

The Role of Ethics in a Fair, Efficiency and Effective Marketplace

**Remarks made to:
The Canadian Centre for Ethics & Corporate Policy
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*Barbara Stymiest, President, Toronto Stock Exchange***

Good (afternoon) ladies and gentlemen. I'm happy to be here today, to talk about a subject that is – in a very real sense – at the core of what we are all about at the TSE.

As you may be aware, this is a particularly significant point in history for us. We are about to take a major step at the TSE. We are – in the parlance of the lawmakers – about to demutualize. As soon as the provincial government makes it official, we will no longer be a non-profit organization owned by our members. We will be a for-profit business – completing the process that our members voted in support of last summer. Our new governance structure will not only help us to be more competitive, but it will also give us the ability to respond more effectively to the needs of our customers.

This is an exciting and important time for the TSE and its customers. Demutualization will give us greater opportunity to work, to grow, to prosper and ... to become successful together.

Now, I'd like to pose a question: What do you think makes a stock exchange "successful"? I suspect that some of you might assume the answer lies behind the numbers. The number of trades. The number of listings. The market capitalization of the listed companies.

Of course, these are all-important indicators. But this is much more than a numbers game.

The key to success for the Toronto Stock Exchange is the same key that makes most businesses and people successful – our reputation. Who we are, in the eyes of Canadians and in the eyes of the rest of the world. As a stock exchange, our reputation is built on the quality and integrity of our marketplace.

Our reputation is as good as:

- our ability to attract quality companies;
- our ability to ensure that investors have equal access to these companies;
- our ability to sustain a liquid market; and,
- our ability to provide a trading environment that is reliable, efficient and cost-effective.

The reputation of our market – as fair and honest – is our most precious asset. It is our only true capital. We all know the cliché about reputation. About how difficult it is to recapture once it is lost. This is as true for institutions as it is for individuals.

Stock markets are built – and sustained – on a foundation of public trust and confidence. That is why we take great care to protect our reputation... to ensure that it is kept strong for all of our stakeholders and soon, our shareholders

Investing is always based on the balance – or imbalance – between risks and rewards. When investors buy and sell stocks, they are taking a calculated risk on the future profitability of the company they are investing in. They make their investments based on a belief – a faith, perhaps – that someone has already made sure that the company is sound. And that's our job: to ensure that stocks listed and traded on our market are worthy of investors' trust. Regardless of a particular company's long term success or failure, it's up to us to do the due diligence necessary to ensure they qualify for a listing in the first place.

When investors trade in a stock, they also want to know that they are getting the best possible price. That requires participation from other investors – the more the better. This will only happen if all investors feel they are treated fairly and equitably. Otherwise, they'll take their business elsewhere. So will the listed companies that depend on them.

This is a significant challenge... and a tremendous responsibility.

Which is why – because it is fundamental to our reputation – we take our regulatory role so seriously.

For us, regulation is far more than just being a good cop. Market regulation means being a good facilitator. A strong partner. It means that we will provide counsel and direction to companies listed on the exchange to help them stay in business and grow. We are partners in their success.. .

At times, that means we are helping to find the best way for a company to get a deal done.

At other times, we help them solve a problem or manage a difficult situation.

Let me offer one example:

When Ballard Power Systems agreed to a strategic alliance with Daimler Chrysler they were looking at a rather unusual and complex financial structure. It was one that clearly tested our rules. Here's what Ballard Power's Vice President Strategic Development, Noorden Nanji, said to us after the company called us in to help: "In a relatively short time, TSE staff understood the structure and purpose and showed a lot of flexibility in determining how the rules should apply. Their genuine interest allowed us to get the transactions done in a way that made good business sense." Mr. Nanji added one more comment. He said, "The TSE also made it very clear to us where the boundaries were and the rationale behind them." So our role is both as a facilitator... and a cop. It's a dual role that aims both to support the market... and to protect it.

All of us – all of our listed companies, all of the securities firms and individual traders, and all investors – benefit from the TSE being the best it can be.

