the federal government; "area long occupied by the provincial government's 'local powers'"; "local diversity"; promotion of "local interests"; "paradigm shift"; "reallocate" (at paras. 47, 48). Theories are not difficult to divine: the constitutional compact fosters and guarantees local autonomy. Perhaps, though unmentioned, there are wisps of subsidiarity in the Court's decision – the idea, dusted off by members of the Supreme Court in the December 2010 *Assisted Human Reproduction Act Reference,* (2010 SCC 61, para 183 per Lebel and Deschamps JJ), that decisions are to be taken by governments closest to concerned citizens.

So, the suspense deepens. Similar References are before the Quebec Court of Appeal and the Supreme Court of Canada. Ultimately, of course, the Supreme Court will rule. Meanwhile this is the first shot – the Western shot – in the national securities regulation legal battle.