Pots and Kettles: Governance Practices of the Ontario Securities Commission

by

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Abstract

An analysis of the governance policies of the Ontario Securities Commission (OSC) is undertaken in light of that institution's drive to improve governance practices in the private sector. It turns out that the Commission itself does not practice many of the governance practices required and/or advocated for the corporate sector. Furthermore it is argued that governance policies necessary to resolve the principal – agent problem for the corporate sector are necessary to resolve that problem for a public sector regulator, but they are not sufficient. This is the result of the greater difficulty in monitoring the regulator because the objectives of the principals/electorate are more difficult to measure than profits, and those objectives are only loosely correlated with cash flows. The insistence on publicly available cost-benefit analyses for new and existing OSC initiatives is one method to improve monitoring.

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Pots and Kettles

1. Introduction

Good corporate governance practices have been much in the news because of both the recent corporate scandals in the U.S., and the collapse of the technology bubble. In the U.S, the apparent breakdown of corporate governance has led the SEC, Congress and some states to initiate new regulations and procedures to enforce their version of good governance on corporations listed on US exchanges. For whatever reason, Canadian regulators also appear ready to impose new regulations and laws in Canada along virtually the same lines as those in the U. S.[1]

The practices that have come to light over the last five years have indeed been major violations of the principal – agent relationship between shareholders and the management of the principals' firms: accounting standards have been violated (Enron and WorldCom); proper auditing procedures apparently have been bypassed (Enron and its auditor, Anderson); the absence of transparency and the toleration of conflict of interest seems to be rife in the industry with a notable case being the breaching of the supposed Chinese wall between sell side analysts and investment bankers. Finally, the outright looting of the firm by members of management seems to be at the heart of a number of cases (Tyco).

Despite the fact that most managements are honest and keep the principals' interests uppermost in carrying out their actions, the actions of those that have not has caused this rush to more intrusive and costly regulation. Even if these regulations will increase costs of operating the firm and reduce the welfare of most principals, regulators seem to believe that, despite this, the benefits outweigh the costs of doing so. In particular, it is argued that something is needed to restore confidence to investors, and appearance matters almost as much as the effectiveness of the new regulations. Consequently all firms will be required to follow new rules instituted because of these rare, but spectacular, U.S. corporate scandals.

Appearance may, indeed, be important in the United States where these scandals have occurred. It is more problematical in Canada, which has been relatively free of governance scandals despite darkly hinted rumors that they simply have not yet been exposed. Publicly traded Canadian firms may, in fact, have sufficiently good governance practices that new regulations on these practices simply impose greater costs on the private sector while conferring little, if any, benefit. If that is the case, then it may be useful to reexamine the role financial regulation is expected to play in society and especially reconsider the regulators' own "governance structure" to determine whether or not they are providing leadership through their own governance procedures, or if there is more than a hint of hypocrisy in their admonitions. In this note I wish to do this and, in particular, apply some basic concepts of corporate governance to the primary regulatory body of security markets in Canada, namely the Ontario Securities Commission. While

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[1] C.f. OSC (2003a).

other financial regulators have similar governance issues, the OSC appears to be an extreme.[2]

In assessing OSC governance, I consider two aspects: their formal governance structure and modifications that may be necessary for government agencies to meet the basic standards provided in the private sector. In the next section I provide a brief review of the principal – agent problem for government. Section 3 provides a review and critique of OSC governance since 1997 in meeting those requirements, as well as comparing their own practices with what they require of the private sector. In section 4 I examine alternative mechanisms that might improve governance practices and section 5 concludes.

2. The Government's Principal – Agent Problem

The principal-agent problem for the private sector is well known: the owner/principal delegates to a manager/agent the responsibility to provide some services for the principal. The problem is one of structuring contracts and institutions to insure that, in carrying out her duties, the agent acts in the principal's interest rather than her own.