The TSE already plays a far greater role in this country than many Canadians realize. The TSE facilitates growth and success for business, creates jobs for our economy as well as wealth and economic security for millions of individual Canadians.

The total market capitalization of companies listed on the TSE is \$1.5 trillion and our domestic companies represent \$1.1 trillion of that amount. As a percentage of Canada's GDP, our domestic market capitalization is equal to 120% percent of the total annual economy. Our companies are worth more than what our country produces as a nation on an annual basis.

Strong economies and markets create an environment of strong growth. Look at the technology sector as one example. We are increasingly dealing with "the new economy", with knowledge-based companies that bring both real excitement and a clear challenge to the TSE.

Because we have a healthy market, we are able to attract cutting edge companies. In the past five years, the technology component of the TSE 300 has more than quadrupled to 24%. Today, the TSE has over 140 high tech companies with a combined market-capitalization of \$275 billion. To name just a few examples, look at ATI Technologies, Open Text, Vasogen and Ballard Power Systems which I mentioned a moment ago. Many of these companies did not exist a decade ago. Without a strong, visible, liquid and efficient Canadian stock exchange, The majority of these companies would not have:

- access to effective and efficient sources of capital,
- they wouldn't have created jobs here,
- wouldn't have grown, and
- they wouldn't have contributed either revenues or taxes to the economy

Our support doesn't stop there. We are committed to listing on the TSE a positive experience. Like our listed companies, that continually reassess themselves relative to their markets, the TSE is also subject to the same, on-going self - scrutiny. That's why we constantly review our listing standards. Our original listing standards were last updated only 18 months ago and our continued listing standings were revised in 1999. We are looking at them again.

When a manufacturer or a financial services company wants to be listed, we can follow a well-worn and relatively straightforward path to assess whether they meet our listing standards. It's not dissimilar to the old banking model that evaluated companies on revenues plus "bricks and mortar" measures. But how do you evaluate brand-new, potentially break-through intellectual property? How do you put a market value on proprietary technology?

We will continue to ensure that our standards evolve to keep pace with our customers' needs. This includes the recognition of the special circumstances of companies that fall into this new and tremendously important sector.

We also are – as we must be – open to change in our traditional industry sectors. When concerns were raised about the mining sector, the TSE launched an in-depth probe into the regulation of the resources industry. The result was our widely acclaimed Mining Standards Task Force Report that was published in 1999. The Report provided a comprehensive study that included 66 recommendations – smart and innovative solutions to the fundamental challenges of assessing prospective listings for mining companies.

I am pleased to report that 30 of the recommendations have already been adopted in the Canadian market. The others are expected to soon follow suit. Perhaps more significant is that the task force's recommendations are being reviewed and adopted globally as well. Our leadership has been recognized...

The Mining Standards Task Force also opened the door for the TSE and other industry participants to establish guidelines that would clarify the role and process to be followed by research analysts in the industry. The Analysts Study, like its predecessor the Mining Standards Task Force, is aimed at both strengthening the industry and protecting investors. This work is underway right now and we expect to publish that report later this year.

In a nutshell, our job, as a regulator, is to ensure that everyone plays by the rules; and that the rules evolve to keep pace with change in the market. At the same time we cannot lose sight of our primary objective – a fair and equitable market.

This can only be accomplished if we provide the high quality service that attracts high quality companies.

Of course, earning a new listing is just the beginning. Once a company is listed on the TSE, our staff keeps a close eye on its progress, watching every material change. Along the way, we provide advice and guidance whenever we can.

Our market surveillance team constantly monitors all of the nearly 1,500 companies listed on the TSE. They are looking for unusual trading prices or volumes that might possibly indicate a problem. Not so long ago, this was a tedious manual job. But with new technology, we've honed it to a sophisticated, computer-driven activity using a program called Intelligent Market Monitor. We have a surveillance team comprised of highly experienced professionals. They monitor all of the activity around the trading of our listed companies' shares, tracking the activity and patterns for every one of the more than 162,000 trades made every day. That is a number that continues to climb.

