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AN EXAMINATION OF THE TRADE AND COMMERCE POWER IN THE REGULATION OF INSURANCE COMPANIES AS FINANCIAL INSTITUTIONS

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An Examination of the Trade and Commerce Power in the Regulation of Insurance Companies as Financial Institutions

SUMMARY

The thesis of this paper is that Parliament has jurisdiction to regulate insurance companies --in particular, life insurance companies-- as financial institutions by virtue of its power to regulate trade and commerce under subsection 91(2) of the Constitution Act, 1867 ("the 1867 Act"). If the trade and commerce power enables Parliament to regulate life insurance companies as financial institutions, it ought to enable federal regulation of other financial institutions that do business as financial intermediaries.

It is argued that the business of financial institutions is financial intermediation and that this activity falls within s.91(2) under the "second branch" of the federal trade and commerce power as provided in Citizens Insurance v. Parsons (1881) 7 A.C. 96 (P.C.), namely, "general regulation of trade affecting the whole Dominion".

Chartered banks and "banking" are, of course, already given to Parliament under s. 91(15). The so-called "near banks", that is, financial institutions such as trust companies, credit unions and caisses populaires might also fall within s. 91(15), as has been argued by others. However, the ambit of s.91(15) is not the subject of this paper. Rather, it is the ambit of s.91(2) with respect to these same institutions and others such as investment dealers and life insurance companies.

The jurisdictional proposition advanced in this paper cannot be considered in vacuo but only within the recognizable limits of the Canadian constitutional framework as derived from the 1867 Act and the constitutional rulings of the courts.

The constitutional framework relevant for purposes of this paper has two dimensions. First, there is, of course, s.91(2) and its meaning developed by the courts as a matter of constitutional interpretation. Second, there is the broader constitutional dimension of federalism, both the general theory of federalism as a form of constitutional government and the particular design of Canadian federalism as established by the 1867

Act as written and as interpreted by the courts since the time of Confederation. The regulation of trade and commerce is but one of several legislative powers distributed in the Canadian federal system and the constitutional design of the Canadian federal system necessarily governs interpretation and application of this power.

The constitutional framework is examined through two questions. First, to what kind of trade does s.91(2) apply? Second, what kind of federalism is it that we have in Canada? It is argued, in response to the first question, that s.91(2) applies to systemic, abstract economic matters at the national level. In response to the second question, it is argued that the federalism provided by the 1867 Act is one of strong economic powers vested in the central authority --Parliament-- to enable the central authority to deal with matters affecting the economic life of the country as a whole.

As a case study of the broader proposition, the paper considers the prospects for regulating life insurance companies under s.91(2). Life insurance companies are one of the four major categories of financial institution in Canada (one of the "four pillars" of the financial system in Canada). It is widely believed, based on a series of Privy Council decisions from Parsons, above, to Re Insurance Act [1932] A.C. 41, that insurance is a matter within exclusive provincial jurisdiction.

It is argued that the so-called "insurance cases" do not establish that the business of insurance or the business of insurance companies is a matter within provincial jurisdiction. At best, the insurance contract, as a matter falling within s.92(13), "property and civil rights in the province", falls within exclusive provincial powers. The same applies to trust company contracts, regardless of the level of incorporation of the trust company.

Some statistical material is offered with respect to the factual proposition on which the jurisdictional proposition advanced in this paper depends, namely, that insurance companies, like banks, trust companies and investment dealers, are engaged in the business of financial intermediation at the interprovincial or transprovincial level and are not in the business of simply providing insurance coverage under contract. The reader may not find the treatment given to this factual proposition conclusive or persuasive. It is not intended to be conclusive or persuasive but only to offer an indication of the kind of material that could be submitted in support of the factual proposition and to indicate that this proposition is not fanciful or without any foundation in fact.

The recent federal reforms, both enacted and proposed, relating to financial institutions are examined and found wanting insofar as they reflect, in form if not in substance, a continuation of the existing regime where jurisdiction is based on the type of institution being regulated, that is, on the level at which the institution is incorporated, rather than on the function that is performed by the institution. Nonetheless, the federal reforms, through allowing federal institutions to own provincial subsidiaries, extend federal regulatory powers to provincial institutions that are otherwise beyond their reach.

The paper concludes with a summary of the argument for central regulatory control of financial institutions, with some suggested criteria that the Court might apply in justifying federal legislation regulating financial intermediation under s.91(2).

(End of Summary)

An Examination of the Trade and Commerce Power in the Regulation of Insurance Companies as Financial Institutions

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I INTRODUCTION

The regulation of financial institutions in Canada occurs at both legislative levels. Under the Constitution Act, 1867 ("the 1867 Act" or "the Act"), as interpreted by the courts to date, banks are regulated exclusively at the federal level while insurance companies and trust and mortgage companies are regulated at either the federal level or the provincial level, depending on the level at which they are incorporated. Investment dealers are regulated at the provincial level.

The four financial institutions just mentioned --banks, insurance companies, trust and mortgage companies and investment dealers-- are considered the major categories of financial institution in Canada and are often referred to as the four "pillars" of the Canadian financial system. According to the four pillars philosophy, financial institutions ought to be limited to their "core" function --banking, selling insurance, fiduciary services, underwriting-- and be regulated and supervised separately under each pillar.

Thus, the regulation of financial institutions in Canada is divided in two respects: as between two legislative levels and as between different "pillars" or categories of institution.

Some argue that the limited role enjoyed by Parliament in the area of financial institutions regulation, the growth of the so-called "near banks" at the provincial level and the domination of securities regulation by the provinces are due to a failure of political will in Parliament and that this limited role is not due to any constitutional limitation inherent in the relevant s.91 enumerations but rather to a failure on the part of Parliament to exercise its powers fully. This may be so. However, this is a political question more than a legal one and thus outside the terms of reference of this paper.

In legal terms, the regime of divided powers over financial institutions in Canada is as much the result of what the 1867 Act fails to provide as what it provides. While banks and banking are expressly assigned to Parliament by s.91(15), insurance is not mentioned in the Act despite specific mention of a variety of economic matters in the s.91 enumerations. Likewise, the business of trust companies or of fiduciaries generally is not mentioned in the Act.

This paper examines the basis for constitutional control by Parliament of financial institutions generally. Particular attention is given to the business of life insurance companies, for two reasons.[1] First, there is a history of legislative struggle between the two legislative levels with respect to insurance and the business of insurance companies. This is not the case with the other categories of financial institutions. Second, it is widely assumed by students of the constitution, based on the so-called insurance cases decided in the Privy Council some years ago, that insurance is a matter within exclusive provincial jurisdiction.

It is contended here that financial intermediation is the basic function or activity that is common to the business of banks, insurance companies, trust companies and investment dealers alike as financial institutions.[2] The legislative subject-matter for regulation is financial intermediation.

Federal jurisdiction over financial institutions, as financial intermediaries, depends upon the application of s.91(2), the federal power to regulate trade and commerce. This federal power, as we shall see, includes the regulation of general trade matters that affect the country as a whole. Financial intermediation, it is argued, is a general trade matter that affects the country as a whole and, as such, is within the legislative powers of Parliament under s.91(2).[3]

The courts appear to have recognized Parliament's jurisdiction under s.91(2) over the regulation of competition.[4] It is submitted that financial intermediation is a legislative and economic equivalent of competition insofar as financial intermediation and competition are both fundamental to the operations of a national economy. Federal legislation, directed toward the regulation of financial intermediation as an integral part of the national economy, ought to receive the same treatment as has been given to federal legislation regulating competition.

Financial institutions are facing changes in their markets and in the economic and regulatory environment in which they do business. Advances in technology now enable financial transactions to routinely take place across provincial and national boundaries in volumes and at speeds far greater than was the case when the existing federal legislation governing financial institutions was enacted in 1932.

Financial institutions have complained that legislative restrictions limit their ability to compete in the financial marketplace, particularly in foreign markets that have seen some deregulation. At the same time, money market pressures have led institutions under one pillar, through introduction of innovative financial products, to reach beyond their own markets and into markets reserved for institutions doing business under the other pillars.

In addition, commercial and industrial interests have entered the financial services industry through ownership of financial institutions as subsidiary or affiliated companies. This has led to concerns about cross-industry ownership of financial institutions, conflicts of interest, self-dealing, the concentration of ownership of financial institutions and the degree of foreign ownership of Canadian financial institutions.

In December 1986, the federal government introduced a legislative reform program on financial services which it said was designed to render Canadian financial institutions and the financial system in Canada more competitive and financially sound. We shall look at these reforms to see to what extent they reflect the legislative approach suggested here, namely, the regulation of financial intermediation as a general trade matter, rather than the regulation of financial institutions according to obsolete functional categories or "pillars" based on the level of incorporation of the institution.

It is contended that effective regulation of the Canadian financial system as a whole is imperative and that such regulation can only be provided by a central regulating authority. If financial intermediation is accepted as the relevant legislative subject matter, Parliament has the requisite jurisdiction under s.91(2) to regulate a financial institution that does business as a financial intermediary outside the province of its incorporation, regardless of the legislative level at which the institution was incorporated.

II FINANCIAL INTERMEDIATION

Before consideration of the constitutional framework with respect to the regulation of financial institutions, it may be helpful to consider what we mean by financial intermediation and why it is important that it be effectively regulated.

Financial intermediation is the process whereby surplus funds (capital) are transferred from persons ("savers") who have more than they need for their own use to persons who do not ("users"). Although the intermediation may be provided through different mechanisms and give rise to different kinds of legal relationships between the intermediary and the saver or the intermediary and the user (debtor and creditor, trustee and beneficiary, principal and agent, insurer and insured), the institution's role remains one of financial intermediation.

In monetary terms, financial intermediation is the process by which asset balances in the money supply are converted from an idle state as savings to an active state as loans or investments. Financial intermediaries facilitate credit expansion as a tool of monetary economic management. Asset balances held by financial institutions are used to meet the demands of business activity in the economy. In theory, when economic resources are fully employed, all asset balances or savings are at work in the economy.

In terms of monetary economic policy, as a tool of economic management, it is important to keep the level of current real (non-inflationary) investment in balance with the level of real savings that would be generated were the economy operating at approximately full capacity. In this fashion, it is hoped, an economy that is working at less than full capacity can be brought up to full capacity.

If the money supply is increased when the economy is already working at full capacity, however, the resulting credit expansion causes inflation because the investments made possible by the credit expansion are in excess of real savings which, because the economy is working at full capacity, are already fully utilized. Thus, credit expansion, as a tool for economic management, is controlled by an agency of government, the Bank of Canada, through regulation of the supply of money provided to the financial system.

Although the Bank of Canada, as a central bank, directly affects only banks, non-bank financial intermediaries are indirectly affected by credit expansion initiatives taken by the central bank. With an expansion of credit, the asset balances that non-bank financial institutions accumulate are increased in the normal course of doing business, along with the asset balances of the banks themselves. The increase in the money supply, caused by the credit expansion, eventually and soon shows up in the asset balances on non-bank financial institutions. These asset balances must, in turn, be converted into active investments. In this fashion, all financial institutions are players in the application of monetary and fiscal policies in the management of the economy.[5]

Financial institutions do business with other people's money. They deal in financial assets and liabilities as opposed to physical goods or non-financial services. In this fundamental respect, they are to be distinguished from other businesses. According to the Porter Royal Commission on Banking and Finance (1964), financial institutions are "professional dealers in financial claims":

> Their assets are the debt instruments and equity shares of final borrowers or users of funds, and to a lesser extent of other intermediaries. These are financed by issuing their own liabilities, principally in the form of promises to pay of various kinds but also in the form of shares, which are held as assets by final lenders or suppliers of funds and, in minor amounts, by other financial institutions.[6]

The assets of financial intermediaries, that is, their own financial claims, can range from short term government treasury bills to risky, long-term investments in untested businesses. Their liabilities, that is, the financial claims against them, can vary from chequable deposits redeemable on demand to long-term life insurance contracts that are payable years later.[7]

Financial intermediaries are able to do business profitably because they provide a service whereby savers are able to "meet" users without the difficulties that would apply were such parties required to find each other directly. In the absence of financial intermediaries, the saver-lender would have to take the time and expend the money that would be required to find a user-borrower who offers the right terms. There would be increased risk for the saver who would likely not be personally familiar with the borrower. The saver, unlike a professional financial intermediary with a diversification of loans, would probably lend all his or her savings to one borrower or perhaps to only a few borrowers.

The saver, acting alone, would also have considerable difficulty disposing of the claims (assets to the saver) that are received directly from borrowers in exchange for the funds advanced by the saver. In addition, the obligation or claim issued by the borrower (a liability to the borrower) would not be accompanied by any of the financial services often provided by professional financial intermediaries. Corresponding and similar considerations apply for the borrower. As the Porter Royal Commission has said:

> If financial institutions did not exist to take [the borrower's] claims into their balance sheets and to issue...claims to final lenders in their place, much of the credit which now flows from lenders to borrowers in this way would only move at higher rates and under more restrictive conditions, while a good deal of it would probably not flow at all.[8]

Financial institutions, as "professional dealers in financial claims", develop a broad and specialized knowledge of the financial marketplace generally and of capital markets in particular. They are able to do business on a scale much larger than an individual or corporation can do alone. They acquire a diversified portfolio of assets (claims) and develop specialized skills and efficient procedures for processing credit applications. For these reasons, the institutions are less risky as users of the savings of the individual saver. Also, they develop greater lending efficiency and capacity to meet the needs of borrowers than would be the case were borrowers dealing directly with savers:

> In short, [financial institutions'] activities facilitate the flow of funds from lenders to borrowers by reducing costs and improving liquidity, by increasing the number of routes over which credit may pass, and by enhancing the flexibility of the financial system.[9]

Thus, the dynamics of a financial system as a whole may be generally described as follows: capital is generated through savings and, through the workings of the capital markets, these savings are put to work as investments through indirect financing provided by financial institutions acting as financial intermediaries.

For capital markets, as for other markets, the ultimate objective is an efficient allocation of limited resources through competition based on price. With respect to financial intermediaries, a competitive price-based capital market means, first, that financial institutions will direct their investments toward higher-yielding investments; second, that price factors will play an active part in the sale of the institutions' liabilities; and third, that financial institutions, in tending to deal with businesses having higher earnings, will be assisting efficient firms to do well.[10]

Efficiency through competition is the operative premise to a free-market, price-based economy. It applies to all players in the marketplace except, perhaps, to government-owned monopolies. Competition induces financial intermediaries to assist general economic growth and to do so by facilitating trade and commerce generally.

A competitive capital market is not enough, however:

> After all, when it comes to protecting savers and having an effective financial system, what counts is that a government can establish rules of conduct applying to all companies and, once they have been established, can supervise their application.[11]

The business of financial intermediaries also depends on public confidence in the financial institutions themselves. A saver must have confidence, not only that a financial institution will not lose his or her savings, but that it will later repay the savings plus a reasonable return. This confidence is easily shaken by scandals of financial chicanery or incompetence, whether or not insolvency or bankruptcy of the institution results.

For the individual saver, confidence in a financial institution is nothing less than an act of faith. It is the same act of faith that each one of us manifests when we accept cash money in exchange for a good or a service. We must have faith that money received for value given in exchange will be accepted at face value when later offered in payment for a good or a service. If cash money is to function effectively as legal tender, as a routine medium for the exchange of value, all of us must have faith in its continuing value.

Our faith in money is made easier by the fact that one piece of money is as good as another. We need not examine each dollar bill or coin to satisfy ourselves that it is legal tender. We know from experience that, despite its diminishing value in inflationary times, money is generally acceptable as a medium of exchange. With respect to financial institutions, however, as holders of our savings, our own private reserves of money, one institution may not be as reliable as another. For this reason, modern financial systems look to regulation and supervision of financial institutions by government.

The agent of effective regulation can only be government. It is government that is charged with defending the collective public interest. The regulation of financial institutions by government means regulation that is designed to assure the solvency of the institutions and thereby to preserve public confidence in those institutions and in the financial system, if not also the economy, as a whole. The regulation of financial institutions by government must also mean regulation that allows for innovation so that the institutions can respond to the changing demands of savers and borrowers and, at the same time, can remain competitive with each other and with institutions from other regulatory jurisdictions.

In other words, regulation must protect and preserve public confidence in financial institutions and the financial system without putting the institutions or the system at a competitive disadvantage.

Canada does not have separate, autonomous provincial financial systems. The provinces do not restrict the interprovincial movement of capital in the interest of their financial systems. Further, the provinces do not maintain their own system of banks or legal tender. Also, capital is "fluid", that is, it follows the proverbial path of least resistance and flows to the place that promises the best return, within acceptable degrees of risk. It would be counterproductive, if not futile, for a province to try to restrict the movement of capital in order to support a provincial financial system independent of the rest of Canada.

Effective regulation of a national financial system in a federated state can only be done through central regulatory control.[12] Where several regulatory regimes operate within one national financial system, financial institutions can shop around for the least restrictive jurisdiction.[13] Some jurisdictions may be tempted to lower their regulatory standards in order to attract institutions to establish in their territory. Such "regulatory havens", in the absence of central regulatory control and in the absence of territorial restrictions on the business activities of the institutions, would likely facilitate the improper business practices of some institutions and thus place in jeopardy the welfare of the national financial system as a whole.

In Canada, effective regulation and supervision of financial institutions doing business as part of the national financial system means regulation by Parliament as the central legislative authority and supervision by federal officials acting under federal legislation. The question is whether, within the existing constitutional framework of Confederation, the federal general trade power under s.91(2) is sufficient for such a purpose.

III THE CONSTITUTIONAL FRAMEWORK

The federal trade and commerce power under s.91(2) has been given a very limited application in the courts.[14] It has usually met defeat when confronted by s.92(13), property and civil rights in the province, where this enumeration has been applied in defence of provincial autonomy.

Application of s.91(2) to the regulation of financial institutions generally would be a new departure for this enumeration. The Court must find within the existing constitutional framework the grounds for such application of the federal power.[15] The constitutional framework includes foremost the jurisprudence to be found in the decided cases on s.91(2). It also includes the larger constitutional dimension that is federalism itself.

Section 91(2) is a federal trade power, that is, a federal power and a trade power. The distinction raises two fundamental questions that must be asked on a consideration of the limits of this enumeration. First, to what kind of trade does s.91(2) apply?

Second, does the particular design of Canadian federalism, as provided by the 1867 Act, support application to financial intermediation of s.91(2) as a federal trade power?

With respect to the first question, we have the decided cases of the Court and the Privy Council where the meaning of s.91(2) has been examined on several occasions and over a period of more than 100 years. With respect to the second question, we have theories of federalism as devised by learned authors on systems of government and, as well, we have decisions of the Court where the federal principle and other underlying principles of federalism have been recognized and applied.

To what kind of trade does s.91(2) apply?

Judicial consideration of the trade and commerce power begins with the Privy Council decision in Parsons (1881), a case that involved provincial fire insurance legislation.[16] The Ontario statute prescribed mandatory conditions for a valid policy of fire insurance and it applied to all insurers doing business in Ontario, regardless of their place of incorporation. The Privy Council observed that the Ontario statute dealt with policies of insurance

> entered into or in force in the province of Ontario for insuring property situate therein against fire, and prescribes certain conditions which are to form part of such contracts.[17]

Sir Montague Smith, on behalf of the Privy Council and in support of the legislation, said that s.92(13), property and civil rights in the province, in its "fair and ordinary meaning", included rights arising from contract and that such rights were not expressly included in any of the s.91 enumerated classes of subjects so as to take them out of the s.92 enumerations.[18]

Nonetheless, the Privy Council in Parsons considered whether the Ontario legislation came within s.91(2), the regulation of trade and commerce, and so "is or is not thereby overborn".[19] Sir Montague said the words in s.91(2), "the regulation of trade and commerce," are by themselves broad and comprehensive but that a consideration of the Act shows that the words are not used in this "unlimited sense":

> [T]he collocation of No. 2 with classes of subjects of national and general concern affords an indication that regulations relating to general trade and commerce were in the mind of the legislature, when conferring this power on the Dominion parliament.[20]

As an illustration of the generality of the language used in s.91(2), Sir Montague referred to the Act of Union Between England and Scotland (U.K.) and other Acts of State where Parliament (U.K.) had used the same words as are found in s.91(2), that is, words granting freedom of trade to all subjects and providing that all parts of the United Kingdom shall be under the same "regulations of trade". Yet Parliament, said Sir Montague, subsequently passed laws affecting and regulating specific trades in one part of the U.K. only. Thus, specific trades are not to be included in general language with respect to the regulation of "trade":

> [C]onstruing therefore the words "regulation of trade and commerce"...they would include political arrangements in regard to trade requiring the sanction of Parliament, regulation of trade in matters of inter-provincial concern, and it may be that they would include general regulation of trade affecting the whole Dominion.... [T]he authority does not comprehend the power to regulate... the contracts of a particular business or trade... and therefore... its legislative authority does not... conflict or compete with the power over property and civil rights assigned... by No. 13 of sect. 92.[21] (underlining added)

The underlined words in the above quoted passage from Parsons have since been referred to as the "second branch" of Parsons and provide the jurisprudential basis for the application of s.91(2) as a general trade power.

According to Sir Montague in Parsons, "trade" is to be distinguished from "trades" or "a trade". The difference in the meanings of these words, as distinguished in Parsons, may suggest the basic difference in the legislative powers of the two legislative levels with respect to trade or trade matters.

The word "trade", as a noun, is abstract in its meaning and refers to an aspect of the economic system at large. The word refers to an economic activity simpliciter. The words "trades" or "a trade", on the other hand, as nouns, are non-abstract in their meaning and refer to an activity carried on by persons.[22] The distinction is between a word of systemic abstract meaning and words of non-systemic non-abstract meaning.

Systemic abstract economic matters are those matters that pertain directly and primarily to the economic system as a whole or to some aspect of the economic system as a whole, such as competition. Non-systemic non-abstract trade matters are the private activities of persons engaged locally in a trade or occupation, such as the selling of insurance policies.

A systemic abstract word is replaced with a non-systemic non-abstract word when the object to which the systemic abstract word refers becomes tied to a person through ownership, possession or use by the person. For example, "property" and "civil rights" are tied to the person. "Land" is not tied to the person. "Land" becomes "property" when it is lawfully owned, possessed or used by a person. Similarly, "rights" and "civil rights" are empty notions except when seen as entities possessed by a person as a matter of civil law.[23] In a similar fashion, "a trade" or "trades" refer to the systemic abstract economic activity ("trade") when carried on by a person. Such words have no meaning except with reference to a person.

