



Stop the insanity

Why is it that Canadian investors repeatedly accept inept securities regulation?

It was either Benjamin Franklin or Albert Einstein who supposedly said that the definition of insanity was doing the same thing over and over again and expecting a different result. But it doesn't take a worldly diplomat or nuclear scientist to see that many Canadian investors are badly in need of psychiatric help. Why do they repeatedly accept inept securities regulation?

Canadians are routinely being delivered weak responses to serious regulatory problems in our capital markets. Typically, made-in-Canada versions of tougher U.S. standards amount to little, if any, gain for investors. Indeed, many read like they were crafted by the wrongdoers, because those are the parties from whom the regulators primarily take their marching orders.

About a month ago, the Canadian Securities Administrators (the umbrella organization of the provincial securities regulators) delivered another kick to the groin of Canadian investors. This decision, concerning company internal control reporting, can be added to the long list of standing insults covered in some of my previous columns. The new proposal by the CSA would require all publicly traded companies in Canadian jurisdictions to report on the effectiveness of their internal controls over financial reporting, as early as Dec. 31, 2007. The accompanying press release read: "After extensive consultation, the CSA has decided not to proceed with an earlier proposal that would have required companies to obtain from their external auditors an audit opinion in respect of management's evaluation of the effectiveness of internal controls over financial reporting."

Phew! The "consultation," of course, was mainly with public companies that eagerly trotted out eye-popping estimates of what these external audits (preferably not by shareholders' auditors) would cost. Not one of those companies publicly opined about the benefits of such an investment.


What would the benefits have been to have Nortel's internal controls checked in 1997-99, and modified to eliminate any malfeasance? I would estimate it to be somewhere north of \$100 billion. And that's just one company. If we spread that benefit over all public companies in Canada, it more than covers even the wildest cost estimates.

There are three major problems with the regulators primarily consulting only the companies on the need for internal control



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Once again, another made-in-Canada securities solution boils down to nothing more than a public relations exercise. Management becomes responsible for grading its own performance. A bogus internal control certification might help to pinpoint management culprits after investors have already lost another boatload of money. However, it is far from proactive in helping to prevent such fallouts.

Indeed, certifications seem even more worthless given the fact that our regulators have such a weak history of prosecuting capital markets scams, and in light of the fact that we don't have a tough class-action bar in Canada. It seems that we have sunk into widespread collective delusions; the reality is that our markets are extensively one-sided against small investors. Therefore, what is required capital-markets practice in the United States has once again been laughed off by Canadian regulators as being unnecessary. Apparently, we are either much more honest people than Americans, or we just choose to think we are. 

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