Citizens of a country also face a principal – agent problem. Citizens "own" the machinery of government and employ bureaucrats to act as their agents in running this machinery. To reduce the costs of monitoring, the principals choose a legislature/board of directors to oversee the agents. Monitoring mechanisms are similar to those in the private sector: there are financial accounting standards that are met for each budgetary unit, and an external auditor checks these internal accounts. Transparency is maintained, in part, through freedom of information regulations. Compliance with procedures and other regulations are met both through internal monitoring and checks by units external to the bureau. Finally, contracts are structured, at least in a limited manner, to align the incentives for agents with those of the principals.

There is, however, an additional problem in the public sector that does not exist for private firms. The firm has a well defined objective function – the maximization of profits – whereas the apparent objective for the government is the maximization of some index of a (weighted) level of welfare of the electorate. An unambiguous index of social welfare has been impossible to construct and, in its absence, monitoring the public sector is further complicated because data is generally lacking on whether or not the objective was actually approached and/or achieved and what the costs are that are linked to any specific objective. In effect, because of distribution issues and public goods, the cash flows measured with traditional accounting procedures will be, at best, only superficially correlated with that objective. Thus, looking at cash flows will provide the principals an extremely poor method of monitoring their public sector agents.

Most governments are aware of this and, in some cases, have determined that traditional accounting systems must be augmented by some method of cost – benefit analysis. At least as far back as the 1960s Canada has tried to develop an operational method to

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[2] Cf. Chant and Mohindra (2001) or Mohindra (2002).

provide at least an approximate, quantifiable, measure for evaluating government programs.[3] In essence, the use of cost-benefit analysis played an increasingly important role in providing such a method. However, while preprogram cost-benefit is fairly regularly used, the follow up of a post program assessment is rarely undertaken in any meaningful sense unless the Auditor General's office decided to address the issue.

Regulatory agencies, especially when structured as crown corporations, are potentially more difficult to provide legislative oversight. This is because these bodies often exist because the legislative branch believed that the policies were too complex and/or the area of operations too quickly changing to leave to the legislative process. In particular the financial regulator tends to have an objective that is broadly defined and allows the agency to determine for itself the specific elements necessary to achieve that objective. Furthermore, in many cases, the agency has the ability to set rates and generate revenue outside the budgetary process. Relative to other budgetary units this provides it even greater leeway from the oversight of the legislature. Nonetheless, it remains an agent for citizens of the state and if it is less directly monitored than other units then it is incumbent that it put governance practices in place to ensure that the principal – agent problem can be favorably resolved. Because the OSC is the Canadian agency most concerned about governance practices in the private sector, it is useful to examine that institution as an example of governance of a regulatory body. It is to this examination I now turn.

3. OSC Governance Practices

The Board

Prior to 1997 the OSC was a part of the Ministry of Finance of Ontario. In that year they became a crown corporation. The corporation is composed of 9 commissioners plus the staff. The commissioners are the ones that set policy, and adjudicate cases brought before them by the OSC staff. The board of directors is also composed solely of the commissioners themselves. As such, they constitute the full membership of both the audit and the compensation committees.

The nature of board membership of the OSC is in sharp contrast to recent requirements imposed on the private sector where the use of independent directors for private corporations has taken on special importance. It has been argued that these directors will better represent shareholders and keep management under control.[4] Sarbanes –Oxley (SOX) requires a substantial proportion of directors be "independent". In Canada, the OSC (2003a) has pushed strongly for independent audit committees arguing that it would increase the economic value added of those companies by between one and nine billion dollars. The argument is that, by having independent audit committees, boards would be less likely to put a better face on the results of the corporation. As a result, recent regulations require that all firms listed on the Toronto Stock Exchange require a majority of independent directors on the audit and compensation committees. Other publicly

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[3] See Sutherland (1990) for an assessment of Canadian developments in program budgeting.