In sum, then, we can say that <u>Parsons</u> has given us three rules or propositions with respect to s.91(2):

(a) a subject-matter regulated under s.91(2) must be "trade affecting the whole Dominion" or affecting interprovincial or export trade and not specific trades or a trade;

(b) contracts are not subject to federal regulation under s.91(2); and

(c) the federal power under s. 91(2), properly understood as a general power, does not "conflict or compete with" the provincial power under under s.92(13).[24]

In Natural Products (1936), a marketing case in which the first two rules from Parsons were applied, the Court, per Justice Duff, struck down federal legislation that established a federal marketing board with the power to regulate the marketing of natural products in interprovincial and export trade.[25] The fatal flaw in the legislation was the power to regulate transactions which took place entirely within a province with no connection to interprovincial or export trade:

> The enactments in question, therefore, insofar as they relate to matters which are in substance local and provincial are beyond the jurisdiction of Parliament. [26]

The application of federal legislation to local trade, although only a part of the legislative scheme in Natural Products, was enough to defeat the entire legislative initiative. This served to confirm subordination of the federal trade power under s.91(2) to provincial powers under either s.92(13) or s.92(16). With respect to the kind of trade regulation that would fall within s.91(2), Justice Duff said:

> [T]hese [federal] enactments operate by way of the regulation of dealings in particular commodities and classes of commodities. The regulations contemplated are not general regulations of trade as a whole or regulations of general trade and commerce within the sense of the judgment in Parson's case. [27]

It would appear that the presence of an identifiable trade commodity in Natural Products prevented recognition of the federal legislation as legislation relating to trade generally.[28]

In Ontario Farm Products (1957), Chief Justice Kerwin articulated the "stream of commerce" doctrine under s.91(2):

> - Once an article enters into the flow of interprovincial or external trade, the subject matter and all its attendant circumstances cease to be a mere matter of local concern.[29]

A recognizable demarcation line between local trade and interprovincial or external trade was not offered by the Court except that once a trade activity involved "a matter of extra-provincial interest or concern" it was thereafter beyond provincial powers.[30]

In Murphy v. C.P.R. (1958), the Court upheld under s.91(2) federal legislation regulating the export of grain from a province.[31] In R. v. Klassen (1959), the Manitoba Court of Appeal upheld federal legislation establishing a national scheme in the area of interprovincial and export trade of surplus grain. The Manitoba court said the federal legislation, for the sake of the national scheme, could regulate local trade that fell within the scheme.

> [T]he pith and substance of [the Act] is the provision of an export market for surplus grains, a matter which has undoubtedly assumed a national importance.[32]

In Carnation Company (1968), the Court upheld Québec milk marketing legislation, rejecting the company's argument that the legislation affected its interprovincial trade.[33] The Court said the test was not whether the legislation affected interprovincial trade but whether it was enacted "in relation to" the regulation of trade and commerce. The Quebec regulations did not "purport directly to control or restrict such trade."

The test used in Carnation Company was used in Manitoba Egg & Poultry (1971) and brought the opposite result.[34] Manitoba egg marketing legislation was struck down by the Court on the ground that the legislation was intended to regulate interprovincial trade directly.[35] Insofar as the legislation was designed "to restrict or limit the flow of trade between provinces as such", it was an invasion of the exclusive federal trade and commerce power.

In Caloil Inc. (1971), the Court upheld federal legislation which prohibited importers from selling gasoline west of the Ottawa Valley line.[36] The Court rejected the argument that regulating the importation and internal distribution of an imported product was interference with provincial jurisdiction.

The Court in Caloil Inc. upheld the federal legislation notwithstanding the existence of conflicting provincial powers. The Court engaged the paramountcy rule that where the constitutional division of powers results in overlapping authority and the field is not clear, the federal legislation shall prevail over the provincial legislation.[37] This requires, however, that the federal legislation be valid in its own right. Pigeon, J., on behalf of the Court, said:

> It is clear ... that the existence and extent of provincial regulatory authority over specific trades within the province is not the sole criterion to be considered in deciding whether a federal regulation affecting such a trade is invalid. On the contrary, it is no objection when the impugned enactment is an integral part of a scheme for the regulation of international or interprovincial trade, a purpose that is clearly outside provincial jurisdiction and within the exclusive federal field of action.[38]

The "true character" of the regulation restricting distribution of the imported product, said the Court, was an incident in the administration of an extraprovincial marketing scheme as in Murphy and is not "an unwarranted invasion" of provincial jurisdiction.

In Burns Foods (1974), the Court struck down Manitoba legislation that required meat processors in the province to purchase all their hogs from the Manitoba Hog Producers Marketing Board, thereby effectively prohibiting importation from another province.[39] The Court said the regulations directly controlled extra-provincial trade and were therefore beyond the competence of the province.

The Court in Burns Foods turns the Privy Council decision in Natural Products on its head. If in the earlier case federal legislation could not survive simply because regulation of the extra-provincial trade would be facilitated by regulation also of the intra-provincial trade in the product, then similarly provincial regulation of the intra-provincial trade is not sufficient reason to allow regulation of the extra-provincial trade in the same product:

> In other words, the direct regulation of interprovincial trade is of itself a matter outside the legislative authority of any Province and it cannot be treated as an accessory of the local trade.[40]

In Vapor Canada (1977), the Court struck down a provision of the federal Trade Marks Act that prohibited unfair business practices.[41] Section 7(e) provided that no person shall do an act or adopt a business practice contrary to honest industrial or commercial usage in Canada. Section 53 enabled a court to give relief by way of injunction or damages where s.7(e) is contravened.[42]

Chief Justice Laskin, speaking on behalf of the majority in Vapor Canada, said s.7(e) simply enacted the common law tort of conversion for the purpose of extending to the area of trade marks and competition a civil cause of action that was, as a matter of civil rights, within provincial jurisdiction. If the provision were part of a federally administered regulatory scheme, suggested the Chief Justice, it might survive under s.91(2) but as a provision standing on its own and dependent on private process for enforcement, it remained a matter of local concern.[43]

As in Parsons and Natural Products, so also in Vapor Canada, provincial powers under s.92(13), civil rights, and s.92(16), local and private matters, combined to defeat federal powers under s.91(2). In Vapor Canada, however, had the legislation included a valid federal regulatory scheme governing interprovincial or transprovincial trade generally, s.7(e) might have survived as being pertinent to federal legislation otherwise valid under s.91(2).[44]

The federal trade power under the second branch of Parsons, that is, the regulation of trade affecting the country as a whole, next received the Court's attention in Dominion Stores (1980) and in Labatt Breweries (1980). In both cases, however, the Court reinforced provincial jurisdiction over local trade as the predominant power.[45]

In Dominion Stores, the appellant had been charged with an offence under the federal Canada Agricultural Products Standards Act. The appellant was selling, under a certain prescribed grade name, apples that did not meet the requirements for agricultural products of that grade. In short, the apples were bruised. The offence took place in Toronto where the appellant sold apples retail.[46]

The federal Act was challenged on the basis that it applied to local trade, that is, to the sale of agricultural products in the province of Ontario, and for this reason constituted an interference with provincial jurisdiction over local trade. The Act was defended as valid legislation under s.91(2) insofar as it was directed toward the establishment of national, or nation-wide, agricultural products standards.

In the Supreme Court of Canada, Justice Estey, on behalf of the Court, cited Parsons and Natural Products and said the trade and commerce power had been settled "until now at least", that it was limited to international and inter-provincial trade and did not empower Parliament to regulate local trade

> simply as part of a scheme for the regulation of international and inter-provincial trade.[47]

Justice Estey said he approached the jurisdictional issue on the basis that

> the Parliament of Canada may not, in the guise of regulating trade and commerce, reach into the fields allocated to the provinces by s.92(13) and (16) and regulate trading transactions occurring entirely within the provinces.[48]

Labatt Breweries (1980) involved federal legislation that established a national standard for the product designation, "light beer".[49] With respect to federal jurisdiction over interprovincial trade under s.91(2), Mr. Justice Estey, speaking for the majority, referred to the "stream of commerce" cases but went on to find

> no demonstration... of any inter-provincial aspect of [the beer] industry.[50]

With regard to s.91(2) as a general trade power, that is, as a trade power based on the general concern doctrine from Parsons, Justice Estey said such power rested on an "embryonic definition" of the trade and commerce power which is

> predicated upon the requirement that the purported trade and commerce legislation affected industry and commerce at large or in a sweeping, general sense.[51]

Even if the federal legislation were to cover, said Justice Estey,

> a substantial portion of Canadian economic activity, one industry at a time, by a varying array of regulations or trade codes applicable to each individual sector, there would not, in the result, be at law regulation of trade and commerce in the sweeping, general sense contemplated in [Parsons].[52]

For Justice Estey, federal regulation of general trade affecting the country as a whole does not include regulation of a single trade or industry. As if by definition, a single trade or industry cannot be a matter of general, national concern or interest. Furthermore, contracts of an individual trade are not of general, national concern.[53] Justice Estey thus affirmed the first two of the three rules that we have from Parsons, infra.[54]

It is difficult to grasp the limits of

s.91(2) as a general trade power as Justice Estey conceived it in Labatt Breweries. His Lordship said that the power was limited to a very general legislative application, yet he failed to offer any useful criteria or indicia for determining what would constitute a valid application of the power.

In C.N. Transportation (1983), Justice Dickson (as he then was), in a partially concurring and partially dissenting judgment, offered an analysis of the federal trade and commerce power that may give new jurisprudential life to s.91(2) as a general trade power.[55]

The practical issue in C.N. Transportation was which level of government had the power to prosecute offences under the federal anti-combines legislation. This issue, for Justice Dickson, gave rise to the question of whether the regulation of competition fell within the federal trade power under s.91(2) in addition to the federal criminal law power under s.91(27). If it did, federal prosecution of offences would not be prevented by virtue of the assignment of the administration of justice to the provinces under s.92(14).

Justice Dickson agreed with Rand, J., in Ontario Farm Products where Justice Rand said that the provincial power to regulate trade was a "subtraction from the scope of the language of s.91(2)".[56] The question was how much ought to be subtracted from s.91(2) to preserve "the proper constitutional balance":

> [T]he difficult underlying task facing a court determining the constitutional status of federal economic regulation is, without passing on the substantive merits of the legislation, to assess whether and how far it encroaches on the degree of local autonomy contemplated by the constitution.[57]

Justice Dickson allowed that every general enactment will have some local impact and that there are "equal dangers" in over-emphasizing either local impact or general concern:

> The reason why the regulation of a single trade or business in the province cannot be a question of general interest throughout the Dominion, is that it lies at the very heart of local autonomy envisaged in the Constitution Act, 1867.[58]

Even if federal legislation regulating a trade or business is applicable equally throughout Canada, said Justice Dickson, it amounted to "an exact overlapping and hence a nullification" of a provincial area of jurisdiction. His Lordship continued (underlining added):

> A different situation obtains, however, when what is at issue is general legislation aimed at the economy as a single integrated national unit rather than as a collection of separate local enterprises. Such legislation is qualitatively different from anything that could practically or constitutionally be enacted by the individual provinces either separately or in combination. The focus of such legislation is on the general, though its results will obviously be manifested in particular local effects .... Nevertheless, in pith and substance such legislation will be addressed to questions of general interest throughout the Dominion. The line of demarcation is clear between measures validly directed at a general regulation of the national economy and those merely aimed at centralised control over a large number of local entities.[59]

Justice Dickson suggested three factors which the Court might consider as indicia for the valid exercise of the general trade and commerce power: (a) that the federal legislation involved a national regulatory scheme, the oversight of a regulatory agency and a concern with trade in general rather than with an aspect of a particular business, (b) that the provinces, jointly or severally, were constitutionally incapable of passing the enactment, and (c) that failure to include one or more provinces in the scheme would jeopardize the successful operation of the scheme in other parts of the country:

> [T]he presence of such factors does at least make it far more probable that what is being addressed in a federal enactment is genuinely a national

> economic concern and not just a collection of local ones.[60]

Competition, said Justice Dickson, would not be maintained if any one of the provinces should neglect or refuse to legislate in support of competition standards. Thus, competition was seen by Justice Dickson as a constituent part of the national economy and therefore legislative action to maintain competition in the economy fell within the ambit of s.91(2).

Only a few years before Justice Dickson made his comments in C.N. Transportation, the Ontario Court of Appeal spoke of federal power to regulate competition under s.91(2) in the following terms:

> [The disputed statutory provision in the federal anti-combines legislation] is part of a legislative scheme aimed at deterring a wide range of unfair competitive practices that affect trade and commerce generally across Canada, and is not limited to a single industry, commodity or area. The conduct being prohibited is generally of national and of international scope. The presence or absence of healthy competition may affect the welfare of the economy of the entire nation. It is, therefore, within the sphere of the federal Parliament to seek to regulate such competition in the interest of all Canadians.[61]

This passage, and the views subsequently expressed by Justice Dickson in C.N. Transportation, were later cited with approval by MacGuigan, J., in the Federal Court of Appeal in Québec Ready Mix (1985).[62]

In Québec Ready Mix, Justice MacGuigan said the recent decisions of the Supreme Court of Canada on the federal trade power indicated that the starting point for analysis is Parsons,

> and that the authority of such Privy Council decisions written by Lord Haldane as the Insurance Reference case of 1916... has been greatly diminished.... I propose generally to rely, therefore, on the recent decisions of the Supreme Court in the belief that what remains relevant of the Haldane approach is incorporated in them.[63]

Nevertheless, said Justice MacGuigan, quoting Laskin, C.J.C., in Vapor Canada (1977), the words of Sir Montague Smith in Parsons articulating the second branch of the trade power [see page 21, infra] remained "the guide or lead to the issue of validity".[64]

After a hundred years, from Parsons (1881) to C.N. Transportation (1983), it appears that the federal trade and commerce power, as a general trade power, includes the power to regulate trade generally, that is, in its abstract dimension. Competition, for example, is an abstract dimension of trade generally and has been recognized as within federal powers under s.91(2). Although application of competition legislation in a given case may be specific and tied to a person, the object of the legislation is the regulation of trade at the abstract level.

It would appear that federal trade legislation under s.91(2), as a general trade power derived from the second branch in Parsons, must be directed to establishing a regulatory regime for the administration and enforcement of rules and standards that are applicable to trade throughout Canada generally (Vapor Canada) and must not be directed toward the regulation of a particular trade that is carried on locally in a province (Labatt Breweries). The legislation ought to be directed toward general regulation of the national economy as a single integrated national unit (per Justice Dickson in C.N. Transportation).[65]

The design of Canadian Federalism

There remains the second of the two questions earlier posed, namely, what does the particular design of Canadian federalism, as provided by the 1867 Act, support as an appropriate application of s.91(2) as a federal trade power? In other words, is federal regulation of financial institutions, as a general trade matter under s.91(2), consistent with the kind of federalism provided by the 1867 Act?

Writing in 1947, Canadian legal scholar, F.R. Scott, argued that the 1867 Act should be examined as a whole and only then should the entire constitutional scheme be characterized:

> We should not say "A federal state requires such and such relationship between the governments, therefore we shall find them in the Canadian constitution." We should say "This is what the Canadian constitution provides: what kind of federalism is it?"[66]

To answer Frank Scott's question briefly, it would seem that the federalism provided by the 1867 Act is an awkward mix of general and particular powers assigned to two levels of government on an "exclusive" basis.[67] The exclusivity of powers, with broad enumerated powers such as property and civil rights and matters of local and private nature assigned to the provinces, has produced, after 120 years of legislative practice and legal interpretation, a federal system where the constituent provinces are the stronger legislative level.

The central authority in the Canadian federal system, Parliament, has had difficulty establishing a strong legislative role for itself in trade matters in the face of the broad provincial powers. Whether this is appropriate in terms of the federal system in Canada and whether s.91(2) may be given a broader application than has been allowed in the past requires consideration of the underlying principles of Confederation and of the 1867 Act.

The Canadian federating process began in earnest, perhaps, in June, 1864 when the leading political opponents of the two provinces of Canada met and hammered out a statement of intent with regard to a union of the provinces of British North America:

> - The government are prepared to pledge themselves to bring in a measure next session for the purpose of removing existing difficulties by introducing the federal principle into Canada. ... And the government will seek ... to secure the assent of those interests which are beyond the control of our own legislature to such a measure as may enable all British North America to be united under a general legislature based upon the federal principle.[68]

At the conference in London, England, in December, 1866, Sir John A. Macdonald said of the Confederation resolutions passed at the conference in Québec City in 1864 (and slightly modified in London):

> We have given the general legislature all the great subjects of legislation .... [W]e have expressly declared that all subjects of general interest, not distinctly and exclusively conferred upon the local governments and local legislatures, shall be conferred upon the general government and legislature.[69]

Lord Carnarvon, in introducing in the House of Lords the Bill that would become the 1867 Act, said:

> The real object we have in view is to give the central government those high functions and almost sovereign powers by which general principles and uniformity of legislation may be secured in those questions that are of common import to all the Provinces; and at the same time to retain for each province so ample a measure of municipal liberty and self-government as will allow and indeed compel them to exercise these local powers which they can exercise with great advantage to the community.[70]

When the Bill was introduced in the British House of Commons, its sponsor said:

> [B]y these provisions arrangements are made as far as possible for ensuring the unity and strength of the Central Government.[71]

Mr. Cardwell, the Colonial Secretary, said the local (provincial) legislatures were only allowed to deal with questions "which are supposed to be local".[72]

From the foregoing it would appear that the object of Confederation, broadly speaking, was a federation of provinces with a strong central government on matters of general concern to the federation and with legislative autonomy for each of the provinces on matters of local or provincial concern.[73]

The general interest versus local interest rule would seem a sensible and straightforward rule on which to base a federation of autonomous colonies. Studies on theories of federalism indicate that this rule is the basic tenet of federalism as a system of government.

A year before the Fathers of Confederation met at Quebec City in 1864, a British historian of the day, E.A. Freeman, offered his definition of a "perfect form of federal government":

> On the one hand, each of the members of the Union must be wholly independent in those matters which concern each member only. On the other hand, all must be subject to a common power in those matters which concern the whole body of members collectively.... [74]

In the same year, 1863, the French anarchist philosopher, Pierre-Joseph Proudhon (1809-1865), published his Du Principe fédératif.[75]

For M. Proudhon, political order of any kind depended on balancing two "contrary" principles: authority and liberty:

> What I have to say is: that all political constitutions, all systems of government, including federations, fall within the scope of one formula, the balancing of authority by liberty, and vice versa.[76]

It is the contract, the political contract, that provides the mechanism by which the forces of authority and of liberty are balanced or reconciled in a federation.[77]

More recently, in 1964, the American political scientist, William Riker, defined a federal state as one where (a) two levels of government rule the same land and people, (b) each level has at least one area of action in which it is autonomous, and (c) there is some guarantee of the autonomy of each government in its own sphere.[78] A federal constitution arises as a result of a "political bargain" by which distinct territories accept some degree of central control while retaining some degree of autonomy.[79]

In his 1972 study of modern political constitutions, C.F. Strong concluded that a true federal state requires two conditions for its formation: (a) a sense of nationality among the federating units, and (b) though desiring union, not desiring unity:

> [A] federal constitution attempts to reconcile the apparently irreconcilable claims of national sovereignty and state [provincial] sovereignty .... Whatever concerns the nation as a whole is placed in the care of the national or federal authority; whatever concerns the states individually, and is not of vital moment to the common interest, is placed under the control of the government of each state. This division of powers...is the essential characteristic of the federal state.[80]

M.J.C. Vile, in a 1973 study on federalism for the British Commission on the Constitution, identified two basic characteristics to federalism. First, the two levels of government enjoy, as a matter of constitutional guarantee, an independence of each other. Second, the constitutional and political system links the two levels with a significant degree of interdependence.[81]

Thus, the foregoing theoretical studies of federalism suggest the following typical characteristics:

(1) a division of legislative powers between, on the one hand, a common central authority on matters that concern the member states collectively and, on the other, the autonomous member states on matters that concern the member states alone;

(2) a reconciliation of central authority and member state liberty or autonomy through a federating political contract or bargain;

(3) a sense of nationality among the federating member states;

(4) an interdependence between the two legislative levels; and

(5) a set of basic ground rules of constitutional and political action with mechanisms for change regarding the division of powers.

The third and fifth characteristics do not concern us here. The bargain or contract may be taken as the 1867 Act, the end result of the Québec and London Resolutions. It is the first and fourth characteristic that interest us here. The first is the general interest versus local interest rule discussed earlier. The fourth, interdependence, is not often discussed in the constitutional law context but is basic to any constitutional jurisprudence that aspires to reconcile, on a reasoned basis, the contending forces of central authority and member state autonomy.

Interdependence, simply put, is a relationship of dependency which arises between persons or entities that form an association to attain objectives that each of the persons or entities cannot attain alone. The parties to the relationship or the members of the association have recognized a collective interest and have become associated and dependent on one another for the sake of benefits to be secured by virtue of their association.

In a federal state such as Canada, national and provincial interests --economic, social and, certainly, financial-- do not co-exist in splendid isolation from one another. Basic to the Canadian federal system, as with any other federal system as well, is the constitutional and legislative interdependence of the two levels of government.

The interdependence of two legislative levels in a federal system of government may be taken as a fundamental and underlying constitutional principle and, as such, is implied in the 1867 Act. Recognition and application of underlying constitutional principles is not something new to the Court. In other contexts, the Court has accepted and applied such underlying principles.

In Patriation Reference (1981), although the Court rejected theories of federalism as sufficient to alter the law ("Theories of federalism do not engage the law."), it accepted, as a matter of constitutional convention, that amendment of the 1867 Act by the British Parliament could not be sought by the federal government, based on resolutions of the House of Commons and of the Senate of Canada, however lawful this process may otherwise be, without substantial agreement with the provinces ("The reason for the rule is the federal principle.").[82] In support, the Court quoted the Privy Council dicta of Lord Watson in Liquidators of the Maritime Bank of Canada v. Receiver-General of New Brusnwick (1892):

> The object of the [1867] Act was neither to weld the provinces into one, nor to subordinate provincial governments to a central authority, but to create a federal government in which they should all be represented, entrusted with the exclusive administration of affairs in which they had a common interest, each province retaining its independence and autonomy.[83]

The Court invoked the "federal principle" as an underlying constitutional principle that regulated how the two legislative levels are to conduct themselves on constitutional matters.

In Manitoba Language Rights (1985), the Court approved the approach taken in Patriation Reference. Chief Justice Dickson, on behalf of the Court, after reviewing the reasons expressed in Patriation Reference, concluded as follows:

> [I]n the process of Constitutional adjudication, the Court may have regard to unwritten postulates which form the very foundation of the Constitution of Canada. In the case of the Patriation Reference, supra, this unwritten postulate was the principle of federalism. In the present case it is the principle of Rule of Law. [84]

It would appear that the Court is prepared, in an appropriate case, to search out and apply underlying constitutional principles that are not self-evident on a simple reading of the provisions of the 1867 Act.

It remains, then, to identify the operative underlying principle that arises from the constitutional interdependence of the two legislative levels. A possible principle is one that might be called the "federal imperative".