When there is a significant change in a company's value or trading volumes but no news to support it, we immediately contact the company for an explanation. It wouldn't make any sense, nor would it be in anyone's best interest, to automatically halt trading on every

one of the 400 or so alerts we see every day. That would defeat the purpose of a free market.

In fact, most of the time, price or volume swings reflect routine news like recent earnings or a new analyst report. If the company has properly disseminated the news on the disclosure wires, everything is fine. Sometimes though, we see indications that word may have leaked out about something that could have serious impact on a stock's value, but which was only known by a few insiders. It might be negotiations concerning a merger or acquisition. It could be drilling results or a change in management. When this happens, we require the company to issue an immediate release so that everyone can have access to the most current information.

There have been several stories in the media lately about this very issue: proper disclosure. Timely and accurate disclosure is central to our ability to sustain a quality market and is the cornerstone of our regulatory policy. The rules are very clear on this point: Whenever a listed company has news that may be material to investors, they are expected to inform our surveillance team. This is the company's responsibility. We have to rely on management's judgement and sense of accountability to their shareholders to report news and to prevent people who could use it to their advantage in the market. This news must be provided to us – and the market- immediately.

It is really a joint effort. Our job is to provide advice on the contents of any press release and to help determine whether a "halt-trading" order is necessary to allow for fair dissemination of the news. We will do whatever we can to ensure that level playing field for all participants in this equation – investors, issuers and the trading community.

Most of the time, this surveillance and disclosure system works smoothly. Sometimes though, when neither the company nor its registered trader can explain the unusual trading activity, we call in our investigation team. They try to establish whether there is preliminary evidence of either artificial manipulation of the stock price or the breach of timely disclosure rules. Both are potentially very serious violations. Our investigators are the real "cops" in the system. They analyze every suspicious trade and speak with every person involved in these trades. They will even go beyond our jurisdictional and national boundaries... whatever it takes to peel back the layers that will reveal the facts and the truth.

And if they confirm that someone has not played by the rules, then the case is referred to enforcers at either the TSE or the Ontario Securities Commission. .

Of course, none of us wants things to get this far. We would rather the abuses were prevented in the first place. Our best defense against includes education and intelligent counsel. But reality is that there will always be a few who try to beat the system and bend the rules. Chances are, they will be caught. Why? Simply put, we have the technical and practical expertise to recognize when the market is not behaving as it should.

Broadly speaking, we approach our "dual" roles of facilitator and cop by having two distinct groups, within the TSE, that deal with companies. Between these groups there exists what we call a "Chinese Wall". This wall ensures that there are no breaches of confidentiality from one side of our business to the other. It protects us, and those we are here to serve and protect, from conflicts of issue.

On the one side of the wall is our regulatory and surveillance team. They are charged with protecting investors and the quality of the market. On the other side of the wall – standing quite distinctly – are the business development and relationship management teams. So, how are we doing at striking this balance? To go back to what I said at the outset, I believe the numbers tell the story.

As well as being Canada's sole senior equity market, the TSE is also among the best-respected exchanges world - wide:

- we rank 7th in the world by domestic market capitalization ;
- our total market capitalization - \$1.5 trillion – is more that double what it was five years ago,
- for seven consecutive years, we have broken the record for the total dollar value of all shares traded - representing a 236 per cent increase in total value of all shares since 1993,
- in 1999, our trading value was \$530 Billion and we set at least seven - seven seems to be our lucky number -major growth records in areas such as daily volume, daily transactions, monthly volumes and record high closes -all factors that contribute to strong liquidity, and in 1999, the TSE 300 index - for the first time since 1993 - outperformed the Standard and Poors 500 - and we did so by an impressive 10 per cent.

The health and continued growth of this market is a tribute to the strength of the companies listed here and the market they trade in. We are determined to support them all by ensuring we continue to operate a well-regulated market that meets the highest standards in the world... an ethical market, a market that makes us all proud. Thank you.