[4] See OSC (2004) for governance practices proposed by the OSC.

traded corporations that have not met the independence requirements are required to report why they have not met the "voluntary regulations" on board membership.

Because all commissioners are involved in both administrative and adjudication activities within the OSC, there is, at least in the context of the current debate, some question as to the quality of the leadership role the OSC is playing in demanding increased independent board membership for private corporations, Indeed, a similar argument can also be levied against the OSC. Because all audit committee members are involved in the operations of the Commission, from putting regulations in place to adjudicating, they have every incentive to place a favorable spin on the operation of their corporation. Perhaps fortunately, the bulk of the commissioners are lawyers who are acting as humble civil servants and thus would be fully forthcoming if there were any material errors in the financial accounts of the Commission.

Despite the absence of external directors on the compensation committee, the OSC appears to believe they are also above reproach in deciding the compensation of other board members with similar responsibilities as themselves.[5] On the other hand, a cynic could suggest that this represents a conflict of interest of the crudest type. Certainly, in the private sector, regulators have defined anyone who has worked in the firm within the last three years a non-independent director. An OSC commissioner who is *currently* involved in both policy initiatives and adjudication at the OSC is unlikely to meet the perception that they are independent. The actions of the compensation committee also do not lend much credence to that committee's restraint in establishing salary levels. Prior to incorporation, civil service pay scales were in effect. With the founding of the corporation, such restrictions were removed and salaries surged. For instance, in 1997, only seven members of the OSC earned more than $100,000; by 2004, 137 were making that amount or more. More telling perhaps is that, using compensation consultants and the "independent" compensation committee, David Brown, the Commission head, received more than two and one half times as much as the head of the U.S. Securities and Exchange Commission.[6]

Oversight

Prior to incorporation, the OSC budget was determined by the legislature rather than from internally generated registration fees and fines. The 1997 enabling legislation freed them from this financial control of the legislature and they were free to set fee schedules as they saw fit. Any revenue generated that is over and above the cost of running the Commission is to be remitted to the general accounts of the provincial government. This

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[5] The "independence" of the Commission is presumably assured because only part time commissioners-who are involved in policy making and adjudicating-can be on this committee.

[6] See Chant and Mohindra (2001), p.34. This is not to say that the OSC chair is overpaid. Yet it is worth noting that Canadian financial regulators have been virtually the only group in the entire Canadian economy where the compensation is greater than their U. S. counterpart.

financial freedom has also significantly reduced the ability of the government to exercise oversight.

What formal oversight that remains is in the domain of the Minister of Finance.[7] The OSC must report to the minister at least once a year, indicating past undertakings and future priorities. The minister can require the Commission to address specific issues, reorder priorities, and the like. Nonetheless, relative to other countries, there are surprisingly few venues where critical assessments of the securities regulator can be undertaken.[8] In the US the SEC must report to legislative committees where there are members of both political parties. Australia and the UK both have strong oversight mechanisms. Even some smaller provinces have legislative committees composed of members of all parties that oversee crown corporations, including the securities regulator. Compared to those, the OSC Board can initiate a committee to assess the actions of the commission itself, but this committee reports directly to the Board and was last active in 1988. The other venue appears to be the 5 year review where the recommendations go to the provincial Standing Committee on Finance and Economic Affairs.

Accounting

Given the absence of any significant degree of oversight by the provincial government there are at least two other means of monitoring by the electorate. The first is to trust to the good offices of those in control of the Commission and pray they behave honorably. While this may well be adequate, it is hardly the response that the regulator itself would demand of a private sector corporation. Rather, the financial regulator would require that there be sufficient information – prospectus, quarterly reports, auditor's reports, etc. – made available to allow the shareholders to make informed decisions and backed up by the force of law. In effect, the firm is required to have a degree of transparency and be vulnerable to lawsuit if information is misleading and/or incorrect. Requiring a similar level of transparency of the regulatory process is thus a second means to provide some oversight, and further, would be consistent with the OSC mandate in regulating private firms.