The federal imperative, as a concept, is not unlike the concept of "federal fidelity" (sometimes referred to as "federal comity") that has been developed by the constitutional court of the Federal Republic of West Germany. Both concepts govern or regulate the relationship between the legislative powers of the two levels of government. The two concepts are alike in that each attempts to reconcile the conflict that is basic to a federal system of government: the conflict between central authority and provincial or member state autonomy.

The West German doctrine of "federal fidelity" is based on the principle of "bundestreue" or federal comity. The doctrine is sometimes described as the doctrine of federal good faith or friendly federal behaviour. It is said that the doctrine is addressed less to the content of legislative powers than it is to the method of exercising the powers.[85] The member states (Land) are required to have regard to the interests of each other and of the federation (the Bund) as a whole and to not embark on mutually harmful courses.[86] The remedy for jurisdictional conflict must be found in the inner harmony of the West German constitution and the principle of federal comity must be relied upon to resolve the conflicts.[87]

Canadian federalism, by comparison with that of West Germany, may be more a co-ordinate federalism than a co-operative one as in West Germany. A co-ordinate federal system is one where the respective powers of the two levels are treated as exclusive. The judicial approach in a co-ordinate system is to protect the federal structure from mutual interference by the two levels and to restrict the reach of central powers so as not to encroach unduly on provincial powers. Canada has been described as "a notable case" of a co-ordinate rather than a co-operative federal system.[88]

As federal fidelity mandates co-operation so that the West German federation can function in its collective interest, the federal imperative mandates acceptance by the Canadian provinces of federal action. For its application, the federal imperative requires that (a) the matter legislated at the federal level be capable of falling within one of the general powers of the central authority, (b) the legislative action be necessary due to provincial legislative inaction or incapacity and (c) the action be taken in the collective interest of the federal state. In short, the federal imperative, based on the constitutional interdependence of the two legislative levels and of the provinces inter se, means the central authority has jurisdiction to regulate matters that, in the collective interest of the federal state, must be regulated by the central authority.

As mentioned earlier, the central legislative authority in a federal state, broadly speaking, has power to legislate on matters of general concern to the federation as a whole. The federal imperative adds to this general proposition, in the case of Canada, the gloss that the federal level can regulate a matter that is otherwise within provincial jurisdiction, that is to say, can regulate a matter that falls within a provincial power enumerated in s.92 where the provincial power has been "carved out" (Parsons) of a federal power enumerated in s.91.

Where Parliament so acts, the provinces must honour the legislation where it is enacted in the collective interest and on a matter that cannot be effectively regulated by provincial legislative action.[90] The federal imperative does not create new federal legislative capacity. Rather, it returns to the federal level the legislative capacity it had by virtue of an enumerated power in s.91 before the provincial powers enumerated in s.92 were "carved out".

The "subtraction" approach to s.91(2) was adopted by Justice Dickson in C.N. Transportation, following an earlier example offered by Justice Rand in Ontario Farm Products. Indeed, the federal imperative principle is implied in the dicta of Justice Dickson (as he then was) in C.N. Transportation:

> A different situation obtains, however, when what is at issue is general legislation aimed at the economy as a single integrated national unit rather than as a collection of separate local enterprises. Such legislation is qualitatively different from anything that could practically or constitutionally be enacted by the individual provinces either separately or in combination.[90]

In C.N. Transportation, Justice Dickson said there must be a constitutional balance between the two levels. To date, federal trade power under s.91(2) has usually been found insufficient to override provincial trade-related powers under either s.92(13) or s.92(16). It is hoped that the federal imperative, as a constitutional principle would provide a constitutional counterweight to these provincial powers. The federal imperative principle offers "a check and a balance," as it were, to the federal principle that was applied in Patriation Reference on behalf of the provinces. The federal principle ought not to provide protection to provincial powers where, in doing so, it causes the collective interest of the federal state to be neglected.

The federal imperative does not stand alone in its support of s.91(2) as a general trade power. The inclusion of the "common market" provision of s.121 and, to a lesser extent, of the concurrent powers over immigration and agriculture in s.95, along with assignment to Parliament of such economic powers as currency, banking, legal tender and customs and excise, seems to confirm an intention to establish a central regulatory basis for a national economy.[91] The 1867 Act seems to recognize the need for a central authority with legislative powers appropriate to the regulation of a national economy in the collective interest of the constituent provinces.[92]

The preponderance of economic powers at the federal level is indicative of a federal design wherein Parliament is to exercise regulatory control over those economic matters that enable the economy to work as a national system that operates for the benefit of the federated provinces and territories together. Banking, coinage and currency (to name only a few specific examples) are essential to the continued viability of a national economic system. It would seem unnecessary, as a matter of constitutional design, to specifically assign these economic powers to Parliament if one was not concerned about establishing an integrated (systemic) national economy out of the regulatory regimes that had developed before Confederation in each of the colonies of British North America.

IV INSURANCE AS A FEDERAL TRADE MATTER

Introduction

Although the central proposition of this paper relates to financial institutions generally, the regulation of life insurance companies, as a jurisdictional question, warrants particular attention. If Parliament has jurisdiction to regulate life insurance companies as financial intermediaries, jurisdiction over trust companies and investment dealers ought to follow on the same basis. Banks (and banking), for their part, are already assigned to Parliament under s.91(15).

The conventional legal view, based on the so-called insurance cases decided in the privy Council between 1881 and 1932, is that insurance is a matter within exclusive provincial powers. One needs to ask, however, what the term "insurance" includes here. Does it include the business activities or functions of insurance companies generally?

It seems reasonable that insurance, as a matter of contract, is a matter within s.92(13), property and civil rights in a province. Moreover, as a consequence of their powers of incorporation, it also seems reasonable that each legislative level can regulate the corporate affairs of the corporations that it incorporates. It does not seem reasonable, however, that, because insurance as a matter of contract is within provincial powers, the business of insurance companies is within provincial regulatory control.

In a similar fashion, it does not seem reasonable that because a provincial or federal insurance company is under provincial or federal regulatory control as to its corporate affairs, that its business activities are necessarily under the same control. When analysed in these terms, the so-called insurance cases, as we shall discuss in this Part, are seen to be of limited relevance to the regulation of insurance companies as financial institutions engaged in the business of financial intermediation.

Consideration of the legal question of federal jurisdiction to regulate insurance companies as financial institutions would not be complete without some attention being given to the factual basis on which the proposition would be based. The application of s.91(2) as a federal trade power depends, in part, on the answer to one central question of fact: is the business of life insurance companies, properly considered, one of financial intermediation? In this Part we shall look at some recent trends and statistics with respect to the business of insurance companies so as to indicate the kind of factual material that might be marshalled for presentation to the Court in support of the proposition of fact that the business of life insurance companies is financial intermediation and not simply the selling of insurance policies.[93]

The Insurance Cases: 1881-1932

The conventional view with respect to jurisdiction over insurance, that is, that insurance is a matter within exclusive provincial powers under s.92(13), has evolved from only a handful of cases, the last of which was decided in 1932.[94] These insurance cases do not provide a legally useful analysis of insurance <u>per se</u> or of the business of insurance companies.

In the insurance cases, insurance and the business of insurance companies are treated as matters of contract and of corporate capacity, respectively, and thus within s.92(13), property and civil rights in the province. The larger jurisdictional question, namely, whether jurisdiction over contracts of insurance includes jurisdiction over insurance companies as financial institutions or over the business of insurance companies generally, was not addressed by the Privy Council and has yet to be considered by the Court.[95]

Although often cited as the starting point on s.91(2) generally, <u>Parsons</u> is also the starting point on insurance as a jurisdictional question. In <u>Parsons</u>, provincial fire insurance legislation, imposing statutory conditions applicable to all fire insurance policies sold in the province (Ontario), was being applied to the Citizens Insurance Company of Canada, a federal insurance company. It was argued that a federal insurance company is not subject to provincial legislation. Sir Montague Smith, on behalf of the

Privy Council, in rejecting this argument, said the provincial legislation did not interfere with the "constitution or status" of the federal company:

> It deals with all insurers alike, including corporations and companies, whatever maybe their origin, whether incorporated by British authority... or by foreign or colonial authority, and without touching their status, requires that if they choose to make contracts of insurance in Ontario, relating to property in that province, such contracts shall be subject to certain conditions.[96]

Counsel also argued that the provincial legislation was inconsistent with the federal insurance Act which required fire insurance companies to obtain licences from the federal minister of finance as a condition to carrying on the business of insurance in Canada and that where a company had a federal licence, it was beyond the competence of a provincial legislature to subject such a company to the imposition of manadatory conditions. Sir Montague rejected this argument also:

> [T]he [Ontario] legislation does not really conflict or present any inconsistency. The statute of the dominion parliament enacts a general law applicable to the whole dominion, requiring all insurance companies, whether incorporated by foreign, dominion, or provincial authority to obtain a licence from the minister of finance, to be granted only upon compliance with the conditions prescribed in the [federal] Act. Assuming this Act to be within the competency of the dominion parliament as a general law applicable to foreign and domestic

> corporations, it in no way interferes with the authority of the legislature of the province of Ontario to legislate in relation to the contracts which corporations may enter into in that province.[97]

In the Supreme Court of Canada, Chief Justice Ritchie, with the majority, relied on s.92(16) in upholding the provincial legislation:

> In my opinion, this Act has no reference to trade and commerce in the sense in which these words are used in the British North America Act. It is simply an exercise of the power of the local legislature for the protection of property in Ontario, and the civil rights of the proprietors thereof in connection therewith, by securing a reasonable and just contract in favor of the parties insuring property, real or personal, in Ontario, and deals therefore only with a matter of local and private nature.[98]

The question of whether insurance could be considered a trade within s.91(2) was considered at both levels. Henry, J., with the majority of the Court, discussed the distinction to be made between trade as an activity and personal rights that arise from, or are affected by, such activity:

> "Trade" means the act or business of exchanging commodities by barter, or the business of buying and selling for money-commerce-traffic-barter; it means the giving of one article for another for money or money's worth. "Commerce" is only another term for the same thing. Neither of the terms includes the rules of law by which parties engaged in trade or commerce are bound to each other, and when their regulation is given to a legislative body, it must be assumed the

> intention was that control in some respects was to be exercised, but to what extent, we must judge in this case by taking the whole Act into consideration. I have no doubt that the Dominion Parliament has power to enact general regulations in regard to trade and commerce, but not to interfere with the powers of the local legislatures in the matter of local contracts, amongst which is properly included policies of insurance against loss by fire on property in the same province.[99]

In the Privy Council, Sir Montague addressed the question of whether the business of insuring buildings against fire was a trade:

> This business, when carried on for the sake of profit, may, no doubt, in some sense of the word, be called a trade. But contracts of indemnity made by insurers can scarcely be considered trading contracts, nor were insurers who made them held to be "traders" under the English bankruptcy laws; they have been made subject to those laws by special description. Whether the business of fire insurance properly falls within the description of a "trade" must, in their Lordships' view, depend upon the sense in which that word is used in the particular statute to be construed.[100]

Sir Montague concluded by saying that their Lordships did not find it necessary to rest their decision on the "narrow ground" that the business of insurance is not a trade.

The Supreme Court of Canada in Parsons upheld the Ontario fire insurance legislation because the fire insurance to which the legislation applied related to property situated in the province amd, for this reason, related to a matter of property and civil rights under s.92(13) and a matter of a local or private nature under s.92(16). For its part, the Privy Council relied on a distinction between corporate status and rights, on the one hand, and rights of contract, on the other, to uphold the provincial fire insurance legislation.

Insurance next appeared before the Privy Council 35 years after Parsons. In Insurance Reference (1916) the Privy Council struck down the federal Insurance Act of 1910 which had required that all insurers, except provincial companies doing business wholly within their incorporating province, have a federal licence before engaging in the business of insurance anywhere in Canada.[101] Unfortunately for the legislation, the exeption did not apply to an unincorporated individual who might carry on the business of insurance within a province.

Viscount Haldane said the 1910 Act interfered with exclusive provincial jurisdiction over civil rights under s.92(13), in two respects. First, the Act prevented an individual, but not a provincial company, from carrying on the business of insurance within a province without a licence. Second, and more important for our purposes, the prohibition against a provincial company doing business outside the province of incorporation was an interference with its corporate capacity to take advantage of powers and rights proffered to it by authorities outside the provincial limits:

> Such an interference with [the provincial company's] status appears to their Lordships to interfere with its civil rights within the province of incorporation, as well as with the power of the Legislature of every other province to confer civil rights upon it.[102]

Viscount Haldane rested his civil rights argument on the Privy Council's decision (handed down earlier the same day by Viscount Haldane) in Bonanza Creek.[103]

Bonanza Creek (1916) involved a federal statutory provision that applied to companies incorporated "under a Canadian charter". An Ontario mining company was being denied mining rights in the Yukon by federal authorities on the ground that the company was not capable of acquiring rights outside Ontario because it was not incorporated "under a Canadian charter".

In the Supreme Court of Canada, Justice Duff decided that provincially incorporated companies were companies incorporated "under a Canadian charter" and so were entitled to receive a federal license under the legislation. The Privy Council agreed and went on to consider "the larger question", i.e.,

> whether a company incorporated by provincial letters patent, issued in conformity with legislation under section 92 of the British North America Act, can have the capacity to acquire and exercise powers and rights outside the territorial boundaries of the province.[104]

Viscount Haldane in Bonanza Creek said that s.92(11), "the incorporation of companies with provincial objects", limited a province's legislative and executive powers to granting corporate powers and rights in respect of objects inside the province, but that this restriction did not affect

> the ability of the corporation, if otherwise adequately called into existence, to accept such powers and rights if granted ab extra.[105]

The 1867 Act, per s.92(11), limited the "actual powers and rights" that a province can grant to such powers and rights as are "exercisable within the province":

> But actual powers and rights are one thing and capacity to accept extra-provincial powers and rights is quite another.[106]

The important distinction in Bonanza Creek is the distinction made between a provincial corporation's capacity to acquire powers, which is virtually unlimited, and its capacity to exercise powers, which is limited.

In Insurance Reference, Lord Haldane struck down the federal insurance legislation because, in requiring a provincial company to first obtain a federal license before it engaged in insurance business outside its province of incorporation, the legislation interfered with the corporation's natural capacity to acquire powers and thus legislated on a matter of civil rights:

> In other words, the capacity is interfered with which, according to the judgment just delivered by their Lordships in the case of the Bonanza Company, such a company possesses to take advantage of powers and rights proffered to it by authorities outside the provincial limits. Such an intereference with its status appears to their Lordships to interfere with its civil rights within the province of incorporation, as well as with the power of the Legislature of every other province to confer civil rights upon it.[107]

Viscount Haldane's "larger question" of corporate capacity in Insurance Reference, based on Bonanza Creek, enabled the civil rights argument to obscure the real constitutional question, namely, whether the federal insurance legislation may be valid, not for who it regulates (provincial companies or federal companies) but for what it regulates, i.e., insurance.

In an earlier Privy Council decision, Russell

(1882), the Privy Council had upheld federal temperance legislation under the introductory words of s.91, "peace, order and good government". The Privy Council in that case felt the federal legislation dealt with a matter which was outside the subject matters enumeratively entrusted to the provinces under s.92 of the 1867 Act.[108] The federal Insurance Act, 1910, however, could not be justified on the same grounds:

> No doubt the business of insurance is a very important one, which has attained a great dimension in Canada. But this is equally true of other highly important and extensive forms of business in Canada which are to-day freely transacted under provincial authority. Where the British North America Act has taken such forms of business out of provincial jurisdiction, as in the case of banking, it has done so by express words which would have been unnecessary had the argument for the Dominion Government addressed to the Board from the Bar been well founded.[109]

In the Court below, Justice Duff said the fact that the insurance business had grown "to great proportions" did not affect the question of jurisdiction:

> The question is: On what ground can it be contended that this is a matter which because of its importance has ceased to be substantially of local interest?[110]

Without answering his own question, Justice Duff went on to say the 1910 Act

> illustrates the extremes to which people may be carried when acting upon the theory that because

> a given matter is large and of great public importance it is for that reason a matter which is not substantially local in each of the provinces.[111]

The 1910 Act, said Duff, involved

> a degree of interference with matters "substantially local" that could not have been contemplated by the framers of the [1867] Act.[112]

Justice Duff did not cite evidence or offer a conceptual basis in support of his conclusion that the insurance business was "substantially local".

<u>Reciprocal Insurers</u> (1924) and <u>Re Insurance Contracts</u> (1926) struck down the federal insurance legislation of 1917.[113] In this legislation, Parliament had tried to get around its earlier jurisdictional defeat in <u>Insurance Reference</u> by framing the legislation, in <u>Reciprocal Insurers</u>, within the criminal law power under s.91(27) and, in <u>Re Insurance Contracts</u>, within the federal power over aliens under s.91(25). In both cases, the legislation was considered a colourable attempt to do indirectly what <u>Insurance Reference</u> in 1916 had established that Parliament could not do: legislate on the business of insurance.

Is this what <u>Insurance Reference</u> had decided in 1916? It is not. The 1916 case decided that the federal insurance legislation of 1910 interfered with civil rights in the province and so was invalid. The case did not decide that insurance was a matter within exclusive provincial jurisdiction.

In Re Insurance Act (1932) the Privy Council decided what it hoped would be "the last of the series of litigations" on insurance.[114] Viscount Dunedin, speaking for the Privy Council, held the federal legislation to be invalid:

> [T]he sections here ... do not deal with the position of an alien as such; but under the guise of legislation as to aliens they seek to intermeddle with the conduct of insurance business, a business which by the first branch of the 1916 case has been declared to be exclusively subject to Provincial law.[115]

Is this what Insurance Reference in 1916 decided? Again, it is not.

In Re Insurance Act, Viscount Dunedin cited Parsons as confirming provincial jurisdiction over

> the way in which insurance business or any other business shall be carried on in the Provinces.[116]

With respect, this language does not accurately summarize the ratio decidendi of Parsons. The case established only that regulating a particular trade in a province is not within s.91(2). Whether this includes the business of insurance companies beyond the selling of insurance was not considered.

In the court below, the King's Bench of Quebec, Howard, J., voting with the majority in upholding the federal insurance legislation, said he saw no "logical principle" by which to distinguish the granting of a license to an alien insurer on such conditions that he pay fees, submit to inspections, etc., which is within federal powers, and the granting of a license on condition that only certain kinds of contracts be entered into by the alien insurer in Canada:

> That, to my mind, is not an interference with property or civil rights in any Province which the alien may enter. The citizen of that Province will find that, when he plans to take out a policy with the foreign company, he will be asked to agree to certain conditions in the policy. He has no "civil right" to demand another sort of contract from the company with different conditions, whether the conditions contained in the policy were inserted by the company of its own volition or at the request of the Dominion.[117]

The Privy Council on appeal did not respond to this view.

Federal power to regulate the contracts of federal companies did not mean that provincial powers over the business of those companies, when carried on in the province, was diminished as a result. Justice Howard agreed with Smith, J.A. of the Ontario Court of Appeal in Re Insurance Contracts (1926), that a province, by virtue of its jurisdiction over civil rights, could prohibit contracts of the kind that a federal insurance company, under federal regulation, may be obliged to make. This view was not addressed by the Privy Council on appeal.

In Re Insurance Act, the Privy Council seemed to accept as settled, without considering the question afresh, that a province had exclusive and virtually unqualified jurisdiction over the insurance business when carried on within its territory. Moreover, it would appear that the business of insurance was seen essentially as the selling of policies of insurance.

The earlier insurance cases confirmed three propositions. The first, established by Parsons, is that s.91(2) does not enable Parliament to regulate a particular trade (e.g., the selling of fire insurance) carried on in a province. The second, established by Insurance Reference, is that the federal powers do not include the power to regulate provincial companies, even where the companies do business outside the province of incorporation as this would amount to an interference with their civil rights. The third, confirmed by Reciprocal Insurers, Re Insurance Contracts and Re Insurance Act, is that Parliament cannot do indirectly what it cannot do directly. Local trades and civil rights are to be protected from federal regulatory encroachment. Parliament cannot by "colourable" legislation encroach on these fields of exclusive provincial jurisdiction. These insurance cases do not decide that the business of insurance is a subject matter within exclusive provincial jurisdiction.

The business of selling insurance policies, on the one hand, and the business of insurance companies, on the other, ought to be distinguished for jurisdictional purposes. The former is carried on by insurance agents and brokers as a local business or trade activity. The latter is carried on by corporations that, by virtue of their substantial capital resources, are able to act as insurers.

Insofar as the insurance agent or broker sells insurance coverage that is offered by an insurance company, the business of the agent or broker is dependent on that of the insurance companies. Similarly, the business of an insurance company, in part, depends on the sale of policies of insurance by agents and brokers. This interdependence of two related fields of trade activity ought not to cause them to be treated as one for purposes of legislative jurisdiction. The words "the business of insurance" have served as a convenient phrase by which these two but distinct business or trade activities have been described as if they are one and the same business or trade activity.

It remains for the Court to decide, as a question of law, whether and to what extent the business of insurance companies, as distinct from the business of selling policies of insurance, falls within federal jurisdiction under s.91(2).[118] The so-called insurance cases are not binding or persuasive precedents with respect to the regulation of insurance companies as financial institutions. The cases do not turn on an analysis of the business of insurance companies as a legislative subject matter but rather on Lord Haldane's emphasis on civil rights as a field of exclusive provincial power.

Civil rights, as the dominant jurisdictional field, may now be past its jurisdictional prime, however. In Multiple Access (1982), federal legislation imposed a civil liability for insider trading in the shares of a federal corporation to which the legislation applied.[119] It was argued that such a provision created civil rights or obligations which can only be the subject matter of provincial legislation in relation to property and civil rights in a province. The Court, per Dickson, J. (as he then was), said the impugned provision imposing civil liability had a "rational, functional connection" with company law which was the subject-matter of the federal legislation and had been found to be within Parliament's jurisdiction. Therefore the civil liability provision, by virtue of this connection, was itself valid federal legislation.

