MANAGEMENT'S DISCUSSION AND ANALYSIS

DELIVERING ON OUR MANDATE

MD&A

This Management's Discussion and Analysis (MD&A) contains management's interpretation of the OSC's financial performance for the 2018 fiscal year ended March 31, 2018. While the financial statements reflect actual financial results, the MD&A explains these results from management's perspective and sets out the OSC's plans and budget for the year ahead.

This MD&A should be read in conjunction with the OSC's 2018 Financial Statements and related notes. Together, the MD&A and financial statements provide key information about the OSC's performance and ability to meet its objectives.

Important information about this MD&A

- The information in this MD&A is prepared as of June 5, 2018.
- The terms "we", "us", "our" and "OSC" refer to the Ontario Securities Commission.
- This MD&A contains forward-looking information and statements regarding strategies, objectives, expected operations and financial results, which are based on the OSC's current views of future events and financial performance. Key risks and uncertainties are discussed in the Risks and risk management section of this MD&A. However, some risks and uncertainties are beyond the control of the OSC and are difficult to predict. Actual future outcomes may substantially differ from the expectations stated or implied in this MD&A.
- The words "believe", "plan", "intend", "estimate", "expect", "anticipate" and similar expressions, as well as future conditional verbs, such as "will", "should", "would" and "could" often identify forward-looking statements.
- The words "plan" and "budget" are synonymous in this MD&A and are used interchangeably. Both describe the planned budget revenue and expenses for the related fiscal year.
- Unless otherwise specified, references to a year refer to the OSC's fiscal year ended March 31.
- Notes to the financial statements refer to the OSC's 2018 Notes to the Financial Statements.
- All financial information related to 2017 and 2018 has been prepared in accordance with International Financial Reporting Standards (IFRS). For more information, see the notes to the financial statements, in particular, Note 2 *Basis of presentation*, Note 3 *Significant accounting policies* and Note 20 *Accounting pronouncements*.
- Amounts shown in this MD&A are expressed in Canadian dollars, unless otherwise specified.
- Due to rounding, some variances may not reconcile and analysis of components may not sum to the analysis for the grouped components.

About the OSC

A summary of our role, mandate and goals

The Ontario Securities Commission is responsible for regulating the capital markets of Ontario. We are an independent self-funded Crown corporation of the Province of Ontario. Our powers are given to us under the *Securities Act* (Ontario), the *Commodity Futures Act* (Ontario) and certain provisions of the *Business Corporations Act*. We operate independently from the government and are funded by fees charged to market participants. We are accountable to the Ontario Legislature through the Minister of Finance.

We use our rule making and enforcement powers to help safeguard investors, deter misconduct and regulate market participants in Ontario. The OSC oversees the operation of marketplaces, self-regulatory organizations (SROs), clearing agencies, and investor protection funds in Ontario. We work to regulate market participants including: firms and individuals who sell securities and derivatives, firms who provide investment advice in Ontario and public companies.

The OSC operates under the direction of the Commission. The Commission has two related but independent roles. It serves as the Board of Directors of the OSC and it performs a regulatory function, which includes making rules and policies, and adjudicating administrative proceedings.

We are an active member of the Canadian Securities Administrators (CSA), the forum for the 13 securities regulators of Canada's provinces and territories. The CSA works to foster a nationally coordinated and modernized securities regulatory framework.

The OSC also contributes to the international securities regulatory agenda by actively participating in the International Organization of Securities Commissions (IOSCO) and other international organizations.

Mandate

To provide protection to investors from unfair, improper or fraudulent practices, to foster fair and efficient capital markets and confidence in capital markets, and to contribute to the stability of the financial system and the reduction of systemic risk.

Vision

To be an effective and responsive securities regulator – fostering a culture of integrity and compliance and instilling investor confidence in the capital markets.

Goals

1. **Deliver strong investor protection**
2. **Deliver effective compliance, supervision and enforcement**
3. **Deliver responsive regulation**
4. **Promote financial stability through effective oversight**
5. **Be an innovative, accountable and efficient organization**

Capital Markets Regulatory Authority (CMRA)

The OSC plays an important advisory role to the Ontario Ministry of Finance on the project to create the CMRA. The CMRA is an important initiative among the Ontario, British Columbia (BC), Saskatchewan, New Brunswick (NB), Prince Edward Island (PEI), Yukon and Federal governments. The Ministers responsible for capital markets regulation in Ontario, BC, Saskatchewan, NB, PEI and the Yukon published for comment a revised consultation draft of the uniform provincial/territorial Capital Markets Act (CMA), draft initial regulations and related materials in August of 2015. The CMRA, once established, would administer the uniform provincial/territorial CMA and a single set of regulations.

