How adding regulations may reduce the regulatory burden

By Kevin Thomas
March 11, 2019 – *The Globe and Mail*

How can adding new regulations reduce the regulatory burden?

Simple. Picture what happens whenever a traffic light goes out of service at a busy intersection. Each car that approaches the intersection has to navigate uncertainty, unsure whether to proceed or stop, and traffic slows to a crawl as individuals try to guess how other drivers and pedestrians are going to act. What was a relatively smooth and efficient system has now become cumbersome and slow.

Not because we added regulation, but because we removed it.

Adding a traffic light at a busy intersection actually increases efficiency and reduces everyone's burden.

That's why we should be wary of simplistic and unspecific calls to remove a "regulatory burden." Regulations can certainly create burdens, but they can also remove them.

Efficient and productive capital markets are seldom created by dismantling institutions and rules, but by thoughtful construction and oversight of rules and institutions that facilitate transparent market interactions. A crude approach to regulatory reform – such as the overly simplistic idea of removing two regulations for every one that is created – generates uncertainty rather than efficient markets and sustainable, inclusive and productive economies.

The Ontario Securities Commission, for example, has just concluded public consultations on the "regulatory burden" of existing securities laws. Constructed over decades, the existing framework of laws and regulations that apply to listed companies in Canadian capital markets aren't perfect, and may create burdens for some issuers. On the other hand, let's be clear: they've also created a system that helps to protect investors and eliminate many inefficiencies that would otherwise exist in a less-regulated marketplace. They've prevented the shifting of burdens onto other stakeholders that are best shouldered by the issuers themselves.

This is particularly true of our Canadian continuous disclosure regime. Comprehensive, consistent, comparable, cost-effective and timely disclosure of information by issuers is critical for investor confidence and therefore capital formation.

In fact, in the current environment, the best way to reduce the regulatory burden on corporate issuers is actually to increase regulated disclosure, not reduce it.

In 2018, our organization engaged with 87 TSX-listed issuers on behalf of our institutional investor clients, and we were also approached by additional issuers seeking our guidance on appropriate decision-relevant disclosure of environmental, social and governance (ESG) information. Due to the nature of our stewardship work for institutional investors, we are often at the intersection between issuer and investor views on ESG oversight, policy, performance and disclosure.

Like those cars at the unregulated intersection, a message we have heard far too often in those exchanges is one of confusion and uncertainty.

Issuers are being asked to respond to too many disparate systems, surveys and requests for information, and investors are receiving contradictory, unclear and incomparable information from issuers that is unusable for efficient decision-making on their part. Multiple and sometimes contradictory voluntary frameworks for reporting of ESG information have sprung up, either developed

by investors and investor-focused institutions or service providers, or by issuers, trade associations and other institutions.

These initiatives and approaches have arisen because there is no regulated framework for reporting ESG information in Canada. Absent a comprehensive, consistent, comparable and cost-effective reporting framework, the accountability of issuers to their share owners and other stakeholders for corporate performance and good governance is undermined, and each Canadian issuer is left with the burden of navigating this maze of standards.

In order to reduce the real burden for Canadian issuers, Canadian securities administrators should therefore take steps to develop new regulations that answer the need for a comprehensive, consistent, comparable and cost-effective ESG disclosure regime, including disclosure of the board's processes for identifying, assessing and managing salient environmental, social and systemic risks, management's role in assessing and managing risks, and how these processes are integrated into overall risk management.

While these additions to disclosure rules will add to the regulatory requirements expected of issuers, they will effectively reduce the practical burden on issuers by creating a common and reliable disclosure framework rather than the piecemeal approach that dominates Canadian markets today.

Disclosure, including ESG disclosure, is now a part of navigating Canadian capital markets, and it's time we acknowledged its role by setting up a few traffic lights.

Kevin Thomas is executive director of the Shareholder Association for Research and Education (SHARE), a Canadian leader in responsible investment services, research and education for institutional investors.