In Québec Ready Mix (1985), the Federal Court of Appeal applied Multiple Access in support of federal competition legislation that provided civil remedies against persons who contravened the legislation.[120] Mr. Justice MacGuigan, on behalf of the Federal Court of Appeal, commented that the authority of Privy

Council decisions on s.91(2) by Lord Haldane, such as Insurance Reference (1916), "has been greatly diminished" and that what "remains relevant of the Haldane approach" to constitutional interpretation has been incorporated in the recent decisions of the Court on such matters.[121]

Justice MacGuigan quoted the remarks of Dickson, J., in Multiple Access with respect to a "rational, functional connection" and added:

> I believe this is to say that such a civil remedy must be genuinely and bona fide integral with the over-all plan of supervision. The precise balance of governmental regulation and private enforcement is, then, a matter of policy for Parliament....
>
> Within reasonable limits indicated, Parliament must be free to adopt and even to experiment with various approaches to the regulation of the economy. From their respective perspectives, both the courts and Parliament must respect those reasonable limits. That, it seems to me, is of the essence of the federal framework which defines the expression of democracy in Canada.[122]

The civil remedy provision, concluded the court, had a rational functional connection

> with the over-all federal economic plan manifested in the Act in relation to competition.[123]

The dicta of Justice McGuigan in Québec Ready Mix regarding an "overall plan of supervision" and an "over-all federal economic plan" is reminiscent of the dicta of Chief Justice Laskin in Vapor Canada (1977) where the Chief Justice spoke of a

> general regulatory scheme to govern trading relations going beyond merely local concern.[124]

If this "rational, functional connection" test were applied to the federal insurance legislation that appeared before the Privy Council in Insurance Reference (1916), could Lord Haldane have struck down the legislation because it required an insurance company doing business outside its "home" province to obtain a federal licence? The answer would depend on how the federal legislation is framed, whether the legislation reflected, to use Justice MacGuigan's words in Québec Ready Mix, an "over-all federal economic plan" with respect to, say, the financial services industry in Canada, that is, with respect to the business of insurance companies as financial intermediaries doing business as a part of the national financial system.

Even where federal legislation is framed to reflect the regulation of financial institutions, including insurance companies, as financial intermediaries, the Court might nonetheless ask, as a preliminary question of fact, whether the business of insurance companies, for example, is one of providing insurance coverage through policies of insurance sold locally by agents and brokers or is one of financial intermediation taking place at the interprovincial or transprovincial level.

If the Court accepts the proposition that the business of insurance companies is financial intermediation and accepts that financial intermediation is a legislative subject matter falling within federal powers under s.91(2), the issues are then reduced, according to Multiple Access and Québec Ready Mix, to whether a particular aspect or provision, such as mandatory policy conditions, has a "rational, functional connection" to an "overall federal economic plan".

It remains, however, that the nature of the business of insurance companies, as a factual matter, is important to the constitutional question of federal jurisdiction under s.91(2) over insurance companies as financial institutions. The jurisdictional argument depends on acceptance of the fact that the business of insurance companies is something other than the local sale of policies of insurance.

The business of insurance companies, as a factual matter, is not the central concern of this paper on the legal question of constitutional control of financial institutions by Parliament. The factual contention that the business of insurance companies is more than the selling of insurance is a mere supposition that is presumed for purposes of examining the legal question. It would seem appropriate, however, that this supposition receive some consideration here, if only to indicate, first, the kind of material that could be presented to the Court, albeit more cogently organized and thoroughly researched, in support of the factual contention and, secondly, to indicate that the factual premise on which the jurisdictional argument is based is not fanciful.

Insurance as a Business

In the 1970's, with the first oil price shock of 1973, inflation was on the increase and interest rates became uncertain and, on average, higher. Interest rate uncertainty caused lenders and borrowers to shorten the terms of liabilities and assets acquired in financial intermediation. This shortening of terms had adverse effect on institutions such as life insurance companies that specialized in long-term financial liabilities such as life insurance policies.[125]

It is suggested that in recent years the market for life insurance, as distinct from annuities, reached a saturation point in Canada and that life insurance companies have had to face strong competition from other financial institutions for a share of the saver's dollars, at a time of dramatic changes in the way the financial markets function.[126]

Life insurers' share of personal savings has dropped from 13.7% in 1976 to 11.9% in 1983 while their share of Canadian assets of major savings-type institutions in Canada has dropped from 21.4% in 1971 to 14.5% in 1983.[127] As for total financial system assets in Canada, in a comparison of the years 1967 and 1982, the share of contractual savings institutions such as life insurance companies declined from 17% to

8.3%, while the share of deposit-taking insitutions generally increased, in the case of chartered banks from 32% to 37.1% and of co-operatives from 4.4% to 6.7%.[128]

In response, life insurers have developed personal short-term deferred annuities which are much like savings accounts traditionally held by banks or term deposits and guaranteed investment certificates offered by trust companies.[129]

The development of competitive, short-term investment/savings vehicles by insurance companies appears to have begun with the arrival of what are called "segregated funds". These funds are an accumulation of the savings or investment component of life insurance policy premiums, under policies other than whole life policies. The insured usually has a fixed premium payment, but has a choice of segregated funds into which the savings or investment component of the premium may be placed. According to an insurance company executive:

> The excess money in the product is working for you at the market rate, and the return will depend on investment performance.[130]

Segregated funds are kept separate from the company's other financial transactions and are not used to pay debts or dividends. Although segregated funds have been around for about 20 years, the use of these funds in the stock market is new. More importantly, insurance companies have begun to sell segregated funds separate from life insurance. In such cases, the funds are offered as deferred annuities and operate like conventional mutual funds.

Thus, by reaching into areas outside their traditional area of business, life insurance companies have innovated to protect their share of the savings market. According to the president of Mutual Life Assurance Company of Canada:

> It's not understood, the swing of the insurance companies away from just insurance products. In 1975, 60% of our premium income was from life insurance, 15-20% was from health insurance and the rest from savings. Now, 60% of our premium income is from savings products.[131]

By 1981, annuity revenues for life insurers were 61% of total direct premium income received by the industry in Ontario, up from 31% in 1971.[132] By 1985, annuities represented 59% of total net premium income in Canada for life insurance companies, up from less than 50% in 1980 and prior years. As much as 49% of this annuity income represents premiums under personal annuity contracts.[133] Life insurance premiums in Ontario, in 1981, amounted to $1.3 billion while revenues for annuities amounted to $2.1 billion. In the period 1971-1981 in Ontario, life insurance premiums increased at an annual average rate of 7.9% while annuities increased at a rate of 22%.[134]

Perhaps the most striking feature of the insurance industry in Canada, in relation to the question of legislative jurisdiction, is the extent to which the industry has developed "voluntarily" as a federally regulated industry, this despite the long-standing conventional view that insurance is a matter within exclusive provincial jurisdiction.

As much as 92% of all life insurance in force (in dollar value) at the end of 1985 was held by federally registered companies.[135] In 1984 federal life insurance companies, constituting approximately 80% of all life insurance companies in Canada, held 91% of all assets held by life insurance companies.[136]

At December 31, 1984, of 257 life insurance companies doing business in Canada, 199 were federally regulated and 58 were provincially regulated.[137] Federal regulatory powers over corporations that Parliament creates, coupled with federal control over foreign companies entering Canada to do business here, have enabled federal regulators to acquire substantial regulatory control over insurance companies generally and, as a result, their business activities.

In 1985, federal companies received 92.8% of insurance premium dollars received by all life insurance companies.[138] As for the premium dollars earned by provincially incorporated companies, 89.7% were earned within the province of incorporation.[139] According to E.P. Neufeld (1972), the business of provincial life insurance companies has never exceeded 10% of that of federal companies.[140]

The limited market share of provincial insurance companies is illustrated by Québec companies in 1986. Of 150 life and health insurance companies doing business in the province, only 15 were incorporated under Québec laws. Québec life insurers held only 3.1% of the assets held by insurers licensed to do business in the province, compared to 83.3% held by federally incorporated companies and 12.8% by foreign companies.[141]

In 1986, Québec companies collected 20.9% of the life and health insurance premiums collected in the province, compared to 62.3% collected by federally incorporated companies and 16% by foreign companies. While the Québec companies had 20.9% of the market share in Quebec, these same companies had virtually no market share in any of the other provinces.[142] Québec charter life insurers collected 92.8% of their premium income from within Québec.[143]

Thus it might be shown to the Court, first, that insurance companies sell more than insurance policies, that they actively compete for funds from savers who are looking to invest their money for a later return. Second, it might be shown that the business of most insurance companies is conducted in two or more provinces. Finally, it can be shown that federal insurance companies already far outnumber and, in fact, dominate provincial companies.[144]

It does not seem unreasonable to suggest, therefore, that as a point of fact the business of insurance companies is one of financial intermediation and that this business is not carried on, if it ever was, as a local trade within a single province.

V FEDERAL REFORMS: 1986 - 1988

The Four Pillars: Changing Times

According to the four pillars philosophy for the regulation of financial institutions, the integrity of the financial system depends on maintaining the separation and independence of each "pillar" or category of institution. A financial institution whose core function falls under one pillar should not also do business under one of the other pillars. Insurance companies, for example, that have a duty to meet future contingent liabilities arising under their contracts of insurance, should not be allowed to use their premium income to engage in lending money (banking) or in equity investment brokerage (securities investment dealer). A bank should not engage in underwriting lest it use its customers' savings to underwrite securities of doubtful value and give priority to the underwriting business over the duty to invest its customers' savings prudently.

Consistent with the four pillars philosophy, the major financial institutions in Canada are governed by separate statutes according to each of the pillars. Federal insurance companies are governed by the Canadian and British Insurance Companies Act ("CBIC Act") and the Foreign Insurance Companies Act ("FIC Act"), trust companies are governed by the Trust Companies Act and banks by the Bank Act.[145] In this fashion, the financial institutions are kept within their respective categories or pillars.

The four pillars philosophy, as a basis for the regulation of financial institutions, may now be obsolete. Recent market pressures, both domestic and foreign, along with legislative and technological changes, the trend toward the internationalization of financial services, the emergence of financial conglomerates and the growing concentration of ownership are said to have caused a "blurring" of the traditional distinctions between the different kinds of financial institutions.[146]

Technological advances are changing the way financial institutions do business. A 1985 Ontario study on employment and new technology in the insurance industry commented:

> The internal functions of the life insurer have been altered by computerization of actuarial estimates and of insurance policy information, and by the introduction of electronic communication of data within the company. This has enabled the companies to increase their capacity to administer and distribute insurance products and to create the scope for introducing new products. At the same time, theintroduction of electronic funds transfer and the computerization of the operations of other financial institutions has unleashed similar forces in the banks and trust companies. Finally, because Canadian financial insitutions and markets have close ties with those in the United States, there has been a spillover of technological developments from south of the border. All of these changes have put financial markets in a state of turmoil for two reasons:
>
> -The technological change enhances the capacity of each company and each industry to provide financial services,
>
> -Technological change also blurs the distinctions between institutional roles and between financial products.
>
> The net effect is a significant increase in competition for a share of the individual's savings dollar and major strains on the regulatory framework intended to monitor the activites of financial institutions.[147]

A 1984 federal government paper explained technological change in terms of money as information:

> [R]apid technological change seems to have become in recent years an increasingly important factor in at least opening up new possibilities for financial innovation. The technological developments which have affected the financial industry have come with regard to the processing, transmitting and storing of information. Money, and financial products of all types, can be considered a form of information and the technological developments have, therefore, directly affected the creation and manipulation of these products.[148]

According to the executive director of the Bank of England,

> the regulator, in both Canada and the United Kingdom, is responding to global macro-economic, technological and other pressures that have been building up for many years. Among these were the move to floating exchange rates in the early 1970's, the enhanced role of monetary policy in the battle against inflation and, in the United Kingdom case, the abandonment of exchange and other controls in 1979. There has also been the pervasive influence of new technology, similarly global and irresistible in its potential span. Just as the possibility of nuclear Big Bangs eroded the ultimate significance of any national boundary, so also technology in financial services obliges us increasingly to look at the problems and opportunities of the industry on a global basis.[149]

The growth of financial conglomerates in recent years has led to the idea of "one-stop" financial shopping, the "financial supermarket". The consumer of financial services, it is argued, wants to be able to take care of a variety of financial and related matters at the same institution.[150] Also, equity financing has become more prominent as a source of capital for corporations.[151] Banks have seen themselves losing some of their lending business to the equity markets and have sought entry to the underwriting business to service the corporations that formerly had taken out loans.

In the result, a movement is started to promote and, as well, to establish a regulatory regime that permitted delivery of a variety of financial services either by a single financial institution or by a group of related financial institutions. It is soon apparent that the four pillars are cracking, if not crumbling altogether.

The Federal Reforms: new wine in old bottles

On December 18, 1986, the federal government announced legislative proposals for changes to the regulatory system affecting federal financial institutions.[152] Minister of State for Finance, Mr. Thomas Hockin, announced that the federal government proposed a "reform agenda" based on four elements:

> --the integration of the financial services industry through common ownership of institutions and extensions of powers;
>
> --a pragmatic ownership policy which checks the growth of commercial-financial links in the economy while maintaining balanced competition within the financial services sector;
>
> --a stronger framework for prudential regulation; and
>
> --a modern and effective supervisory system.[153]

The minister explained that the proposed removal of cross-pillar ownership restrictions "recognizes market trends towards greater competition among all types of financial institutions":

> The policy recognizes that the financial system worldwide is evolving in a manner that will allow financial institutions in any one of the traditional four pillars to provide, directly or through affiliates or subsidiaries, a full range of financial services. It protects the capacity of Canadian institutions to be effective world-scale participants by bringing financial services in Canada into step with the needs and realities of the market, at home and throughout the world.[154]

Trust, mortgage loan and insurance companies are to receive "significantly increased powers" to enable them to undertake consumer and commercial lending. Banks and insurance companies shall have increased powers to exercise trust powers. Non-bank financial institutions will be given the status of natural persons and the formulation of their powers will be adjusted accordingly.[155]

There are four major features to the federal legislative reforms to date.[156] First, the supervisory powers of the Canada Deposit Insurance Corporation ("CDIC") are strengthened considerably. Second, a new federal supervisory office, the Office of the Superintendent of Financial Institutions ("SFI") is is created with considerable supervisory powers with respect to federal financial institutions. Third, federal financial institutions are allowed to engage in the business of securities trading. Fourth, corporate powers are broadened to enable cross-pillar activity.

The federal legislative reforms are a continuation of the existing legislative framework. Parliament continues to regulate trust companies _qua_ trust companies and insurance companies _qua_ insurance companies, although the federal legislation, even as amended by these latest reforms, applies only to federally incorporated trust, loan and insurance companies.

Notwithstanding their adherence to the established jurisdictional framework, the federal reforms are capable of reaching into provincial regulatory fields by virtue of the power given to federal institutions to hold an interest in, or to own outright, a provincially incorporated financial institution. Parliament, through the CDIC or the SFI, can indirectly regulate a provincial institution through the federal parent or affiliate.[157]

According to the Canadian Life and Health Insurance Association, the draft Trust and Loan Companies Act

> introduces the concept of exporting its regulatory framework, if not in a compulsory way then at least in a highly persuasive way, to all financial institutions affiliated with the trust company. To summarize, the Federal Government is trying to promote the institutional test with the draft Trust and Loan Companies Act just as it did with the Kwinter-Hockin securities accord [April 28, 1987, see fn.3, infra]: it wants to control the institution and its peripheral intersectorial activities.[158]

The indirect regulatory reach of the federal reforms into the provincial domain may simply reflect a lack of political will at the federal level to assert federal powers fully under s.91(2). Perhaps the federal government perceived that had it taken jurisdiction over financial institutions generally, including insurance companies, the provinces would challenge the legislation before the courts and thereby delay if not defeat the federal legislative program respecting financial institutions. Unfortunately, the federal government's seeming reluctance to boldly go where previous federal governments had not gone before may only serve to preserve and thus to strengthen the traditional jurisdictional view that gives a very limited ambit to federal powers under s.91(2), whether or not this view is sound as a matter of constitutional law.

VI CONCLUSION

Broadening the powers of federal financial institutions will not result in effective regulation of the financial system as a whole when provincial financial institutions remain beyond the same regulatory reach. What is required is comprehensive financial intermediation legislation that would address such traditional matters as solvency, corporate governance, disclosure, supervisory powers and ownership, as may be required to preserve and promote the viability of the financial institutions doing business as financial intermediaries, and, at the same time, apply the same regulations to all institutions doing business as a part of a national financial system.

While the legislation might include provisions appropriate to an insurance function or a banking function, it would be the function or the activity that is regulated. A provision would apply to an institution whenever it engaged in a function or activity to which the provision applied. There would be no need to limit the activities permitted to each category of institution.

When appearing before the House of Commons Committee on Banking and Finance (the Blenkarn Committee), with respect to Bills C-42 and C-56, the responsible minister, the Minister of State for Finance, Thomas Hockin, explained, with respect to federal institutions entering the securities business, that the federal authorities must have

> supervision of in-house activities of federally regulated financial institutions when they are in the securities business.

The minister went on to explain:

> We are regulating by institution, rather than by function.... [T]hings that are going to happen in the federal institution are regulated by the federal supervisor.... Where [the activity] is provided will determine who regulates it.... It is where it is provided, in the subsidiary or in-house, that will determine who regulates it.[159]

The federal reforms are applied to federal institutions as if the federal jurisdiction depended on the level at which an institution is incorporated. While it is clear that Parliament's power of incorporation includes jurisdiction over the companies it incorporates, such jurisdiction is for corporate purposes only.[160]

Parliament may also have jurisdiction over the activities in which a financial institution engages, whether the institution is incorporated at the federal level or the provincial level. Many of the enumerations of the 1867 Act, including s.91(2), identify an activity as the "class of subject matter" that is assigned to Parliament. For this reason, with respect to a financial institution, the activities of the institution can provide a basis for a federal regulatory jurisdiction that is separate and distinct from a jurisdiction based on the level at which the institution is incorporated.

The raison d'être for the legislative regulation of financial institutions is the preservation of public confidence in the reliability of these institutions as the holders of other people's money. The function or activity that these institutions carry on and which depends on public confidence is financial intermediation. Financial intermediation is a general trade activity, comparable to competition, on which the financial system depends. The financial system as a whole must be regulated, therefore, through regulation of the institutions that do business as financial intermediaries.

The emphasis given in the insurance cases to s.92(13) and, to a lesser extent, to s.92(16) may be understandable in the interest of provincial autonomy. Provincial autonomy on local matters is a basic feature of a federal constitutional system. At the same time, however, provincial autonomy, must be balanced against federal interests.

In the end, the Court must find the appropriate balance. As Justice Dickson said in C.N. Transportation (1983):

> Every general enactment will necessarily have some local impact, and if it is true that an overly literal conception of "general interest" will enganger the very idea of the local, there are equal dangers in swinging the telescope the other way around. The forest is no less a forest for being made up of individual trees.[161]

Justice Dickson offered three criteria for the application of s.91(2) on behalf of federal competition legislation:

(a) the presence of a national regulatory scheme, the oversight of a regulatory agency and a concern with trade in general rather than with an aspect of a particular business;[162]

(b) that the provinces jointly or severally would be constitutionally incapable of passing such an enactment; and

(c) that failure to include one or more provinces or localities would jeopardize successful operation in other parts of the country.[163]

The list of criteria is not meant to be exhaustive and no single criterion is to be decisive. The proper approach, according to Justice Dickson, and taken from Parsons, was a case by case assessment:

> Nevertheless, the presence of such factors does at least make it far more probable that what is being addressed in a federal enactment is genuinely a national economic concern and not just a collection of local ones.[164]

Additional criteria for upholding federal legislation under s.91(2) might include the following:

(a) the federal legislation does not unnecessarily deprive the provinces of their powers over matters of a local or private nature, such as individual trades carried on in a province;

(b) economic equity between and among the provinces is enhanced by the federal legislation where it otherwise would not be;

(c) the aspects of financial intermediation treated by the federal legislation are of manifest or demonstrable national importance to Canada as an international trading partner or member of the international community of nations; and finally,

(d) there is a rational basis for Parliament enacting the legislation in order to preserve public confidence in the regulatory control of financial intermediaries and, more broadly, to protect the public economic interest generally.

The thread that ties these criteria together is economic management. As Justice MacGuigan said in Québec Ready Mix, Parliament must be free "to adopt and even to experiment with various approaches to the regulation of the economy."

After an earlier laissez-faire era, economic management by government has become a permanent feature of present-day public economic life. Economic management by government means legislation on economic matters. In a constitutional system of divided powers where governments at each level are vigilant in the regulation of economic matters that affect their electors, what should the Court do where federal economic legislation encroaches on provincial economic powers?

First, the Court must be vigilant to see that it is national economic matters, and not local or regional matters, that are the subject-matter of federal legislative action under s.92(1). Second, legislative powers must not be denied to Parliament so that the national economy, or a part of it, is left without effective regulation.

The constitutional "threat" posed by s.91(2) in support of federal regulation of financial institutions may be that the autonomy of the provinces is diminished or compromised to an unacceptable degree. This is not so, however. Comprehensive financial intermediation legislation would leave the autonomy of the provinces with respect to the regulation of financial institutions, if not virgo intacta, nonetheless sufficiently intact to enable provincial regulation of provincial financial institutions that restrict their activities to their "home" province, as "Matters of a merely local or private Nature in the Province" under s.92(16). Any loss or reduction of provincial autonomy through federal regulation of financial intermediation generally would, one hopes, be off-set by the collective, national benefits gained through improved economic management of the national economic system.

One has only to remember that financial institutions deal in capital that is the accumulation of the personal savings of their customers. These institutions do business in capital markets wherever the best return can be obtained. There are no interprovincial barriers, regulatory or otherwise, to the movement of capital. There are few, if any, barriers to the movement of capital into or out of Canada. By virtuer of the free market financial system that prevails in Canada, in most western economies and in the international economy generally, capital moves, whether between federated provinces or states or between sovereign states, as if in a single market within a single sovereign state.

Some might argue that there is no sovereign authority today, whether national or international in nature, that effectively regulates the movement of capital.[165] The fact remains, however, that comprehensive regulation of financial institutions by the central suthority of each sovereign state would enable the movement of capital and the activities of financial institutions as the major players in the capital markets to be more effectively regulated in the collective interest of the state.

Even where a state is a federated state, like Canada, that otherwise enjoys a division of legislative powers between the central legislative authority and the constituent provinces or states, the fluid and highly mobile nature of capital and the complex and competitive nature of the business of financial institutions as financial intermediaries require that all capital and all financial institutions be subject to the same rules and the same regulator. In this fashion, savers from any or all of the constituent provinces or territories can take comfort from the fact that the institution that receives their savings is governed by the same rules and is supervised by the same regulator as other financial institutions (other than purely provincial institutions, perhaps).

Savers throughout Canada ought to be able to look to one regulating authority to protect their common interest in the security of their personal savings when placed in the hands of financial institutions doing business throughout Canada (and elsewhere) as financial intermediaries. Each province of Canada ought to be able to, and therefore all provinces must, look to the central government to protect their collective interest in the continued viability of the financial system in Canada, a system which the provinces themselves are unable to protect by their own regulation.

FOOTNOTES

FOOTNOTES

1. It is life insurance companies, and not general insurance companies, that act as financial intermediaries. As such, these companies are financial institutions and constitute one of the four "pillars" of the Canadian financial system. Life insurance companies play a financial intermediation role inasmuch as life insurance policies often include a savings component. Secondly, life insurance companies deal in annuities which are a form of personal savings plan. For this reason, a reference in the text to insurance companies generally is intended as a reference to life insurance companies.