The most essential element in providing the necessary transparency and reducing the costs of monitoring any institution is that there be some well defined set of rules with which to assess its performance, i.e., a method of accounting. The OSC uses generally accepted accounting principles (GAAP) in assessing the financial flows through the organization, as well as providing an annual audit of the books. As indicated earlier, the problem for government agencies is that these accounts serve the private sector well but are seriously deficient for the purpose of evaluating government programs. For a government bureau or ministry, it is net benefits from mandated programs rather than profits that are the objective. While cost-benefit analysis is certainly not a panacea, - benefits and costs may well be ambiguous and/or poorly measured, - it does provide *some* method with which to assess programs and has therefore played an increasing role in the

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[7] See OSC (2003c).

[8] See Mohindra (2002) for an excellent comparison of oversight of financial regulators in Ontario, the US, the UK, Australia and Hong Kong.

conduct and evaluation of policy.[9] Both the elected representatives and members of the public can then use these estimates to assess both the programs and their agents – both the members of the legislature and the civil servants – and can respond in their own best interest.[10]

For a regular government bureau, those who ultimately assess and initiate the cost-benefit analysis of a program are elected representatives who have an incentive – reelection – to get things correct; for a regulatory agency such as the OSC the costs and benefits are evaluated by non-elected officials and the incentives to do the right thing are less powerful. Indeed, it can be argued that it is not in the regulator's interest to provide transparent accounts of costs and benefits. For instance, in the absence of accounts, it is a fairly simple matter for the agent to take credit for any positive outcomes and avoid blame for negative ones.[11] Also, without transparency there is a tendency to formulate ambiguous regulations since such obfuscations limit the ability of outsiders to properly evaluate the regulator. In the case of the OSC, this absence of transparency is suggested by the charge of "acting against the public interest" which is only defined *ex post* if at all.

Given the asymmetric information in conducting policies, what monitoring there is will be ineffectual without some accounting mechanism. Indeed, a major theme for financial regulation that the Crawford Commission[12] identifies is that:

> "Regulation should support clearly identified public policy objectives and be proportionate to the objective. The benefits of regulation (and changes to regulation) must outweigh the costs imposed by it." [13]

The OSC has, in fact, been required to provide such an analysis under current legislation but the Crawford Commission notes that what the OSC has done is best described as "boilerplate". For instance statements on costs and benefits often end with such generalities as "based on experience to date, the [Ontario Securities] Commission believes that the benefits of the proposed rule justify the costs".[14] This is qualitatively the same as a firm's management telling its shareholders that everything it did was profitable – costs were less than revenue in every endeavor – but they didn't keep any books to confirm that assertion. Such a firm simply could not be publicly traded in Ontario.

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[9] Presumably, legislative committees are there to obtain evidence on whether or not the costs outweigh the benefits or not, and the setting of a budget represents the government's assessment where the marginal benefits equal the marginal costs.

[10] Given a reasonably strong opposition (outside directors?), not only will the consequences of the program be transparent, but also there is a time honored method of penalizing an agent who does not act in the interest of the principals.

[11] See Chant and Acheson (1971) for an early application of this analysis to Canadian institutions.

[12] The Crawford Commission was instituted to provide a five year review of the OSC

[13] See OSC (2003b), p. 8.

[14] Ibid, p.81.

It is not that securities regulators are without the means to carry out such analysis. The Crawford Commission speaks favorably of the SEC's use of cost – benefit analysis, and in soliciting others to assist it in identifying additional costs and/or benefits.[15] One could go further. If the OSC is to lead by example, then, at a minimum, it should seriously face accounting rules that have *both* relevance and *some* public acceptance. By this I mean that it have economists, either in-house or under contract, that will undertake cost-benefit analyses on any new regulation, and that they systematically reexamine past regulations to see if they have remained profitable (have benefits that outweigh costs.)