2. There is a distinction to be drawn between financial intermediaries and market intermediaries. Banks, insurance companies and trust companies, amongst others, are financial intermediaries. Investment dealers, on the other hand, are market intermediaries.

   A market intermediary acts as an intermediary between the party that is seeking funds (equity) and the public (market) where the funds are to be found and is more an agent of the party seeking the funds. A financial intermediary, on the other hand, acts on its own behalf in its role as an intermediary between a saver and a borrower and does not act as a mere agent on behalf of the saver or the borrower.

   The distinction is illustrated when put in terms of the essential transaction involved. A financial intermediary facilitates a purely financial transaction between a saver and a borrower by acting as a contracting party at both ends of the transaction, that is, with both the borrower and the saver. A market intermediary facilitates a purchase and sale transaction and does not act as a contracting party at either end of the transaction, that is, with either the corporation issuing the shares or the purchaser buying the shares.

Typically, an investment dealer, acting as a market intermediary for a corporation, undertakes to sell to the public, on a commission basis, the shares of the corporation for the purpose of raising equity funding for the corporation. Investment dealers are sometimes said to act as financial intermediaries, however, where they purchase the corporate shares directly with a view to a later public sale at a profit.

For our purposes in this paper, financial institutions, including investment dealers, are considered in their role as financial intermediaries and not as market intermediaries.

3. The recent entry of chartered banks into the securities industry, traditionally a field of provincial jurisdiction, as market intermediaries and not financial intermediaries, has given rise to jurisdictional conflict between the federal government and the governments of Québec and Ontario.

On April 28, 1987, the Hon. Thomas Hockin, Minister of State (Finance), on behalf of the federal Government, and Ontario's Minister of Financial Institutions, the Hon. Monte Kwinter, announced that an agreement had been reached with respect to the regulation of the securities activities of chartered banks, federally incorporated trust and loan companies and insurance companies and their subsidiaries or affiliates: see Ontario Securities Commission Bulletin, May 1, 1987, p.2553.

The joint press release announcing the agreement referred to the agreement of the two ministers as an "understanding with respect to the implementation of their respective regimes for the regulation of securities-related activities of federal financial institutions". The first recited "understanding" of the agreement is as follows:

> There is a clear interest across Canada in the efficient functioning of the Canadian capital markets. It is essential that comparable activities be regulated in comparable manner. The Office of the Superintendent of Financial Institutions

> ("OSFI") will regulate federal financial institutions. The Ontario Securities Commission ("OSC") will regulate in Ontario the subsidiaries or affiliates of federal financial institutions which are engaged in securities-related activities....

Clauses 3 and 4 of the "understanding" assign to the two legislative levels the various securities-related activities in which an institution might engage.

By clause 3, Ottawa shall regulate federal financial institutions that engage in, inter alia, money market activities, debt securities of the institutions, secondary market trades in corporate debt securities, unsolicited participation in secondary trading of equity securities, portfolio management and investment counselling and trades for fully managed accounts.

By clause 4, the province of Ontario shall regulate primary distribution of equity securities, primary distribution of corporate debt securities, secondary market trading in equity securities, portfolio management and investment counselling (except where such activities are covered by clause 3) and these activities "shall be carried on in a subsidiary or an affiliate". Should a federal financial institution choose to carry on any other securities-related activities through a subsidiary or affiliate, these activities are to be regulated by the province.

The Ottawa-Ontario agreement would appear to be a pragmatic division of regulatory authority in the securities field using the sale of securities to the public at large in the province as the jurisdictional dividing line. Ottawa seems to have retained regulatory control of federal financial institutions that engage in securities-related activities, provided these institutions do not engage in the core function, as it were, of selling securities to the public at large.

It would appear that, for the most part, federal financial institutions are under provincial regulation when they engage in securities-related activities that are oriented to the public market and are under federal jurisdiction with respect to securities-related activities that are more oriented to the role of financial intermediary in the securities field, as if to reflect a concern on the part of the province that it preserve its regulatory control of the securities market even where this means surrendering some control over institutions acting as financial intermediaries in the securities field.

4. R. v. Hoffman-LaRoche Ltd. (Nos. 1 & 2), (1981) 125 D.L.R. (3d) 607 (Ont.C.A.); Attorney-General for Canada v. C.N. Transportation, [1983] 2 S.C.R. 206, (1983) 3 D.L.R. (4th) 16 (S.C.C.); Attorney-General for Canada v. Québec Ready Mix Inc. et al, (1985) 25 D.L.R. (4th) 373 (Fed.C.A.), on appeal to the Supreme Court of Canada (judgment not yet rendered); City National Leasing Ltd. v. General Motors of Canada Ltd., (1986) 28 D.L.R. (4th) 158 (Ont. C.A.), on appeal to the Supreme Court of Canada (judgment not yet rendered); Westfair Foods Ltd. v. Lippens Inc. et al, [1987] 6 W.W.R. 629 (Man.Q.B.).

5. "The Financial Institutions and Markets: A General View," Report of the Royal Commission on Banking and Finance, February 5, 1964, D.H. Porter, Chairman (Ottawa: Government of Canada, 1964), chapter 6, p.89 at p.90. Financial institutions and capital markets, said the Porter Royal Commission,

> play a vital role in the economic process; a sizeable share of the nation's lending and borrowing goes through their hands and they thus have a significant influence over the allocation of resources and the efficiency with which they are used. (p.89)

6. Porter Royal Commission, fn.5, p.89 et seq.; see also A.N. McLeod, "The Mysteries of Credit Creation," (1959) 66 (No.3) Canadian Banker 20.

7. Porter Royal Commission, fn.5, pp.89-90.

8. Ibid., p.91.

9. Ibid., p.92.

10. Ibid., p.105.

11. Report of the Study Committee on Financial Institutions, ("Parizeau Report"), 1969, Government of Québec, p.206. The Parizeau Report argued, on behalf of the financial system in Québec, that the province has jurisdiction to regulate the activities of companies, wherever incorporated, where the activities are not reserved by the Constitution to the federal level, such as with insurance or trust company activities. The doubtful premise here, from our point of view, is the notion that a province has its own financial system.

12. "[Financial institutions] can move money around with the stroke of a pen so one province alone doesn't have a hope of monitoring what's going on:" B.C. Finance and Corporate Relations Minister, the Hon. Mel Couvelier, commenting in the wake of disclosures about inter-corporate transfers of funds by Principal Group Ltd. companies (see fn.157).

The B.C. finance minister agreed that the four western provinces needed more uniform regulation of the provinces' investment industry. Mr. Couvelier cited the Principal Group Ltd. case as a prime example of the problems that arise for a province with respect to financial institutions that operate in more than one province. When B.C. regulators began having concerns several years earlier about the liquidity of two investment contract subsidiaries in the Principal Group, they were stymied by the fact that the parent company was regulated in Edmonton, Alberta: The Financial Post, February 1, 1988, p.6.

13. An illustration of such shopping around was provided recently by the president of Principal Group Ltd. ("PG"), the Alberta-based financial services conglomerate that collapsed in the summer of 1987 (see fn.157).

A $23 million mortgage transaction between two PG subsidiaries was consummated in 1984 to avoid stringent federal regulations. A federally regulated PG subsidiary, Principal Savings and Trust Co., transferred its share in 19 mortgages and four properties to the provincially regulated PG subsidiaries, First Investors Corp. Ltd. and Associated Investors of Canada Ltd., in return for cash, to gain the benefit of weaker Alberta regulatory standards. The latter companies became insolvent on June 30, 1987 causing 67,000 mostly elderly investors to lose about $150 million. Mr. Cormie explained that the Canadian Deposit Insurance Corporation had been pressing Principal Savings (a federal company) to either write down or dispose of the mortgages or have its borrowing base reduced. See "Deal Aimed to Dodge Ottawa: Cormie", by Matthew Fisher, The Globe & Mail, National Edition, April 15, 1988, pp.B1-B2.

14. In a case comment published in 1959, Professor Bora Laskin, as he then was, commented that

> the story of the trade and commerce power ... is in my view the saddest legacy of Privy Council adjudication:

(1959) 37 Canadian Bar Review 630 at 631. Laskin attributed the Privy Council's treatment of s.91(2) to its

> consistent refusal to look at an economic or social problem as a whole, and its correlative *a priori* assumption that every problem of trade regulation necessarily had its national and its local aspects which constitutionally had to be separated regardless of resulting violence to a legislative scheme. (p.632)

In Australia, "trade and commerce" is assigned to the Commonwealth with regard to interstate and foreign trade. Although the federal power may be restricted to interstate trade, the Australian courts have given the power a wide interpretation by characterizing laws as properly incidental to the power even if not directly within it: Howard, C., Australian Federal Constitutional Law (Sydney: The Law Book Company Limited, 1968), at p. 203 *et seq*.

In the United States, Congress is given the power to regulate commerce under Article 1, section 8, clause 3 of the Constitution (the "commerce clause") which provides that Congress shall have the power

> To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

When a state regulation conflicts with federal legislation enacted under the commerce clause, the federal legislation prevails. According to a leading text on American constitutional law,

> the rationale of the commerce clause was to create and foster the development of a common market among the states, eradicating internal trade barriers, and prohibiting the economic Balkanization of the Union.... Recognition of the predominant goal of establishing a unified, national economy has permeated judicial interpretations of state power to regulate commerce. When local legislation thwarts the operation of the common market entity, it has then exceeded the permissible limits within the federal structure:

Nowak, J.E., Rotunda, R.D., Young, J.N., eds., Constitutional Law, 2nd. ed., (St. Paul, Minn.: West Publishing Co., 1983), chap. 9, pp.267-268.

The American commerce clause restricts state powers even where Congress has not legislated on a matter. The so-called "dormant state" of the commerce clause requires the court to balance the national interest in the free flow of trade and the state interest to protect the health and welfare of its citizens: see Nowak et al, supra, p.274, and William C. Nugent, case comment in (1986) 17 Rutgers Law Journal 363 at 367-368. Nowak et al, supra, pp.288-289, summarize the American division of powers over commerce as follows:

> Where the state regulates even-handedly to effectuate a legitimate local public

> interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putàtive local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact with interstate activities.

15. In this paper, "the Court" refers to the Supreme Court of Canada as the final arbiter of constitutional questions in Canada.

16. Citizens Insurance Company of Canada v. Parsons (1881) 7 A.C. 96 (P.C.) affirming (1880) 4 S.C.R. 215 (S.C.C.).

17. Ibid., A.C. 108-109.

18. Ibid., p. 110.

19. Ibid., p. 109.

20. Ibid., p. 112.

21. Ibid., p. 113.

22. The noun "trade" is not being used here, nor was it used in Parsons, to mean specific economic transactions wherein goods are traded, as in a "trade" of a specific product for another product or of specific goods for money (price).

23. The latin word "civis", from which "civil" is derived, relates to the person. The latin word means citizen and in the jurisprudential context refers to the law of private rights.

24. Professor Lederman has described Parsons as a compromise between the overlapping but distinct meanings of s.91(2) and s.92(13), the problem being in such cases to decide where the line is drawn between the two "exclusive" powers. In Parsons,

> the general line of distinction between section 91(2) and section 92(13) was drawn as follows: given that the challenged law is both property or contract law and trading or commercial law, if the trade or commerce is internal to a single province, then the property and civil rights aspect is the more important and provincial power is exclusive. But, if the challenged law is property or contract law about interprovincial or international trade or commerce, then its trading or commercial aspect is the more important and the federal power is exclusive:

Lederman, W.R., "The Concurrent Operation of Federal and Provincial Laws in Canada," (1963) 9 McGill Law Journal 185 at 187-188.

25. A.G.B.C. v. A.G. Canada (Natural Products Marketing), [1936] S.C.R. 398 (S.C.C.).

26. Ibid., p.412.

27. Idem.

28. Justice Duff's views on s.91(2) were upheld on appeal to the Privy Council: [1937] A.C. 377 (P.C.). Lord Atkin said the federal legislation covered transactions which were completed within the province and had no connection with interprovincial or export trade and that the regulation of trade and commerce did not permit the regulation of individual forms of trade and commerce confined to the Province: A.C. 387.

29. Reference re Ontario Farm Products Marketing Act, [1957] S.C.R. 198 at 204 (S.C.C.).

30. Ibid., per Rand, J., pp.209-210.

31. Murphy v. C.P.R. [1958] S.C.R. 626 (S.C.C.).

32. R. v. Klassen (1959) 29 W.W.R. (N.S.) 369 (Man. C.A.), per Tritschler, J.A., at p. 377.

33. Carnation Company Ltd. v. Québec Agricultural Marketing Board, [1968] S.C.R. 252 (S.C.C.).

34. A.G. Manitoba v. Manitoba Egg & Poultry Association, [1971] S.C.R. 689 (S.C.C.).

35. Ibid., at p. 703.

36. Caloil Inc. v. A.G. for Canada, [1971] S.C.R. 543 (S.C.C.).

37. Ibid., at p. 550.

38. Idem.

39. Burns Foods Ltd. v. A.G. Manitoba, [1974] 40 D.L.R. (3d) 731 (S.C.C.).

40. Ibid., at p. 737.

41. Macdonald et al. v. Vapor Canada Ltd., [1977] 2 S.C.R. 134.

42. Chief Justice Laskin, on behalf of the majority, said, at S.C.R. 157, that the relevant questions were,

> whether the liability [under s.7(e)] is imposed in connection with an enterprise or an activity, for example, banking or bills of exchange, that is itself expressly within federal legislative power, or, if not, whether the liability is dealt with in such a manner as to bring it within the scope of some other head of federal legislative power.

Parliament can enter provincial legislative waters provided it is for legislative purposes that otherwise fall within Parliament's legislative jurisdiction.

43. Said the Chief Justice, ibid., at p. 158:

> [The predatory practices prohibited by s.7 of the Trade Marks Act] are left to merely private enforcement as a private matter of business injury which may arise, as to all its elements including damage, in a small locality in a Province or within a province.

See also Hogg, P.W., comment on Vapor Canada, at (1976) 54 Canadian Bar Review 361 at 365-368.

44. Per the Chief Justice, ibid., at p. 165:

> The provision [7(e)] is not directed to trade but to the ethical conduct of persons engaged in trade or in business, and, in my view, such a detached provision cannot survive alone unconnected to a general regulatory scheme to govern trading relations going beyond merely local concern.... [I]t is as applicable in its terms [by virtue of private enforcement] to local or intraprovincial competitors as it is to competitors in interprovincial trade.

45. Dominion Stores Limited v. The Queen and the A.G. of Ontario, [1980] 1 S.C.R. 844 (S.C.C.); Labatt Breweries of Canada Ltd. v. A.G. Canada and A.G. of Quebec, [1980] 1 S.C.R. 914, 110 D.L.R. (3d) 594 (S.C.C.).

46. The appellant was acquitted in provincial court on the ground that the federal legislation was invalid. On appeal to the Ontario High Court, the legislation was held valid, the acquittal was set aside and a new trial ordered. On further appeal to the Ontario Court of Appeal, the federal legislation was again upheld.

47. Dominion Stores, fn.45, S.C.R. 854.

48. Ibid., p. 855. According to Justice Estey, at S.C.R. 859, Dominion Stores boiled down to the following:

> [T]he appellant here offered apples for sale pursuant to an admittedly valid provincial statute. The dealer did not select and adopt a grade name prescribed by a federal statute, but rather complied with applicable, valid provincial legislation. The precise issue facing the Court ... is whether or not, in these circumstances, a charge may be laid under the federal statute.... [T]he offence, if any, must, in my view, be against the provincial legislation and not the artificially extended federal statute.

The fate of the federal trade power in Dominion Stores is not surprising, perhaps, in view of the unfavourable light that Justice Estey cast on the federal legislation, characterizing it as "piggy-backing", "shadow" legislation.

The federal Act adopted provincial regulations that regulated the sale of apples in the province. There was, as a result, a duplication of regulation as between the two legislative levels. The federal legislation was voluntary while the provincial legislation was mandatory. Justice Estey said the "piggy-backing" of the federal legislation on the provincial legislation had the effect of making the "voluntary" federal provisions mandatory insofar as an offence under the mandatory provincial statute is indistinguishable from an offence under the federal statute.

Parliament, according to Justice Estey, can no more enact legislation that is voluntary than it can do so where the legislation is mandatory. Parliament cannot incorporate provincial legislative provisions into its interprovincial trade legislation and then seek to enforce the provisions with respect to local trade. If Parliament is to be allowed to enforce such "shadow legislation", provincial power to regulate local trade, separate from federal legislation and autonomously, could be permanently frustrated: S.C.R. 863.

49. Labatt Breweries, fn.45, S.C.R. 939.

50. His Lordship went on to say of the federal regulations:

> The impugned regulations... are not concerned with the control and guidance of the flow of articles of commerce through distribution channels, but rather with the production and local sale of the specified products of the brewing industry....

With respect, the federal trade and commerce power, even under the stream of commerce doctrine, is not limited, as Justice Estey's remarks seem to suggest, to control of the "flow of articles of commerce through distribution channels".

The Court's preoccupation with the stream ("the flow") seems evident in Justice Estey's comments on the "spectrum" of trade:

> [I]f contractual rights within the province are the subject of the proposed regulation, the province has the authority. On the other hand, if the regulation of the flow in extra-provincial channels of trade is the object, then the federal statute will be valid. Between these spectrum ends, the shadings cannot be foretold in anything approaching a constitutional formula:

ibid., S.C.R. 942-943; see also discussion re production versus marketing in Ontario Farm Products, supra, fn. 29.

The stream metaphor in Ontario Farm Products refers to the movement of trade and in particular to the inter-provincial and international movement of trade. Once an item of trade entered the inter-provincial or international level of trade movement --"the stream"-- the item of trade "and all its attendant circumstances" are no longer matters of local concern.

The so-called stream metaphor means to indicate that federal jurisdiction arises by reason of the inter-provincial and international movement of the trade but is not limited to regulation of the movement itself, as Justice Estey in Labatt Breweries seems to suggest ("control and guidance of the flow").

In Labatt Breweries the Court said there was no demonstration of any "interprovincial aspect" of the beer industry. This would appear to be a conclusion of fact presumably based on material placed in evidence before the Court (or a lack thereof). Indeed, it is common knowledge that in virtually all the provinces, domestic beer is required, under provincial powers over liquor sales, to be produced in the province before the brewer can sell beer in the province. According to the Brewers' Association of Canada:

> Canadian breweries must operate in a province in order for that brewers' beer to

> be sold, or be sold competitively. This being so, the number of plants operating in Canada and their size has been largely determined by provincial authority....
>
> Plant size is, of course, a function of market boundaries. Because interprovincial trade barriers exist in Canada and not in the United States, the Canadian industry does not have the brewery giants that are found there....
>
> The number of breweries operating in Canada is also a function of enforced market boundaries.
>
> Brewing companies are not restricted to selling within state borders in the United States with the result that brewing locations appear to be a function of proximity to population centres, distribution economies and raw materials. Unlike the situation in Canada where all but one province has at least two brewing facilities, there are breweries in only 26 of the 49 mainland states:

"Perspectives on Canada-United States Free Trade," a submission by the Brewers Association of Canada to the Hon. James Kelleher, Minister for International Trade, May 1985, pp.1-3.

With brewers unable to do their business in several provinces while located in only one province and hence the lack of an interprovincial beer trade, it may not be surprising that federal legislation regulating the label designation for light beer is considered regulation of a local trade.

51. Ibid., S.C.R. 943-944.

52. Idem. Insofar as the Court in Labatt Breweries upheld the rule against federal jurisdiction based on uniformity, the Court's decision would appear consistent with authority and not unreasonable in the circumstances. On the other hand, it is important to remember that the interprovincial dimension gives rise to federal jurisdiction and does not restrict federal jurisdiction to regulation of the interprovincial movement alone.

53. Ibid., S.C.R. 940-941.

54. See text, infra, p.23-24.

55. C.N. Transportation, fn.4. The issue in C.N. Transportation was whether the federal attorney-general had constitutional authority to undertake prosecutions under the federal Combines Investigation Act. The Court was unanimous in saying the federal A.G. could prosecute, but the justices disagreed in their reasons and in whether the federal A.G. had exclusive authority. In the latter respect, a majority of four justices said that insofar as the statute rested on the federal criminal law power, the federal A.G. could prosecute and this prerogative was exclusive once the federal authority entered the field. Until and unless the federal A.G. does so, the provincial attorney-general could prosecute by virtue of s.92(14).

Justice Dickson held that validity of the federal statute rested on both the federal criminal law power and the federal trade and commerce power and that the two attorneys-general had concurrect jurisdiction to prosecute under the statute. The two remaining justices agreed with Justice Dickson with respect to application of the criminal law power but did not express an opinion with respect to application of the trade and commerce power.

56. Ibid., S.C.R. 260.

57. Idem.

58. Ibid., S.C.R. 266-267.

59. Ibid., S.C.R. 267.

60. Ibid., S.C.R. 267-268.

61. Hoffman-LaRoche, fn.4, p. 649, per Martin, J.A.

62. Québec Ready Mix, fn.4, per Justice MacGuigan, who had the concurrence of the other two justices sitting on the appeal.

63. Québec Ready Mix, fn.4, pp.389-390.

64. Ibid., p.390, quoting Laskin, C.J.C., in Vapor Canada, fn.41, D.L.R. 24, SCR 164. Québec Ready Mix was followed in City National Leasing, fn.4, and in Westfair Foods, fn.4.

65. In Vapor Canada, fn.41, per Laskin, C.J., at S.C.R. 165, speaking for the Court:

> One looks in vain for any regulatory scheme in s.7, let alone in s.7(e). Its enforcement is left to the chance of private redress without public monitoring by the continuing oversight of a regulatory agency which would at least lend some colour to the alleged national or Canada-wide sweep of s.7(e). The provision is not directed to trade but to the ethical conduct of persons engaged in trade or in business, and, in my view, such a detached provision cannot survive alone unconnected to a general regulatory scheme to govern trading relations going beyond merely local concern.

Although the Court in Vapor Canada did not explain its insistence on the presence of a national regulatory regime, one might surmise that the Court felt such a regime, if established, would confirm that the trade regulations were directed to a general trade matter affecting Canada as a whole.

66. Scott, F.R., "The Special Nature of Canadian Federalism," (1947) 13 Canadian Journal of Economics and Political Science 13 at 15. For Scott, the word "federal" had a meaning in political theory which it did not have in Canadian constitutional law:

> The technical meaning never hampered the framers of Canada's federal system in their purpose of creating a strong national government free from the doctrine of "states' rights" which had so largely contributed to the American Civil War: p.25.

After an examination of the 1867 Act, Scott felt that

> Canadian federalism was to be of a very special type, fitting no theoretical definition and leaning heavily in clear intent and purpose toward a strong, national government: p.19.

Moreover, wrote Scott, whenever the 1867 Act departed from the accepted federal idea, it leaned toward national unity and not toward provincial autonomy: p.22.

Classically defined, a <u>federal</u> state is one in which each citizen is subject to a dual jurisdiction, that of the centre and of the province. A <u>confederal</u> state is one in which the central authority has no direct jurisdiction over the citizens of the constituent states: Vernon, R., op. cit., fn.68, at p. xxiii citing Wheare, K.C., <u>Federal Government</u> (London, 1946). In these terms, Canada is a federal, not a confederal, state: see Kennedy, W.P.M., <u>The Constitution of Canada, 1534-1937</u>, 2nd ed., 1938, at p. 403 et seq. with respect to the confusion of terminology evident in the confederation documents, as between "federal principle", "federal union" and "confederation".

67. Quotation marks are necessary as the competing claims of the two residuary clauses causes the distribution of powers to be of doubtful exclusivity.

68. <u>The Principle of Federation by P.-J. Proudhon</u>, translated and introduced by Richard Vernon, (Toronto: University of Toronto Press, 1979), at pp.295-296.

69. O'Connor Report to the Senate of Canada, 1939, Annex II, p.129.

70. Ibid., Annex IV, pp.76-77; and see F.R. Scott, "Political Nationalism and Confederation," (1942) 8 <u>Canadian Journal of Economics and Political Science</u> 386 at 405.

71. Idem.

72. Idem.

73. Scott, F.R., op. cit., fn. 70, pp.399-407. The 1867 Act's centralist departures from a conventional federalism with strong, autonomous constituent member states, include a central veto over provincial laws (s.56 & s.90), central

control over provincial executives (s.58), central government nomination of provincial superior court justices (s.96), central authority power to commandeer provincial works (s.92(10)(c)), central legislative power on all matters covered by an Empire treaty (s.132) and a general residuary power in the central authority (POGG).

74. Freeman, E.A., The History of Federal Government, (London, 1863), p. 3, quoted by M.J.C. Vile, op. cit., fn.81, Appendix A, p.34.

75. The Principle of Federation by P.-J. Proudhon, supra, fn.68.

76. The Principle of Federation by P.-J. Proudhon, fn.68, pp.6-7: The "regime of authority" produces either monarchy/patriarchy or panarchy/communism, the essential feature of which is the non-division of power. The "regime of liberty", on the other hand, produces either democracy or anarchy/self-government, the essential feature of which is the division of power: ibid., pp.8-9.

To Proudhon history showed that authority "gives way" gradually to the "juridical, rationalist and liberal principle", that authority "becomes progressively the instrument of liberty": ibid., at p. 36. The liberal system was contractual in nature and so it is that we must take the idea of contract as the "principal idea in politics": idem. Contracts were domestic, civil, commercial or political. The political contract is what Proudhon called a federation: ibid., p.38.

77. Ibid., p.45.

78. Riker, Federalism, Origins, Operation, Significance, (Boston, 1964), pp.139-145, as quoted by Vernon, R., op. cit., fn.68, p.xxvi. W.J. Wagner, in The Federal States and their Judiciary, ('s-Gravenhage: Mouton & Co., 1959), pp.21-40, offers eight basic characteristics of a federal state:

(1) the lack of sovereignty of the members of the federal state;

(2) the limitation of central powers is strictly connected with the concept of self-determination;

(3) the division of powers cannot be determined by the central government by itself, without the consent of at least a majority of the member states;

(4) each member state is bound by the decision of the majority of them and a dissentient member state has no right to secede from the union because of any such disagreement;

(5) the member states possess their own sphere of action which includes matters of a certain degree of importance, that are not trivial on the whole;

(6) all member states are equal;

(7) the member states are able to participate in the administration of the affairs of the federal state; and

(8) the constitution is supreme.

For a Québec discussion of the historical origins and theoretical underpinnings of federalism, see Gilles Lalande, <u>In Defence of Federalism: The View from Quebec</u>, (Toronto: McLelland & Stewart, 1978), originally published in french in 1972.

79. Vernon, R., op. cit., fn.68, p.xxvi; see also McWhinney, E., "Constitutional Particularism and the New, Pluralistic Federalism," in <u>Canada Challenged: The Validity of Confederation</u>, R.B. Byers and R.W. Reford, eds., (Toronto: Canadian Institute of International Affairs, 1979), 38 at 44, where the author speaks of "fundamental political compromises" between the French and the English in the 100 years following the Conquest of 1759, which compromises, according to McWhinney, represented the "Grundnorm" or basic premise of the 1867 constitutional system.

By 1969 Riker had come to the conclusion that federalism was a myth and that apart from its historical significance, it had no practical significance for the way government is carried on in those countries which claim to be federal: "Six books in search of a subject, or does federalism exist and does it matter?", (October, 1969) 2 (No. 1) Comparative Politics 135-146, referred to in Vile, op. cit., fn.81, p.35.

In 1984 the Canadian legal scholar, Patrick Monahan, concluded that the "theoretical underpinnings" of federal government are so vague and abstract as to be virtually meaningless when one is attempting to solve concrete social and political problems: "At Doctrine's Twilight: The Structure of Canadian Federalism," (1984) 34 University of Toronto Law Journal 47 at 82.

80. C.F. Strong, Modern Political Constitutions, 8th revised edition, (London: Sidgwick & Jackson, 1972), p.88.

81. Vile argues that historically federalism represents an attempt to cope, in complex situations, with the 19th. century values of representation, democracy and national feeling,

> but when the 20th. century adds to that list of values another --social justice-- the problems of federal systems become complex indeed....

In the 19th. and early 20th. centuries, says Vile, the "device of federalism" was adopted as a compromise between an "all-embracing democratic majority-rule over all matters" and a "Balkan system of petty statedoms":

> [T]he problem was to ascertain those matters over which the nation as a whole contained the relevant "majority" and those over which the state or province contained the relevant 'majority'. Thus federalism is both an assertion of, and a limitation upon, majority rule:

M.J.C. Vile, Federalism in the United States, Canada and Australia, Commission on the

Constitution, Research Paper #2, (London: H.M. Stationery Office, 1973), pp.2-4.

For Vile, the "working constitution" of a federal system must meet three major conditions. First, it must provide for a division of the powers of government. Second, there must be a rigidity about the system, i.e., recognition of, and the institutionalization of, certain basic ground-rules of constitutional and political action which must be observed. Third, there must be a set of mechanisms for change of the rules concerning the division of powers.

82. Re Resolution to Amend the Constitution (Patriation Reference), (1982) 125 D.L.R. (3d) 1 at 45; [1981] 1 S.C.R. 753 (S.C.C.).

83. [1892] A.C. 437 at 441-442 (P.C.), quoted in Patriation Reference, supra, fn.82, S.C.R. 905-906.

84. Re Section 55, Supreme Court Act and Re Section 23, Manitoba Act, 1870 and Section 123, Constitution Act, 1867 (Manitoba Language Rights), [1985] 4 W.W.R. 385 at 409-411 (S.C.C.).

85. Sawer, Geoffrey, Modern Federalism, (London, C.A. Watts & Co. Ltd., 1969), pp.163-164.

86. Federal fidelity has its origins in Concordat (1957), a decision of the West German Federal Constitutional Court. A Land had legislated for non-denominational education for all schoolchildren in the Land. The Bund challenged this legislation on the basis that although education was a matter within Land jurisdiction, the legislation conflicted with the German-Vatican treaty or Concordat of 1933 guaranteeing separate education for all Catholic students in Germany. The constitutional court acknowledged the Lander power to legislate on education and adopted what in this country is known as the rule in Labour Conventions, [1937] A.C. 326 (P.C.), that is, that the fact that the Bund may be bound by international treaty to implement its provisions does not enable the Bund to take on powers that belong to the Lander: McWhinney, fn.87.

The legislative problem, of course, that flows from the decision in Concordat, similar to the one caused by Labour Conventions in Canada, namely, federal legislative implementation of treaty provisions relating to matters within a constituent state's powers, was not lost on the West German court. In recognition of, and as a response to, this constitutional problem, the court articulated the principle of "Bundestreue", which translates as federal comity or federal fidelity.

87. See McWhinney, Edward, Constitutionalism in Germany and the Federal Constitutional Court, (A.W. Sythoff-Leyden, 1962), at p. 46 et seq.; also (1961) 75 Harvard Law Review 5; see also McWhinney, E., Comparative Federalism: States' Rights and National Power, 2nd ed., (Toronto: University of Toronto Press, 1965), chap. 7, "Federalism and the Principle of Federal Comity," at p. 78 et seq.; and case comment in (1957) 35 Canadian Bar Review 842.

In Referenda on Atomic Weapons (1958), the West German constitutional court upheld an affirmative duty on the Lander to co-operate in their dealings with the federal level: McWhinney, op. cit. (1962), supra, pp.52-53 and p.70; see also Sawer, op. cit., fn.85, p.164. The doctrine of federal fidelity was subsequently reinforced in Fernseh (Television): February 28, 1961, 12 B Verf GE (1961) (Second Senate), as cited by McWhinney, op. cit. (1962), supra, p.60.

In Fernseh, the Bund had legislated for a federal monopoly in the regulation of the distribution of a second television channel in West Germany. The Lander challenged the legislation on the basis that such matters fell within recognized Lander competence over cultural matters. The court held in favour of the Lander but went on to comment on the principle of Bundestreue or federal comity and the obligations of inter-governmental moderation on the part of the Bund in its dealings with the Lander:

> [T]he obligation of inter-governmental moderation in a federal society is a

> reciprocal one, involving both the Bund and the Lander. For the federal principle ... not only involves rights but also obligations inter se.... The Bund could not, in a question of constitutional law in which all the Lander were interested and participated, proceed on a divida et impera basis....

McWhinney, op. cit. (1962), supra, p.64.

88. Sawer, op. cit., fn.85, p. 180. See also McWhinney, op. cit.(1962), fn.87, p.52-53, p.60, p.64 and p.70; see also Sawer, op. cit., fn.85, p.164.

89. In 1912, the Privy Council said the 1867 Act had distributed all the necessary legislative powers between the two legislative levels: A.G. Ontario v. A.G. Canada, [1912] A.C. 571 at 581. If this is so, it must be that, with respect to those matters on which the provinces are unable to legislate effectively, Parliament has the requisite power to enact, and the provinces have a corresponding duty to respect and allow, federal legislation on matters, as Lord Watson said in Liquidators of the Maritime Bank of Canada (1892), fn.83, "in which [the provinces] had a common interest."

90. The relevant passage is at SCR 266-267:

> Every general enactment will necessarily have some local impact, and if it is true that an overly literal conception of 'general interest' will endanger the very idea of the local, there are equal dangers in swinging the telescope the other way around. The forest is no less a forest for being made up of individual trees....
>
> * * *
>
> The reason why the regulation of a single trade or business in the province cannot be a question of general interest throughout the Dominion, is that it lies at the very heart of the local autonomy envisaged in the Constitution Act, 1867. That a federal enactment purports to carry out such regulation in the same way in all the

provinces or in association with other regulatory codes dealing with other trades or businesses does not change the fact that what is being created is an exact overlap and hence a nullification of a jurisdiction conceded to the provinces by the Constitution. A different situation obtains, however, when what is at issue is general legislation aimed at the economy as a single integrated national unit rather than as a collection of separate local enterprises. Such legislation is qualitatively different from anything that could practically or constitutionally be enacted by the individual provinces either separately or in combination. The focus of such legislation is on the general, though its results will obviously be manifested in particular local effects any one of which may touch upon 'Property and Civil Rights in the Province'. Nevertheless, in pith and substance such legislation will be addressed to questions of general interest throughout the Dominion. The line of demarcation is clear between measures validly directed at a general regulation of the national economy and those merely aimed at centralized control over a large number of local economic entities.

91. Section 121 of the 1867 Act provides as follows:

> All Articles of the Growth, Produce, or Manufacture of any one of the Provinces shall, from and after the Union, be admitted free into each of the other Provinces.

Section 95 of the 1867 Act provides as follows:

> In each Province the Legislature may make laws in relation to Agriculture in the Province, and to Immigration into the Province; and it is hereby declared that the Parliament of Canada may from Time to Time make Laws in relation to Agriculture in all or any of the Provinces, and to Immigration into all or any of the Provinces; and any Law of the Legislature of a Province

> relative to Agriculture or to Immigration shall have effect in and for the Province as long and as far only as it is not repugnant to any Act of the Parliament of Canada.

92. In "The Constitutional Basis of the Canadian Economic System," [1981] Cambridge Lectures 376 at 381, Raynold Langlois lists the economic powers given to Parliament: public debt and property [s.91(1)(a)], trade and commerce [s.91(2)], customs and excise [s.122], collection of moneys by all modes or systems of taxation [s.91(3)], borrowing of money on public credit [s.91(4)], currency [s.91(14)], banking, the incorporation of banks and the issue of paper money [s.91(15)], savings banks [s.91(16)], weights and measures [s.91(17)], bills of exchange and promissory notes [s.91(18)], interest [s.91(19)], legal tender [s.91(20)], bankruptcy and insolvency [s.91(21)], interprovincial and international transportation and communications [s.92(10)] and works declared for the general advantage of Canada [s.92(10)]. Agriculture is shared with the provinces, with federal paramountcy [s.95].

Langlois noted that the length of the list of federal economic powers obscured their salient features, namely, that apart from s.91(2), they are very specific in nature. When the provincial powers under s.92(13) and s.92(16) and the limitations placed on s.91(2) and POGG are taken into account, federal economic powers are, at best, fragmented, making it difficult for Canada, according to Langlois, to have a "truly coherent national economic policy": ibid., p.383.

Langlois argues that the federal economic powers, such as currency, banking, legal tender, customs and excise, are only suitable for national economic stabilization and that other economic objectives of government such as allocative efficiency and income distribution are, for the most part, not represented among the federal enumerated powers. Langlois suggests this might be explained by the *laissez faire* attitudes of government in matters of economic and social policy in the latter part of the 19th. century.

93. It is acknowledged that the factual account provided in this Part is far from conclusive or fully persuasive in its answers to the questions of fact posed. It is intended merely to illustrate the kind of material that could be included in a brief to the Court on the question of jurisdiction.

94. Parsons, fn.16; A.G. Canada v. A.G. Alberta (Insurance Reference), [1916] 1 A.C. 588, 10 W.W.R. 405, 26 D.L.R. 288 (P.C.), affirming (1913) 48 S.C.R. 260, 5 W.W.R. 488 (S.C.C.); A.G. Ontario v. Reciprocal Insurers, [1924] 2 W.W.R. 397, [1924] A.C. 328, [1924] 1 D.L.R. 789 (P.C.), varying 53 O.L.R. 195; Re Insurance Contracts, [1926] 2 D.L.R. 204, 58 O.L.R. 404 (O.S.C.); A.G. Quebec v. A.G. Canada; Re Insurance Act of Canada, [1932] A.C. 41, [1931] 3 W.W.R. 689, [1932] 1 D.L.R. 97 (P.C.), reversing [1931] 3 D.L.R. 31 (Q.K.B.).

95. A.G. Ontario v. Policyholders of Wentworth Insurance Company, (1969) 6 D.L.R. (3d) 545 (S.C.C.).

96. Ibid., A.C. 113-114.

97. Ibid., A.C. 114.

98. Parsons, fn.16, S.C.R. 245.

99. Ibid., S.C.R. 287.

100. Ibid., A.C. 111-112.

101. Statutes of Canada (1910), 9-10 Ed. VII, c.32. The 1910 Act, section 3, excluded from application of the Act

> any company incorporated by an Act of the legislature of the late province of Canada, or by an Act of the legislature of any province now forming part of Canada, which carries on the business of insurance wholly within the limits of the province by the legislature of which it was incorporated, and which is within the exclusive control of the legislature of such province.

An excluded company could, however, elect to take a license under the Act and where it did,

> such company shall thereafter have the power of transacting its business of insurance throughout Canada.

102. Insurance Reference (1916), fn.94, A.C. 595.

103. Bonanza Creek Gold Mining Company Limited v. Rex, [1916] 1 A.C. 566 (P.C.). The decisions in Bonanza Creek and in Insurance Reference were both handed down on the same date: February 24, 1916.

104. Bonanza Creek, fn. 103, A.C. 576.

105. Ibid., A.C. 585. Lord Haldane referred to his assessment of the 1867 Act in a 1914 Australian case in the Privy Council: A.G. Australia v. Colonial Sugar Refining Company, [1914] 2 A.C. 237 (P.C.). In line with what he had said there, Haldane in Bonanza Creek said the constitutions of the provinces had been surrendered to the Imperial Parliament "for the purpose of being refashioned":

> The result had been to establish wholly new Dominion and provincial Governments with defined powers and duties, both derived from the statute which was their legal source....:

Bonanaza Creek, fn.103, A.C. 579.

Haldane noted that s.65 of the 1867 Act povided that all powers that before Confederation could have been exercised by the Lieutenant-Governor of Ontario shall "as far as the same are capable of being exercised after the Union in relation to the government of Ontario" be vested in the Lieutenant-Governor of Ontario. The effect of s.92(11) is to vest in the Lieutenant-Governor of Ontario and no longer in the Governor-General, the power to incorporate companies in Ontario with provincial objects.

The question remained, however, whether the Crown's prerogative power to incorporate companies with full common-law corporate capacity is still available to a Lieutenant-Governor or whether it had been "abrogated or interfered with" by legislative act so that a Crown charter would no longer grant full corporate capacity beyond provincial objects. The Ontario Companies Act, said Haldane, did not remove the Great Seal of Ontario as the source of the grant of a company's letters patent. The Act merely restricted the cases in which such a grant can be made. Thus, it remained that

> it is by the grant under the Great Seal of Ontario and not by the words of the [Ontario Companies Act]...that the validity of the corporation is to be measured:

Bonanza Creek, fn.103, A.C. 583.

106. Ibid., A.C. 583.

107. Insurance Reference (1916), fn.94, A.C. 595.

108. Russell v. The Queen (1882) 7 A.C. 829 (P.C.).

109. Insurance Reference (1916), fn.94, A.C. 597.

110. Insurance Reference (1913), fn.94, S.C.R. 304. The federal Insurance Act, 1910 was struck down on a 5-4 vote of the Court.

111. Idem.

112. Ibid., S.C.R. 305.

113. See fn.94 for the citations of these two cases.

114. Re Insurance Act of Canada (1932), fn.94, A.C. 45.

115. Ibid., A.C. 51; the 1917 Act was amended in 1927 to conform with the Privy Council decision in Reciprocal Insurers (1924), fn.94.

116. Ibid., A.C. 45.

117. Re Insurance Act of Canada (1931), fn.94, D.L.R. 49 (Q.K.B.).

118. In 1969, the Court declined to set aside federal legislation affecting insurance companies. In

Wentworth Policyholders, supra, fn.95, the Court said Ontario legislation governing the distribution of the deposited securities of an insolvent provincial insurer was invalid as an invasion of the federal jurisdiction over bankruptcy and insolvency under s.91(21). A dissenting minority of four justices said the federal legislation was another colourable intrusion into a provincial field of legislative power, namely, the insurance business, a field that had long been recognized by the courts, according to Justice Hall, as reserved exclusively to the provinces. In Wentworth Policyholders, the conventional view on insurance had its stern defenders.

Where the criminal law power under s.91(27) and the power over aliens under s.91(11) had earlier failed, federal power over bankruptcy and insolvency under s.91(21) succeeded in Wentworth Policyholders without, however, giving rise to an elucidation by the Court of the jurisdictional issues relating to insurance.

119. Multiple Access Ltd. v. McCutcheon, (1982) 138 D.L.R. (3d) 1 (S.C.C.).

120. See also Westfair Foods, (Man. Q.B.), fn.4.

Although the Federal Court of Appeal thought the provision was justifiable directly under s.91(2), the court went on to say that if the provision was "necessarily incidental to effective legislation", as in the third proposition cited with approval by the Privy Council in Fish Canneries (1930) with respect to the reconciliation of conflicts between jurisdictional powers, it would also be justifiable:

> [E]ven if [the provision's] validity has to be assessed on the basis of the third proposition, I would observe that in any event the necessity of means depends on the character of the ends to which they are directed. There is no more a fixed domain of trade and commerce than there is of criminal law.... The necessity of the means is relative to the end sought. Thus

understood as a relational concept, the necessity required for the third Fish Canneries proposition can be seen to be well expressed by the notion of a "rational, functional connection" endorsed by Dickson, J., in Multiple Access:
Québec Ready Mix, fn.4, D.L.R. 400-401.

121. Québec Ready Mix, fn.4, D.L.R. 389-390.

122. Québec Ready Mix, fn.4, D.L.R. 401-402.

123. Ibid., D.L.R. 402.

124. See fn. 44.

125. "Canadian Financial Institutions: Trends and Policy Perspectives," A Working Paper for Discussion and Consultation, Capital Markets Division, Department of Finance, Government of Canada, Ottawa, Ontario, January 1984, p.22-23.

126. Radwanski, George, Ontario Study of the Service Sector: Background Papers (Toronto: Ministry of Treasury and Economics, Government of Ontario, 1986), December 1986, p.247; Currie & Co. Report, fn.132, p.9.

127. M. Farrow and J. Maxwell of Currie,Coopers & Lybrand, Management Consultants, Employment and New Technology in the Insurance Industry, (Toronto: Ontario Publications, 1985), July 1985, Appendix 14 to the Final Report of the Ontario Task Force on Employment and New Technology, ("Currie & Co. Report"), p.10.

128. "Canadian Financial Institutions: Trends and Policy Perspectives," fn.125, p. 5.

129. Radwanski, fn.126, p.244; The Green Paper, fn.137, p.81.

130. Jalynn Bennett, vice-president of corporate development at Manufacturers Life Insurance Company, quoted in "Products on Parade", The Financial Post Moneywise Magazine, March 1988, p.68.

131. Jack Masterman, president and chief executive officer of Mutual Life Assurance Co. of Canada, quoted in "Products on Parade", supra, fn.130.

132. Currie & Co, Report, fn.127, p.8.

133. Report of the Superintendent of Insurance, December 31, 1985, (Ottawa: Government of Canada, 1986), p.29A.

134. Currie & Co. Report, fn.127, pp.14-15. The annuity has enabled insurance companies to remain competitive in the retirement field. With the advent of RRSP's and the development of the Guaranteed Investment Certificate ("GIC's") by banks and trust companies, insurance companies had to develop a comparable product, capable of long-term or short-term savings and within the framework of the RRSP legislation. The annuity went through some changes until, as deferred annuities, they could be offered in competition with GIC's. Deferred annuities are offered by insurance companies with a 90 day guaranteed interest rate or a one-, two-, three-, four- or five-year rate: see "Products on Parade," fn.127.