One of the most important aspects of transparency is that shareholders have access to the accounts of the firm. In the case of the OSC, the equivalent would, at a minimum, involve making public those cost-benefit analyses that are done and, as the Crawford Commission argues, also provide an explanation if they are not. Just as with the firm, this added level of potential monitoring should make the OSC more careful in undertaking costly new initiatives.

Auditing

Without a meaningful accounting system the issue of auditing – the use of an external supplier to assess the activities of the agent – is moot. Nonetheless, suppose that, following the Crawford Commission recommendation, the OSC does make an attempt to conduct cost-benefit analyses for any new policy initiative. Then an external audit would be as necessary here as it is in the private sector. Certainly, the OSC would not tolerate a publicly traded firm that used only internal accountants to measure its profits and/or losses. Rather, it would require both an external audit and that some member of management be held to account if the books were found to be materially incorrect. The public should require no less of its regulatory agents. The "auditors" would thus be outside assessors with some competence in evaluating the programs and would most certainly be independent of the OSC itself. If "accounting frauds" are found, then it would be consistent with policy that someone in that organization would be held accountable and should bear the same consequences as if such fraud occurred in the private sector. For instance, recent regulatory changes in the U.S. and Canada require that the CEO and CFO sign off on quarterly reports, presumably because they can be prosecuted if there were any falsification of those statements. Perhaps the Chair and the chief economist of the OSC should be required to face similar actions if their cost-benefit studies also are materially incorrect.

Compliance

In the current regulatory environment even medium sized firms need to devote considerable resources to ensure that regulations affecting both principals and third parties are not compromised by members of the firm. Crown corporations, such as the OSC, have more limited liabilities due to their quasi judicial role, yet they too are subject to rules on process and the like that also are meant to protect principals and third parties.

[15] These have been used for regulations initiated by the SEC. In the case of Sarbanes – Oxley, the rules were initiated and passed by Congress without the benefit of any significant analysis of the costs and benefits of the legislation.

It is, no doubt, the case that the OSC has procedures in place to control for petty behavior directed at the public that deals with the Commissioners and/or staff such as arrogance, vindictiveness and/or conflict of interest practices, however unlikely. Nonetheless, there appears to be a fundamental difference between how private firms and regulatory agencies ultimately ensure compliance. For the firm, the compliance officer can, and often is required to, go outside the firm – to the regulator or the courts – to report malfeasance. For the OSC, the "compliance officer" reports to the head of the agency itself. At a very minimum, this can lead to the appearance of conflicts of interest and cover-up. Because the OSC insists that appearance is virtually as important as actions, providing some external channel to report violations should lead to greater compliance in appearance as well as in fact. It would also show that the OSC is capable of leading by example.

The Crawford Commission has also focused on a second area of compliance. This is the breaching of the presumed Chinese wall between staff and commission. This focus is fairly recent, appearing in the 2003 final report but not the draft report issued the year before. One possible reason for its appearance as an issue may be because of the quality of the quasi-judicial decisions that have been made since the market has fallen: on the basis of scanty evidence at best, the decisions made have had penalties far in excess of the costs of the apparent crimes committed, and substantial inconsistencies across parties of the same infraction.[16] The separation of prosecutor and judges separated by one flight of stairs does not give many in the financial community much confidence in the justice of the system.[17] One suggestion of the Crawford Commission was to explore the possibility of the separation of the prosecutorial and judicial branches. In effect, removing the adjudication function from the OSC provides at least some oversight of the institution by having the capacity to overturn decisions that would otherwise be conducted "in house". This oversight could help restore some confidence in the decisions made by the OSC.