135. Superintendent's Report, 1985, fn.133, p.8A.

136. The Green Paper, fn.137, p.58.

137. <u>The Regulation of Canadian Financial Institutions: Proposals for Discussion</u>, (Ottawa: Ministry of Supply and Services, Government of Canada, 1985), the "Green Paper", April 1985, at p. 58. Of 314 property and casualty insurance companies, 244 were federally regulated and 70 were provincially regulated. Also, of the 133 trust and mortgage loan companies in Canada, 59 were federal, 63 were deposit-insured provincial companies and 11 were non-deposit, provincial companies outside federal regulation.

138. Superintendent's Report, 1985, fn.133, p.8A.

139. Idem.

140. E.P. Neufeld, <u>The Financial System of Canada: Its Growth and Development</u>, (Toronto: Macmillan of Canada, 1972), at p.233.

141. Reform of Financial Institutions in Québec, Government of Québec, October, 1987, pp.103, 109, 114-116.

142. Idem.

143. Ibid., p.28.

144. As for the international dimension, at the end of the second quarter of 1985, as much as 28% of the total assets of Canadian life insurance companies was held for business placed outside of Canada: Ontario Insurance Exchange Advisory Committee, Report on the Feasibility of an Ontario Insurance Exchange, (Toronto: Ministry of Consumer and Commercial Relations, Government of Ontario, 1983), September 1983, p.65.

In 1983, close to 35% of life insurance in force in Canada was placed with foreign or foreign-controlled "Canadian" insurance companies: idem. See also Neufeld, op. cit., fn.140, at pp.255 et seq. where the author recounts the history of overseas business of Canadian life insurance companies in the period 1900-1968. In 1983, over a third of life insurance sold by Canadian companies was sold outside Canada: Currie & Co. Report, fn.127, p.7.

In 1985, of 152 life insurance companies federally registered, 11 were British companies and 80 were foreign chartered companies: Superintendent of Insurance Report. fn.133, p.1A. Foreign and British companies effected 22.3% of the life insurance sold in Canada in 1985, held 20% of the life insurance in force in Canada at the end of 1985 and received 18.6% of the insurance and annuity premiums received by life insurance companies in Canada in that year: ibid., p.3A.

If one looks at the breakdown of life insurance company investments between domestic and foreign, the latter is a significant proportion. In 1985, about 25% of corporate bond investments were with foreign companies. Approximately 50% of common share investments were in shares of foreign companies. About a third of mortgage loans were placed outside the country while 25% of real estate investments were outside Canada. Half of policy loans and cash loans were placed outside Canada: ibid., p.10A.

145. Post-confederation insurance legislation began with the federal insurance Act of 1868: Statutes of Canada, (1868), 31 Victoria, cap.48.

The first piece of insurance legislation was an Act of the British Parliament in the reign of Queen Elizabeth I: An Act concerning Matters of Assurances used among Merchants, (1601), 43 Elizabeth, cap.XII. It would appear that contrary to the long-established custom Her Majesty's courts were being used to resolve disputes between insureds and their insurers. The Act of 1601 established a body of commissioners whose task it became to adjudicate such disputes. Three of the seven recitals in the Act illustrate the role played by insurance by the end of the 16th century:

> WHEREAS:
>
> (1) it ever has been the Policy of this Realm by all good Means to comfort and encourage the Merchant, thereby to advance and increase the General Wealth of the Realm, Her Majesty's Customs, and the Strength of Shipping; which Consideration is now the more requisite, because Trade and Traffic is not at this present so open as at other Times it hath been:
>
> (2) And whereas it hath been Time out of Mind an Usage amongst Merchants, both of this Realm and of foreign Nations, when they make any great Adventure, (especially into remote Parts) to give some Consideration of Money to other Persons (which commonly are in no small Number) to have from them Assurance made of their Goods, Merchandizes, Ships and Things adventured, or some Part thereof, at such Rates and in such Sort as the Parties Assurers and the Parties assured can agree, which Course of Dealing is commonly termed A Policy of Assurance:

> (3) by Means of which Policies of Assurance it cometh to pass upon the Loss or perishing of any Ship, there followeth not the undoing of any Man, but the Loss lighteth rather easily upon many than heavily upon few, and rather upon them that adventure not than those that do adventure, whereby all Merchants, especially of the younger Sort, are allured to venture more willingly and more freely....

Insurance legislation first arrived in British North America in 1836 with passage of an Act which authorized the establishment of mutual fire insurance companies in Upper Canada. In 1860, a federal Act required fire insurance companies that were not incorporated by any statute of Upper or Lower Canada to obtain a federal licence: 1860, Statutes of Canada, 29 Vict. (2nd Session), c.17; see Foster, R. Leighton, "The Influence of Legislation on the Development of Life Insurance in Canada," (1953) 31 Canadian Bar Review 786 at pp.787-788; E.P. Neufeld, "Canadian Financial Intermediaries: A Century of Development," (1967) 74 (No.1) Canadian Banker 143.

In 1865, legislation by the Province of Canada secured for wives and children the benefits of assurances on the lives of their husbands and parents: 1865, Statutes of Canada, 34 Vict., c.17.

The first insurance agent in British North America was appointed by the Phoenix Assurance Company in 1804. What came to be known as the Halifax Insurance Company started business in Canada in 1809. Quebec Fire began in 1829, Western Assurance Company and Middlesex Mutual began in 1851 and the British American Insurance Company in 1853.

By 1867, there were 40 companies doing business in Canada although only 6 were Canadian. The first purely life insurance companies in British North America were Colonial Life Assurance Company (a subsidiary of Standard Life) and Scottish Amicable which started doing business in 1846-1847: Tumwine-Mukubwa, G., "A History of Regulation of Life Insurance in Canada, 1868-1976," LL.M. thesis, Osgoode Hall Law School, York University, Toronto, Ontario, August 1977, at p. 1; Neufeld, op. cit., fn.140, p.220; see also Rickard, R.A., "The Story of Foreign Activity in the Canadian Life Insurance Business, Part I: The Period up to 1964," (September, 1984) 6 (No.33) Canadian Journal of Life Insurance 19 and (December 1984) 6 (No.34) Canadian Journal of Life Insurance 10.

The first Canadian life insurance company, Canada Life Assurance Company of Hamilton, Ontario, began issuing policies in 1847. The Sun Life Assurance Company was established in 1865 but did not issue life policies until 1871: Rickard, op. cit. (September 1984), p.19; Neufeld, op. cit. (1967), supra, p.145.

In the 1868 Act, insurance companies were prohibited from carrying on the business of insurance "in Canada" without being licensed by the federal Minister of Finance: Statutes of Canada, (1868), 31 Victoria, c.48, s.2. Provincial companies doing business within the province of incorporation were exempted:

> The Provisions of this Act as to deposit and issue of license shall not apply to any Insurance Company incorporated by any Act of the Legislature of the late Province of Canada or incorporated or to be incorporated under any Act of any one of the Provinces of Ontario, Québec, Nova Scotia or New Brunswick, so long as it shall not carry on business in the Dominion beyond the limits of that Province by the Legislature or Government of which it was incorporated, but it shall be lawful for any such company to avail itself of the provisions of this Act. (s.25)

A company that was required to be licensed had to deposit $50,000 with the minister to obtain a licence ($100,000 in the case of a foreign company), to maintain thereafter a deposit of $100,000 and to file a form of annual statement set out in a schedule to the Act: ibid., secs.4,6 and 14. See also Rickard, op. cit.(September 1984), supra, p.19; Tumwine-Mukubwa, op. cit., supra; Foster, R. Leighton, op. cit., supra, p.788; Macdonald, V., "The Regulation of Insurance in Canada," (1946) 24 Canadian Bar Review 257; Report of the Royal Commission on Dominion-Provincial Relations: Canada 1867-1939, ("the Rowell-Sirois Report"), (Ottawa: Government of Canada, 1940), vol II, chap IV, s.4, p.59; Neufeld, op. cit., fn.140, p.234.

By the early 1870's pressure for government inspection of company operations began to appear in the wake of scandalous behaviour by some British and American companies. Insurance companies were developing a bad name. Between 1844 and 1869, of the 355 insurance companies established in that period, 328 went out of business in the same period. In 1868, 30 companies were launched while 17 went bankrupt: Neufeld, op. cit., fn.140, pp.234-235.

Stricter legislative control over life insurance companies was attempted at the federal level in 1871 but defeated as a result of successful insurance industry opposition: Neufeld, supra. By late 1872 and early 1873, the idea of a government insurance commissioner was being advocated. See Neufeld, op. cit. (1967), supra, where the author quotes the Monetary Times editorials of the day:

> Had we an Insurance Commissioner armed with the necessary powers and guided by the well-established principles of life insurance, we should not have such an institution as the Citizens Insurance Company of Montreal flaunting its delusive announcements in the face of the public -- advertising to the world a million dollars of capital when it really has not $10,000 paid up in cash....
>
> A salutary effect of wise governmental supervision would be to impart greater confidence in Canadian companies by giving the public the fullest and most satisfactory assurance of their soundness....

Concern for the growth of Canadian insurance companies was not overlooked by the editorialist:

> It is well known with what rapidity the business of life insurance has grown amongst us even though the policies have been sent from abroad; but had we once impressed on the public mind the fact that home companies were as successful, as safe, and as liberal as the best of those organized and conducted in other countries, and which now carry out of Canada such large sums annually, the result would be a more general resort by our people to the benefits of life insurance....

New federal legislation in 1875 and 1877 required life insurance companies to maintain assets in Canada sufficient to cover their Canadian obligations, to include with their liabilities actuarial reserves sufficient to cover policyholders' claims and to publish financial statements annually. A Superintendent of Insurance was established and charged with examining the annual statements and investigating the financial position of insurers: Statutes of Canada, (1875), 38 Victoria, c.20 and 21; Statutes of Canada (1877), 40 Victoria, c.42. See Rickard, op. cit. (September 1984), p.19; the Rowell-Sirois Report, supra, p.59. The exemption of provincial companies doing business within the province of incorporation remained in the legislation: Statutes of Canada (1875), 38 Victoria, c.20, s.2; (1877) 40 Victoria, c.42, s.28.

Canada's first Superintendent of Insurance emphasized that there should be no secrecy about the affairs of an insurance company, that the directors were only "trustees" or agents for the disposition of the money entrusted to them by policyholders who had the right to know what was done with the money entrusted to the companies: Neufeld, op. cit., fn.140, p.237. The word "trustee" is not used in its technical sense but only to indicate that the insurer had a duty to preserve its solvency in order to repay the moneys "entrusted" to it by its customers. It is around this time that regulators begin to see insurance companies as financial intermediaries and, as such, trustees of the moneys given to them. The new federal superintendent emphasized publicity and solvency as the basis for regulation and supervision.

Although Parliament was the first of the two legislative levels to enter the insurance field, provincial insurance legislation soon developed alongside the federal legislation. Three reasons have been suggested for this: see Foster, op. cit., supra, p.792. First, and as mentioned earlier, the 1867 Act failed to assign insurance to either the federal or the provincial level. Second, friendly or fraternal societies had been exempted from the federal Act of 1868: Statutes of Canada (1868) 31 Victoria, c.48, s.20. Third, there existed a large number of small provincial companies, for the most part fire insurance companies, doing business only within their province of incorporation and they were also exempt from the federal Act of 1868.

By 1893, two life insurance companies and 69 fire insurance companies were operating in Ontario under provincial licence and inspection exclusively, while there were only 6 Canadian fire insurance companies registered under federal insurance laws: Foster, op. cit., supra, p.793. The first Ontario superintendent of insurance was appointed in 1879, only four years after appointment of the first federal superintendent.

In the 1870's, in Ontario, a pivotal event occurred in the legislative history of insurance. Mr. Justice Wilson (later Chief Justice) of the Ontario Supreme Court, in deciding a case before the Court, criticized insurance companies in how they do business:

> This [policy provision requiring the insured to produce a wealth of information in support of his claim] is a degree of inquisitorial power, under the penalty of a forfeiture of the insurance money, which it is vexatious and difficult to comply with, and which is about equal to a forfeiture of itself, and almost a perfect immunity to the insurers against ever paying the money.

* * *

> The conduct of companies, when enforcing rigidly such conditions, has often been complained of by the courts by reason of the number and nature and difficulty of the conditions they introduce into their policies; and the time perhaps has come when the legislature should interfere, to stand between them and those they insure or pretend to insure, or, in other words, the public, by limiting them to such conditions which the courts shall determine to be reasonable.
>
> As the companies have not adopted and are not likely to adopt of their own accord, that mode of doing business, the only way is to force it upon them by the legislature enabling the courts to prohibit and restrict their conditions. And when that is done, the companies will be obliged to be more careful of the risks which they take:

Smith v. Commercial Union Insurance Company, (1872) 33 U.C.Q.B. 69 (O.S.C.), quoted by Foster, op. cit., supra, pp.794-795; see also the Rowell-Sirois Report, supra, p.60.

His Lordship's comments led to the appointment of a provincial royal commission in 1875. In the following year Ontario insurance legislation required all fire insurance companies doing business in the Province to insert certain prescribed terms and conditions in their policies: Fire Insurance Policy Act, 1876, Statutes of Ontario (1875-1876), 39 Victoria, c.24; see E.B. MacLatchy, "Insurance Law: 1923-1947," (1948) 26 Canadian Bar Review 202 at 216 et seq.; Marvin G. Baer, "Harmonization of Canadian Insurance Law," in Harmonization of Business Law in Canada, R.C.C. Cumming, ed., vol. 56, studies for the Macdonald Royal Commission on the Prospects for the Economy, p.207 and pp.213-215. These "statutory conditions" would become the basis for exclusive provincial jurisdiction over insurance as a matter of property and civil rights.

The Ontario Act of 1876 also required that an insurance company, other than a company licensed under the federal Act to transact the business of insurance in Canada, must secure a licence from the Province: Statutes of Ontario (1875-1876), 39 Victoria, c.23, ss.1 and 2. Federal legislation at that time, as we have mentioned, required all insurance companies, other than provincially incorporated companies doing business within the province of incorporation, to obtain a federal licence. In this fashion, then, a division of the jurisdictional field was made. See also the Rowell-Sirois Report, supra, p.60. As friendly or fraternal benefit societies were exempted from the federal legislation, these companies began to fall under provincial legislative control: Foster, op. cit., supra, p.792.

A federal Royal Commission on Life Insurance was appointed in 1906. By the turn of the century insurance company scandals in the United States were causing public concern in Canada about insurance company practices. In July 1905, a joint committee of the Senate and Assembly of the State of New York was formed to investigate the affairs of the American life insurance industry. The Armstrong Committee, as it was called, reported on February 22, 1906: see V. Evan Gray, "An Evolutionary Pattern in Insurance Legislation," [1950] Insurance Law Journal 567 at 571. The report was comprehensive in its breadth and included consideration of matters as diverse as corporate governance, political contributions and the remedies of policyholders: Gray, op. cit., supra, p.571.

The earlier comments of Canada's first superintendent of insurance as to the trust imposed upon insurers were reinforced by the American committee's report. Directors of insurance companies, said the committee, are trustees for policyholders as well as shareholders. The corporation is a custodian of trust funds. The funds of life insurance companies were not to be controlled and managed by the companies as absolute owners of the funds: ibid., p.572.

In its report in 1907, the federal Royal Commission in Canada affirmed that life insurance companies and their directors were "trustees" of the funds entrusted to them by policyholders: idem. See also Neufeld, op. cit., fn.140, p.238 et seq. The 1907 report included a draft Bill which became the basis for the federal insurance legislation of 1910: Statutes of Canada (1910), 9-10 Ed. VII, c. 32.

The 1910 Act, as with the earlier federal legislation, did not apply to provincial companies doing business within the province of incorporation: ibid., s.3.

The 1910 Act, like the earlier legislation, required insurance companies doing business outside the province of incorporation to take out a federal licence. The Act also extended the supervision and control of life insurance companies in such areas as actuarial reserves for liabilities, the publication and auditing of annual and financial statements, investment powers, corporate governance and shareholders' and policyholders' rights in the distribution of profits: see Rickard, op. cit. (September 1984), supra, pp.20-21 and Foster, op. cit., supra, pp.790-791.

Investment powers of federal life insurance companies were first regulated substantively by the 1910 Act. Special investment powers in individual company charters were cancelled. A life insurance company, for example, could not hold more than 30% of the common stock of a company and could only buy common shares where the company had paid regular dividends of at least 4% for seven years: Neufeld, op. cit., fn.140, pp.240-241. These specific limitations replaced the general provisions legislated in 1899 which did not control the investment powers vested by company charter.

The 1910 Act also included mandatory policy conditions applicable to life insurance policies: Statutes of Canada (1910), 9-10 Edward VII, c.32, s.95.

In 1917, after the defeat of the 1910 Act in the Privy Council in Insurance Reference (1916) as an interference with provincial jurisdiction over civil rights, the federal government revised its insurance legislation to permit the issuance (rather than require the holding) of federal licenses but coupled this legislation with an amendment to the Criminal Code making it an offence to carry on the business of insurance without having a licence: Statutes of Canada (1917), 7-8 Geo. V, c.26, s.1 and c.29, s.4.

The legislation of 1917 was also defeated in the Privy Council in Reciprocal Insurers (1924) as an attempt to do indirectly, through the criminal law power, what the Privy Council in the 1916 case had decided Parliament could not do directly, namely, regulate the business of insurance.

In 1922, the Commissioners on Uniformity of Legislation in Canada began working on a uniform statute for life insurance contracts and on July 1, 1924 a uniform act came into force in all the provinces except Québec. The uniformity of the law resolved the conflict of laws problem as to the law of the contract where policies are issued in one province and delivered in another or the insured changes his or her address to another province or dies in another province where he or she makes a will leaving beneficiaries in yet other provinces: see Gray, op. cit., supra, pp.572-573.

A further attempt at federal control of insurance companies, this time using the federal power over aliens, was defeated in the Privy Council in Re Insurance Contracts (1926) and Re Insurance Act (1932), as discussed in the text, Part IV.

In 1932, after the jurisdictional defeats of 1916, 1924, 1926 and 1932, Parliament passed the Canadian and British Insurance Companies Act ("CBIC Act"), the Foreign Insurance Companies Act ("FIC Act") and the Department of Insurance Act: Statutes of Canada (1932), 22 George V, c.45, 46 and 47. The two insurance company statutes are concerned with corporate solvency, governance and investment powers and remain in force to this day although amended several times over the years and most recently by Bills C-42 and C-56. The third statute has been repealed by Bill C-42: Financial Institutions and Deposit Insurance System Amendment Act, Statutes of Canada (1986-1987), c.23, proclaimed July 2, 1987.

146. The Green Paper, fn. 137, at p. 77 et seq.

Changes in the Bank Act in 1954 and in 1967 allowed banks, for the first time, to take chattel mortgages as security for consumer loans and to make conventional mortgage loans. In 1967, the ceiling on chartered banks' loan rates were removed and reserve requirements on banks' notice and term deposits were reduced thus enabling the banks to compete for term savings. Until the changes to the Bank Act in 1954, mortgage lending was the basic staple of trust and loan companies and the co-operative credit institutions. Sales finance companies were the major suppliers of consumer credit.

A 1984 Library of Parliament paper summarized the market changes of the past decade in the following terms:

> During the 1970's the emergence of an increasingly better-educated work force coupled with persistent inflation and extended periods of low or negative real interest rates gave consumers a new awareness of the need to preserve the real value of their savings. Distortions created by inflation were ultimately responsible for a more sophisticated consumer today. Loyalty to a specific company withered in the advent of a more earnings-sensitive savings behaviour. Product differentiation commanded less market influence and power than up front price competition....For insurance companies, the traditional source of funds from whole-life policies has virtually dried up as more people opted for term insurance....The upheavel caused by inflation in the traditional activities of the "four" pillars forced each of them to venture into new areas of business and

> provide new products and services in order to strengthen their traditional positions and diversify future risks. By and large, these new products and services are substitutes for those hitherto provided by another class of institution:

Chan, Randall, "Financial Services Industry: Integration and Public Policy Issues," Economics Division, Research Branch, Library of Parliament, Government of Canada, Ottawa, Ontario, September 20, 1984, pp.2-3.

See also: Final Report, Ontario Task Force on Financial Institutions, J. Stefan Dupré, Chairman, ("Dupré Report"), December, 1985, (Toronto: Ministry of Consumer and Commercial Relations, Government of Ontario, 1986), p. 33:

> This expansion of activities beyond the core functions has, in many cases, been a useful development enlarging the competition among financial institutions for the benefit of the public. However, the diversification of financial institutions into an ever-expanding range of markets has posed particular problems for regulators and policy-makers who historically have monitored these intermediaries for liquidity and soundness on the basis of their core functions. Obviously, the considerations applicable to the monitoring of deposit-taking business differ substantially from what would be appropriate for an insurance business.

The Dupré Report concluded, *inter alia*, at p.36, that

> 8. This expansion of activities...has created new problems...which require a clear recognition that, as the functions of financial institutions change, the system of regulation and supervision must also change;
>
> -----
>
> 10. The public interest in an effective capital market and the public's expectations as to that market require the maintenance of

> an effective regulatory system capable of rapid adjustmwent to the ever-changing risks being assumed by financial institutions.

The Dupré Report acknowledged that financial institutions had come to the stage where they offered

> an ever-growing variety of products that bring these institutions into direct competition with one another in markets removed from their historical core functions.

The implications for the federal government and the provincial governments and for federal-provincial relations, according to the Dupré Report, were serious: p.37.

147. Currie & Co. Report, fn.127, p. 10.

In an address to an international meeting of senior insurance executives in Vienna in July, 1985, an American lawyer and international trade expert describes the impact of technology in these terms:

> Computer and telecommunications technology is bringing new competitors into the financial services industry. The capability in electronics transfer and/or credit cards of companies such as ATT, ITT, IBM Siemens, Phillips and Olivetti will lead them eventually to compete with banks. Automated teller machines (ATM's) are but the first expression of a technological revolution which will, in due course, enable the customer to handle all his needs for financial services and his payments through his home computer. Already Chemical Bank has created a joint venture with ATT to use electronic transfers as a method of avoiding restrictions on inter-state banking:

Thibaut De Saint Phalle, Minutes of Proceedings of the House of Commons Committee on Finance and Economic Affairs ("Blenkarn Committee"), Issue # 70 (September 24, 1985) at p. 70A:84.

In the United States, according to Mr. Phalle, American Express has acquired a large off-shore banking system, a multi-line insurance company and a major securities firm. Sears Roebuck, a major retailer, has acquired a securities firm, a major real estate brokerage company and a savings and loan company. These acquisitions were in addition to the insurance company that Sears-Roebuck had already owned for some years. Merrill Lynch, the investment dealer, has acquired a bank in the United States and a savings and loan company. It also developed the first "cash management account" by which it gave its brokerage customers the ability to write cheques against their securities brokerage accounts.

148. "The Structural Evolution of Financial Markets and Institutions: The Implications for Regulation," A Working Paper for Discussion and Consultation, Capital Markets Division, Department of Finance, Government of Canada, Ottawa, April, 1984, pp.13-14.

A recent report in The Globe & Mail provides an illustration of how interprovincial business might be conducted from within a single province. In September 1986, according to the report, DirecTrust, a division of Counsel Trust Co. of Toronto, established a 24-hour financial service whereby customers can deposit money or obtain mortgages by telephone. Since then the company has written $82 million in business (with almost a third of it conducted outside of regular working hours). The report says DirecTrust has only a single fourth floor Toronto office, spends more than $1 million per year on advertising: The Globe & Mail, National Edition, December 21, 1987, p. B16.

Peoples Trust Co., a Vancouver-based, federally chartered trust company, is reported to have agreed to pay a $25,000 out-of-court settlement to the Ontario government for taking deposits by mail from Ontario residents. The company ran advertisements in Ontario newspapers inviting deposits from Ontario residents. The trust company took the view that it was entitled to take deposits by mail. The province of Ontario said the company had to be registered with the Ontario government. See "Peoples Trust settles dispute" by Virginia Galt, The Globe & Mail, National Edition, March 25, 1988, p.B6.

149. Walker, David, Executive Director, Bank of England, in a lecture given in Toronto as the Kimber Fellow at York University and the University of Toronto, September. 1987, published as "Some Reflections on Big Bangs in Financial Systems," (1988) 13 Canadian Business Law Journal 388 at 389.

150. One of Canada's first financial supermarkets is Geoffrion Leclerc Inc., 45% owned by Laurentian Group, the Montréal-based financial services conglomerate. Geoffrion Leclerc operates a "carrefour", or shopping centre, on the main floor of the Laurentian Building in downtown Montréal. Each of the financial services --securities, banking, insurance and trust services-- is housed in a separate office off a central lobby. According to Patricia Lush in The Globe & Mail, National Edition, January 7, 1988, once inside the offices of any one of the financial services offered, there is no indication of the presence nearby of the related offices providing the other financial services. The idea, however, is that the salesmen will refer clients back and forth. Geoffrion Leclerc is 20% owned by a Paris-based investment banking company and itself acquired two smaller Toronto-based investment dealers. Last year, the company opened offices in Calgary and Vancouver.

151. Although the stock market crash of October 19, 1987 may have, for the present, tempered corporate enthusiasm for equity financing.

152. New Directions For The Financial Sector, The Honourable Thomas Hockin, Minister of State for Finance, tabled in the House of Commons, Ottawa, Canada, December 18, 1986 ("the Blue Paper"); see also Executive Summary: New Directions for the Financial Sector, The Hon. T. Hockin, December 18, 1986 ("the Blue Paper: Executive Summary").

153. The Blue Paper: Executive Summary, fn.152, p.2.

154. Ibid., p.7.

155. Non-resident firms will enjoy the same extensions of powers as domestically owned institutions. Non-resident banks and other non-resident controlled financial institutions will be allowed to own a securities dealer up to 50% as of June 30, 1987 and up to 100% as of June 30, 1988, in line with Ontario's announced changes of December 4, 1986: Blue Paper, fn.152, pp.12-14.

156. On March 3, 1987, the federal government introduced Bill C-42 in the House of Commons, the first of three stages of the federal reform program relating to federal financial institutions, including insurance companies. The second stage arrived with introduction of Bill C-56 on May 7, 1987. Both Bills, after a few amendments, received Royal Assent on June 30, 1987 and were proclaimed a few days later: Bill C-42: Financial Institutions and Deposit Insurance System Amendment Act, S.C. 1986-1987, c. 23, proclaimed July 2, 1987; Bill C-56: An Act to amend certain Acts relating to financial institutions, S.C. 1986-87, c.26, proclaimed July 3, 1987; see also Bill C-81: Statute Law (Financial Institutions) Amendment Act, 1987, First Reading June 30, 1987, amending parts of Bill C-56.

In late December, 1987, the first part of the third stage was launched with the release of draft legislation relating to federal trust and loan companies. The minister, Mr. Hockin, has announced that the trust and loan companies Bill will be introduced in the House of Commons some time during the summer of 1988 and shortly thereafter the Bills relating to banks, insurance companies and co-operative credit organizations will be introduced. According to the minister, the effective dates for implementation would be the same for all the legislation, namely, January 1, 1989 (the date the Canada-U.S.A. free trade agreement comes into effect), as the federal government does not want one pillar of the financial sector to "get the jump" on the others: "Trust, loan legislation coming this summer", by Angela Barnes, The Globe & Mail, National Edition, May 26, 1988, p.B3.

Bill C-42 legislates in the areas of supervision and deposit insurance. The Bill establishes the Office of the Superintendent of Financial Institutions ("SFI") to perform the duties of superintendent in 11 federal statutes listed in a schedule to the Bill, two of which statutes are the Canadian and British Insurance Companies Act and the Foreign Insurance Companies Act. Other statutes listed include the Bank Act, the Investment Companies Act, the Loan Companies Act, and the Trust Companies Act: s.6, Office of the Superintendent of Financial Institutions Act, and Schedule to Part I of Bill C-42, Financial Institutions and Deposit Insurance System Amendment Act.

The powers of the SFI under Bill C-42 include the power, when instructed by the minister, to "inspect and examine" the affairs of an insurance company that is governed by either the CBIC Act or the FIC Act, to determine whether it is able to meet its obligations. Where the SFI is of the opinion that the asset valuations of an insurance company are unsatisfactory or that the company will not be able to pay its liabilities when they become due, or

> that there exists any practice or state of affairs that is materially prejudicial to the interests of the policyholders or creditors of the company,

the SFI may immediately take control of the assets of the company: ss.91.1(1) and 145.1, CBIC Act; s.50.1, FIC Act.

Bill C-42 also amends the Canada Deposit Insurance Corporation Act ("CDIC Act"), R.S.C. 1970, c. C-3. The CDIC Act mandates deposit insurance for all federal deposit-taking institutions and offers this insurance to provincial deposit-taking institutions if the latter become members of the Canada Deposit Insurance Corporation ("CDIC").

CDIC regulates by by-law and supervises by virtue of its investigative and disciplinary powers. Section 8 of the CDIC Act sets out the objects of CDIC. Bill C-42 amends this section to include the power (underlining added)

> (b) to be instrumental in the <u>promotion of standards of sound business and financial practices</u> for member institutions and <u>to promote</u> and otherwise contribute to <u>the stability and competitiveness of the financial system in Canada</u>:

Bill C-42, clause 57, amending s. 8, CDIC Act.

To become a member of CDIC an institution has to be approved by CDIC and, in the case of a provincial institution, the institution must agree not to exercise powers substantially different from the powers exercisable by a (federal) trust company under the <u>Trust Companies Act</u> (Can.) and by a (federal) loan company under the <u>Loan Companies Act</u> (Can.) and, in addition, CDIC must be satisfied that at all times CDIC will have "adequate access" to information regarding the member institution: See Bill C-42, clause 62, repealing s. 16, CDIC Act, and replacing it with a new s.16.

Bill C-42 enables CDIC to impose a premium surcharge on a member that engages

> in such practice as may be prescribed in the by-laws:

Bill C-42, clause 65, as amended at Committee, repealing s.19.1, CDIC Act, and replacing it with a new s.19.1. This wording is the result of amendments made at committee stage. The original wording in the Bill was:

> not following a standard of sound business and financial practices.

The change in wording was made to obscure the reason for the surcharge. Committee members were afraid that depositors would lose confidence in an institution in the event of a surcharge being applied pursuant to a provision that makes reference to business and financial practices: see Blenkarn Committee, Minutes of Proceedings, Issue #62, pp. 33-34, June 8, 1987. The premium surcharge power is described by the minister as CDIC's "intermediate weapon". CDIC's "atomic weapon" is cancellation of the deposit insurance: Blenkarn Committee, Minutes of Proceedings, Issues 55 (pp. 37, 39 and 40), 62 (pp. 7-8, 26-27) and 67 (pp. 32-33).

As a condition of deposit insurance coverage for a provincial institution, CDIC, or a person designated by it, has the right, at least once a year and at such other times as CDIC deems appropriate, to inspect "the affairs" of the provincial institution: Bill C-42, clause 66, repealing s.22, CDIC Act, and replacing it with a new s.22.

Bill C-56, the later of the two Bills, gives the SFI compliance and cease-and-desist powers, strengthens financial standards for (federal) insurance companies and allows (federal) financial institutions to engage in the business of securities trading.

The powers of the SFI as first provided in Bill C-42 are strengthened in Bill C-56 by the provision of compliance and cease-and-desist powers. Where, in the opinion of the SFI, an insurance company, or a person in respect of the company,

> is committing or pursuing or is about to commit or pursue any act or course of conduct that is an unsafe or unsound practice in conducting the business of the company,

the SFI may direct the company or the person to (a) cease or refrain from doing the act or pursuing the course of conduct or (b) perform such acts as the SFI deems necessary to remedy the situation: s.71.2(1), CBIC Act; s.26.1(1), FIC Act. If this process proves ineffective, the minister may, in the case of a Canadian insurance company, direct the SFI to take control of the company: s.91.2(2) and (3), CBIC Act; in the case of a British or foreign insurance company, to take control of the company assets in Canada: s.146(4), CBIC Act, s.51, FIC Act.

Where the SFI takes control of a Canadian company, all the "powers, duties, functions, rights and privileges" of the directors and officers of the company are suspended and the SFI shall manage "the business and affairs" of the company: s.91.3, CBIC Act, as amended by cl.115, Bill C-42. In the case of a British or foreign company, the SFI has power to manage the assets of the company: s.146.01, CBIC Act, s.52, FIC Act.

In December, 1987, the federal government released "Discussion Draft Legislation" with respect to federal trust and loan companies. It is expected that the Canada Insurance Companies Act, yet to be released, will contain much the same provisions as are contained in the draft Trust and Loan Companies Act.

The general power of a (federal) trust company to provide financial services is found in clause 4A.1(1) which reads as follows:

> a company shall not engage in or carry on any business other than such business generally as appertains to the business of providing financial services.

The term "financial services" is not defined. If the trust company intends to accept deposits, it must become a member of CDIC: cl. 4A.1(2). The non-financial undertakings that are permitted to a trust company are listed in the draft legislation: cl. 4A.1(3).

Clause 4A.2 sets out the "core function" that is reserved for trust companies. A similar clause will appear in the forthcoming insurance companies draft legislation and will reserve the core function of selling insurance, presumably. Clause 4A.4 prohibits a trust company from undertaking "the business of insurance" (not defined).

The Canadian Life and Health Insurance Association ("CLHIA") has recently expressed its concerns with respect to the core trustee function given to trust companies in the draft Trust and Loan Companies Act. CLHIA has said it wants life insurance companies to be permitted to act as trustees in the administration of pension plans, retirement savings and other deferred income plans and of funds payable under insurance contracts:

> We are concerned that, as worded, clause 4A.2(b) may not be sufficiently clear to allow this limited exception for life insurers:

CLHIA Submission on the Discussion Draft of the Trust and Loan Companies Act, enclosure with Circular 4638, dated February 19, 1988, at pp.17-18. The mention of a "limited exception" for life insurers, one of the four "pillars", to encroach in the core function area of another "pillar", reflects the crumbling of pillars that has brought on the federal reforms to begin with.

Clause 5C1.2 allows a federal trust and loan company to have "a substantial investment" in, inter alia, a financial institution, a provincial trust, loan or insurance corporation or an underwriter or dealer in securities. CLHIA disagrees with including a definitive list of the subsidiary or affiliated companies in which a company may have a substantial investment:

> We are concerned about the approach of limiting to a specific list those subsidiaries which we may form, without any provision for adding further "ancillary business corporations" to the list as circumstances change. It is impossible to provide for every conceivable type of activity in which we may, in the future, or even now, properly engage through a subsidiary.... There is nothing sinister about the word "ancillary" - it simply connotes a type of business which is relevant to the core function of a financial institution:

CLHIA Circular No. 4638, dated February 19, 1988, p.20. One might ask what is meant by "relevant to the core function". Is this phrase a euphemistic cover for any business that makes money for the insurance company and its clients? The word "ancillary" is already found in this connection in the Canadian and British Insurance Companies Act, section 65(1)(g), which enables federal insurance companies to incorporate any corporation to carry on a business that is "reasonably ancillary to the business of insurance".

By clause 5C1.3, where a federal trust company has a substantial equity investment under clause 5C1.2, the company shall, where the investment is in a provincial trust, loan or insurance company or in an underwriter or dealer in securities,

> give such undertaking regarding the activities of the body corporate and <u>access to information</u> about the body corporate as may be required by the superintendent.

Clauses 5E.3, 7A2.1 and 7A2.2 give the SFI the right to have access to information about a federal trust company <u>or about any company that a federal trust company controls or in which it has a substantial investment</u>.

Clause 4B1.2 allows a federal trust company to combine funds held in trust into a "common trust fund" for the purpose of "facilitating investment of the fund". This enables trust companies to create a kind of mutual trust fund.

Less restrictive investment standards are proposed in clause 5A.2:

> that a reasonable and prudent person would apply to a portfolio of investments and loans to avoid undue risk of loss and to obtain a reasonable return.

It is believed that the federal government intends to increase the staff of the SFI so that the SFI can "play a more hands-on role in making sure companies meet the general standard of the "prudent portfolio". The SFI will be able to revalue real estate that the SFI feels is overvalued by the trust or loan company that owns the real estate or holds security against it, a problem that seems to have played a major part in the collapse of the Principal Group companies in Alberta in the summer of 1987:

> Mr. Hockin said he thinks that the sort of conduct that led to the collapse of Edmonton-based financial services network Principal Group Ltd. would have been obviated under the proposed federal rules. "From what I know ... a number of the guidelines in our regulations would have been violated" by Principal Group, he said....
>
> While his proposed rules would not be applied to provincially regulated organizations such as Principal Group, Mr. Hockin indicated he is trying to get the

provinces to harmonize their regulations with Ottawa's:
John Kohut, "Draft Bill Broadens Powers of Trust Firms," The Globe & Mail, National Edition, December 22, 1987, pp. B1-B2.

According to Kohut, the prohibition against trust companies undertaking "the business of insurance" is meant to prohibit the companies from selling or taking applications for insurance, other than credit insurance. Trust companies will not be allowed to rent out space in their branches to an insurance agent, although they will be allowed to display advertising material from an affiliated insurance company.

Insurance agents, since mid-1986, have been lobbying the federal government to prevent reforms that would allow banks or trust companies to get into the direct selling of insurance: see "Agents laud restrictions on who can sell insurance," by Angela Barnes, The Globe & Mail, National Edition, December 30, 1987, p.B3.

In Québec, insurance brokers have been engaged in a quarrel with Le Mouvement des Caisses Populaires et d'Economie Desjardins. In December, 1987, the brokers started a boycott of the Desjardins credit union, protesting direct sales of insurance by the credit union in some of its 3,500 caisses populaires scattered throughout Québec: see "Insurance Feud puts Québec in Centre of Deregulation Fight," by Benoit Aubin, The Globe & Mail, National Edition, December 23, 1987.

The Toronto-Dominion Bank recently announced that it is interested in selling insurance in its branches and that it could do so for much less cost to the consumer than what can be obtained through an agent: see "TD would sell Insurance, but Claims 'lobby' Stops it," by Virginia Galt, The Globe & Mail, National Edition, January 21, 1988, pp. B1 and B4.

Insurance industry leaders were angered by the comments of the T.-D. Bank and denied that the restriction on banks was the result of insurance industry lobbying: "Insurance Industry denies 'lobby' restricting banks," by Lawrence Surtees, The Globe & Mail, National Edition, January 22, 1988, p.B5. The associations of insurance agents and brokers are prepared to fight the banks on behalf of more than 30,000 property and casualty insurance brokers and 20,000 life insurance agents: "Banks Target insurance turf," by Fred Lebolt, The Financial Post, Weekly/Weekend Edition, February 27-29, 1988.

The insurance agents and brokers, according to The Financial Post, fear that the banks, with their extensive branch networks, will drive independent brokers out of business and that consumers will not receive the expertise and choice now available through the agents and brokers. They also worry that the banks might abuse their influence over their customers by coercing loan and mortgage applicants into doing their insurance business through the banks.

The banks claim that consumers could save as much as 10% on insurance premiums if banks could sell insurance directly: "Banks fire first shot in insurance battle," by Virginia Galt, The Globe & Mail, National Edition, March 9, 1988, p.B1-B2.

157. On the day that Bills C-42 and C-56 became law, June 30, 1987, the $1.2 billion Edmonton-based financial services network of Principal Group Ltd. ("PG") began its collapse, with losses resulting for private investors throughout Western and Atlantic Canada.

On June 30, 1987, the Alberta government cancelled the licenses of two investment dealer PG subsidiaries, namely, First Investors Corp. Ltd. and Associated Investors of Canada Ltd., due to their insolvency. On August 10, 1987, PG itself went into bankruptcy. Soon after, the Alberta Court of Queen's Bench appointed Calgary lawyer William Code to conduct an inquiry into the failure of the two investment companies.

The Code inquiry has heard testimony from PG employees that regulators in Alberta, Saskatchewan and B.C. were often critical of the business practices of several of the PG companies, including the two investment companies. When the Alberta government cancelled the licences of the two investment companies, 67,000 investors in Atlantic and Western Canada lost about $150 million of their $467 million investment.

According to the reports in the press, testimony and documentation submitted to the Code inquiry to date indicates improper conduct by both officers and employees of the PG companies and possibly also by officials of the Alberta government. One press report on the inquiry offered the following comment:

> The picture that has emerged from the inquiry so far is of a company that was rotten from the inside out and from the outside in, and of a Government that was aware of the problems but allowed business to proceed as usual:

Matthew Fisher, "Many Will Share The Blame for Principal Group's Collapse," The Globe & Mail, National Edition, December 21, 1987, p. B8.

A team of accountants from Clarkson Gordon Inc. has submitted to the Code inquiry a six-page list of the companies that were part of the PG empire. After a ten-month "paper chase", the accountants traced as many as 127 companies and, according to inquiry counsel, the search is not over yet. The accountants reported that 36 of the companies used the name "Principal" in their corporate name and 21 were numbered companies registered in Alberta and Ontario. Other companies were registered in Alberta, B.C., Arizona, New Jersey, Delaware, Colorado, Texas, Georgia and the Cayman Islands: see "Principal Connections Traced to 127 Firms," by Matthew Fisher, The Globe & Mail, National Edition, March 17, 1988, p.B7.

Among the investors that may lose all or a substantial portion of their personal savings are 14,000 (approx.) B.C. residents who have about $165 million at stake in the two PG investment companies that failed. The B.C. investors argue that the B.C. government is responsible for allowing the Principal Group companies to carry on business in B.C. at a time when the true value of the assets of these companies was less than their liabilities to depositors and when the company officials were transferring depositers' funds to companies that were not deposit insured. The B.C. investors have formed the Principal Investors Protection Association of B.C. and plan to sue the B.C. government after the Code inquiry submits its report: see "Western Provinces seek Regulatory Accord," by John Twigg, The Financial Post, February 1, 1988, p.6.

Documents submitted to the Code inquiry indicate that three years before PG declared bankruptcy on August 10, 1987, its savings and trust subsidiary, Principal Savings and Trust Co., was threatened by CDIC with losing its deposit insurance due to its "unsound business and financial practices."

The documents indicated a series of disputes between CDIC and the subsidiary with respect to its failure to comply with numerous CDIC rulings with regard to overborrowing and inter-corporate real estate and mutual fund transactions. According to reporter Matthew Fisher in The Globe & Mail, National Edition, February 2, 1988, p.B8, the central issue was a difference of opinion over the appropriate ratio of borrowings to capital base. CDIC suggested a ratio of 15:1 while the company president (and son of the PG founder and chief executive officer) thought 18:1 or 20:1 more appropriate. This dispute began as far back as September, 1981.

In a letter to the company president in May, 1984, CDIC's chief executive officer advised that

> present total indebtedness in respect of moneys borrowed by [the company] is substantially in excess of the limit [CDIC] believes is appropriate...that the company has exposed itself to inordinate risk by not following the sound business and financial practice of matching the maturities of its assets and liabilities.

CDIC gave the company 30 days to correct the situation or its deposit insurance would be cancelled. A few months later, CDIC apparently accepted the changes made by the company, but warned that CDIC would "monitor the situation closely." It is not clear whether this particular company continued its operations in good standing, up to the PG bankruptcy in August, 1987, or whether it, too, became insolvent.

For background on the Principal Group collapse and Donald Cormie, see also "The Rise and Fall of Principal," Canadian Lawyer, May 1988, p.19-24.

158. Canadian Life and Health Insurance Association, Circular 4638, dated February 19, 1988, Appendix A, pp.1-2. See also a study dated February 23, 1988 by Professors Nicolas Roy and Yvan Bernier of Laval University: A Detailed Submission on the position of Québec-chartered Insurance Companies, prepared for C.L.H.I.A. in conjunction with the latter's brief on the draft federal Trust and Loan Companies Act, at p.31:

> The Québec companies consider the draft Federal Trust and Loan Companies Act (sic) a veiled attempt to regulate all financial institutions through heavy, piecemeal regulation.... [W]e wish to voice our profound disagreement with the establishment of a heavy tentacular monitoring system by the Federal Government.

159. Blenkarn Committee, Minutes of Proceedings, Issue #68 (June 16, 1987), p.9-10.

160. See Lederman, W.R., "The Creation of Corporate Bodies and the Functional Regulation of Legal Persons in the Canadian Federal System," chapter 18, Continuing Canadian Constitutional Dilemmas, (Toronto: Butterworths, 1981), p.337 at p.344:

> Why is it that we can distinguish the power to incorporate from the power to regulate?.... The fundamental juristic truth is that all legal relations are interpersonal. So, the definitions of persons by the legal system logically can be distinguished from the regulatory control by

> the legal system of what those persons may or may not do as the operating units of the legal system. Thus,...incorporation and regulation can be distinguished for purposes of a federal distribution of powers. In other words, there is no legal or philosophical necessity for the division of powers in these two respects to follow the same lines.

If priority were given to incorporation, over function, as a basis for regulation, according to Lederman, at p.347, the result would be "chaos and the end of federalism" as we have it under the 1867 Act.

161. C.N. Transportation, fn.4, S.C.R. 266.

162. Ibid., S.C.R. 267-268. This criterion is borrowed by Justice Dickson from Vapor Canada, fn.26, per Laskin, C.J.C.

163. Idem. As to the second and third criteria: S.C.R. 267.

164. Idem.

165. According to David Walker, Executive Director, Bank of England, fn.149:

> The scale and international integration of capital market business is already beyond the control of national authorities, with the business increasingly footloose and able to migrate if it cannot be based satisfactorily in the favoured location of practitioners. (p.399)

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