4. Additional Governance Mechanisms

Government bureaus have had great difficulty in providing performance linked financial bonuses to employees, and this carries over to agencies and crown corporations such as the OSC. Again, this arises from poor accounting. With no measure of the costs and benefits of various programs, the bureau itself can fabricate whatever self-serving values

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[16] A possible motive for the former is to deflect criticism of the Commission and find other scapegoats for the market decline and to assuage the responsibility for the poor returns of individual investors. The latter suggests that the widely disparate penalties – as in the Patterson and Donnini cases – imposed on those that confess and those that maintain their innocence is linked to the Commissioners' willingness to assist staff prosecutors in extracting confessions in future cases. In those cases Patterson received a 2 year suspension and Donnini a 15 year suspension (for speaking with one another). Donnini's suspension was later reduced to 4 years on appeal to the judicial system, where the judge remarked that simply defending oneself is not against the law.

[17] The regularly scheduled meetings of staff and commissioners, to "educate" the latter also would lead some to question the objectivity of the Commissioners. This, too, hardly reflects the absence of *ex partite* communication.

it chooses. Furthermore, because of the difficulty – or unwillingness – to measure outputs, the measures usually settled on generally boil down to being correlated with inputs rather than outputs. But this tends to mean that the greater the extent of regulation, the greater the value the bureaucracy attributes to itself.

For both institutions and individuals, one obvious fact reins in the appetite to expand, namely a budget constraint. Unfortunately, as a crown corporation, the OSC can generate its own revenue in a one supplier market. In particular, any revenue from fees, fines, and/or settlements above and beyond (a) the costs of operation and (b) designated under terms of settlement for allocation to or for the benefit of third parties was to be remitted to the Consolidated Revenue Fund. These terms were added to the legislation to remove the perception that the OSC "encouraged settlements, not because they were in the public interest, but rather to generate additional revenue."[18] If anything, such a revenue structure actually encourages the OSC to over regulate.

It has been argued that regulatory competition can lead to better regulation. Nonetheless, in Canada this competition is fairly limited. For instance, investors resident in the US cannot use Canadian brokers to make their trades and, "in retaliation," the OSC does not permit Ontario residents to use US brokers, so the "competition" de facto takes the form of collusion against the principals who "own" the regulatory machinery.

The regulatory competition among the 13 provincial and territorial security commissions is also limited. Currently, each regional commission insists that firms operating in their area be subject to their specific regulations. A current proposal for reform is the passport system where the firm registers in only one province but can operate in all others on the basis of that registration.[19] All but one of the provincial and territorial security regulators have indicated they are in favor of this reform and most view it as a step in the process of moving to a single regulator. The holdout is the OSC.[20]

The Crawford Commission suggestion to study the separation of the prosecutorial and judicial functions of the OSC was later followed up by the Osborne report which recommended such a separation. The Ontario Standing Committee on Finance and Economic Affairs accepted the Osborne report and it is expected to be put into place some time in the next year. It is this "independent judiciary" and the greater insistence on a relevant accounting system (cost-benefit analysis) that are the Crawford Commission cornerstones to provide the greater oversight of the OSC in the coming years. It is worth

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[18] OSC (2003b), p.219.

[19] Under this proposal, firms would continue to be subject to the local regulations of the province(s) in which they operate.

[20] Regulatory competition across institutions but within the same location is a possibility, with separate regulators for pension plans, insurance companies and securities markets. It remains to be seen if there is or is not competion among them in the case of Capital Accumulation Plans (CAPs). If the regulators settle on one set of quantitative restrictions for all these institutions instead of separate rules for each, then what competition there was will have been co-opted in favor of regulatory collusion.

noting that both are mechanisms that have applied to the private corporate sector since long before the establishment of financial regulators in North America.

5. Concluding Remarks

Corporate and, to an extent, public, governance deals with the institutions, practices and regulations that are meant to resolve the principal – agent problem, and to insure that the legal rights of third parties are not infringed. In the financial sector governance practices have been overseen by a financial regulator for most of the past century. For Ontario, the regulator is the OSC which was restructured as a crown corporation in 1997 and has been quite active during its recent incarnation, especially in imposing new standards of governance for publicly traded corporations. The fundamental question is how we can determine what the best governance practices are. While the evidence is not in on that question there are at least two (admittedly extreme) hypotheses that might be used to get a handle on the answer. One hypothesis is that the regulations imposed by financial market regulators define the minimum necessary conditions for good governance practices: If they did not, then the regulations would not have been imposed by a welfare maximizing government agency. The second hypothesis is that the governance practices of the regulator must be the best practices for governance on the assumption that they would want to provide an example of best practices and, in any case, would be inclined to use best practices in order to operate most efficiently. I have used the OSC as a case study of the differences in policies set for the private sector and used by the regulator itself.

One area where regulations have recently been expanded has been the requirement that there be certain minimum numbers of independent directors on the board and especially on the audit and compensation committees. The OSC Board and its subcommittees are composed solely of non-independent directors – the Commissioners themselves. Now it may be that the Commissioners are so honorable that they do not need to be monitored by an independent set of directors. Or it may be that, indeed, they are imposing unnecessary costs on private firms.[21]

A second area where policy and practice differ is in the enforcement of laws and regulations ostensibly to protect both principals and third parties. Such compliance issues have become quite expensive for private firms and have often taken the form of a specific member of the firm taking on compliance issues full time. These compliance officers have a reasonable degree of independence and can go outside the firm to the legal system and/or regulatory body to back up their assessments. OSC practices are much less transparent. Issues of compliance are handled internally and reported to the

[21] These costs are not trivial. In the US where, admittedly, the Sarbanes - Oxley legislation goes further than in Canada, the costs for some firms can be substantial. The cost to AIG has been estimated at US$300 million and GE estimated theirs to be US$30 million. For public firms with sales under US$1 billion, the average cost increase has been estimated at US$1.6 million. See Bartlett (2004). The NY Times (May 20, 2005) reports that between 2001 and 2003 the securities industry lost 8% of its [US] workforce whereas those involved in corporate oversight grew 30%.

Commissioners themselves. There also appears to be some resistance to making material public as required by the freedom of information act. Again there is a substantial conflict between policy and practice: Either the regulatory burden applied to the private sector is excessive or the Commissioners are headed for sainthood.

An essential element in resolving any principal – agent problem is the ability of the principals to have some measure of performance of the agent in achieving its objective. For the private sector, a complete system of financial accounts and procedures has been developed to satisfy this need for transparency long before financial markets were ever subject to financial regulation. Yet financial market regulators continue to demand modifications to those systems in an effort to provide greater comparability across firms.

If we look to OSC *practice*, we find that their accounting system is far inferior to even pre regulation accounting for the private sector. This is because the OSC has no meaningful measuring mechanism to determine whether or not it is meeting its objectives. To have a meaningful system for the OSC would require that the Commission take seriously cost-benefit analysis for each of their policy initiatives and conduct post audits to determine if their forecasts were correct. To this point they have applied cost-benefit analysis haphazardly and there is no public record of any ex post analysis of the net benefits of any regulation.

This absence of proper accounting is likely the major reason we have no good handle on what best governance practices might be. Certainly it cannot be more lax than the governance procedures used by the OSC itself. Nor could it be as restrictive as current regulations require since, in the absence of cost-benefit analysis, there is every incentive for a regulatory commission to expand its empire and over regulate.[22] In the absence of fundamental changes in governance procedures, and most especially a serious effort to have meaningful accounting and oversight procedures, there is a real question of the legitimacy of such an organization. Institutions that behave contrary to what they insist others should do can hardly command respect from the community that they are supposed to serve.

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[22] If the current regulations *did* represent the minimum for good governance practices then the obvious questions is: Would the OSC Commissioners as well as some senior members of staff be in jail if these regulations applied to their institution? We might add that there is also every incentive for the principals of the private firm to get everything right in structuring its governance practices in the absence of regulation.

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