The CMRA's initial board of directors was announced on July 22, 2016. The board selected the initial Chief Regulator of the CMRA on November 17, 2016. On March 22, 2018, the Supreme Court of Canada held a hearing to consider the constitutionality of the proposed initiative and the proposed federal legislation. The Court's decision is expected sometime in 2018.

During 2018, the OSC expended approximately $0.4 million in staff resources, in addition to the $4.4 million expended from 2014 to 2017, for a total of $4.8 million toward the creation of, and transition to, the CMRA. These totals do not include time spent by OSC's Executive who participate on the CMRA Transition Committee and are otherwise involved in the CMRA project.

Operating results

A summary of our financial results and a discussion of our revenue and expenses

As a self-funded Crown corporation, the OSC operates on a cost-recovery basis. The chart below provides a comparison of results over the last two years. At the end of fiscal 2018, the general surplus was $55.8 million, which increased by $15.2 million from the prior year. Total revenues were 4.1% higher than the prior year and total expenses were 2.1% higher than the prior year. Revenues increased mainly from higher participation fees due to market growth. Expenses increased primarily in salaries and benefits due to additional positions hired during the year and depreciation as a result of increased capital expenditures to support information technology initiatives.

The general surplus is projected to decrease as revenues are projected to remain relatively flat over the next few years while critical investments occur to continue providing data driven, risk-focused, evidence-based regulatory oversight. Capital expenditures are also projected to increase to support these strategic initiatives and provide for facility rehabilitation. As a result of these expenditures and the need to maintain an adequate cash safety margin, OSC fees will remain unchanged for a period of two years beginning April 1, 2018.

The OSC's operations and revenue are directly affected by market conditions and trends. Our fee revenue fluctuates with market activity.

(Thousands)	2018	2017
Revenue	$ 124,819	$ 119,927
Expenses	112,381	110,082
Excess of revenue over expenses (before recoveries)	**12,438**	**9,845**
Recoveries of enforcement costs	854	160
Recoveries of investor education costs	1,475	1,471
Recoveries from insurance proceeds over loss on asset disposal	521	—
Excess of revenue over expenses	**$ 15,288**	**$ 11,476**
General surplus	$ 55,787	$ 40,613
Property, plant and equipment (purchases)	$ 3,384	$ 2,743
Total assets	**$ 276,319**	**$ 254,052**
Non-current liabilities	**$ 184,025**	**$ 176,722**

Total assets increased from 2017 to 2018 primarily as a result of an increase in the following:

- Cash, as a result of Excess of revenue over expenses, ($16.6 million)
- Funds held pursuant to designated settlements and orders, as a result of orders assessed and that have either been paid or deemed to be receivable ($4.1 million), and
- Funds restricted for CSA Systems operations and redevelopement, as a result of Excess of revenues over expenses relating to CSA national system activities ($2.9 million). During the year, the OSC changed the application of its accounting policy for CSA Systems from the recognition of *"Net assets held for CSA Systems operations and redevelopment"* to *"Funds restricted for CSA Systems operations and redevelopment"*. Accordingly, the total balance reflected in the Statement of Financial Position as Non-current asset and an equal offsetting Non-current liability in 2017 has been restated to reduce the balance by $16.8 million to reflect cash and investments rather than net assets. For more information on Funds restricted for CSA Systems operations and redevelopment, see Note 2(d) and Note 17.

Non-current liabilities increased from 2017 to 2018 primarily as a result of an increase in the offsetting liability corresponding to designated settlements and orders and CSA Systems operations and redevelopment, as described above.

About our fees

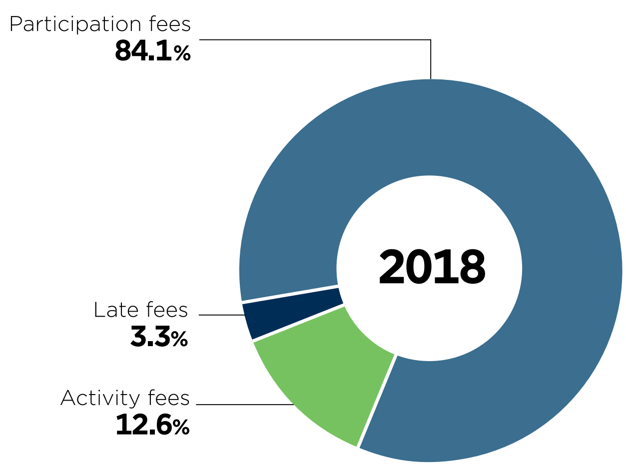
The OSC is funded by fees from market participants. We charge two types of regulatory fees: participation fees and activity fees. Our fee structure is designed to recover costs and is set out in OSC Rules 13-502 Fees and 13-503 *(Commodity Futures Exchange) Fees*. The current fee rule will remain in place for a further two years until March 31, 2020.

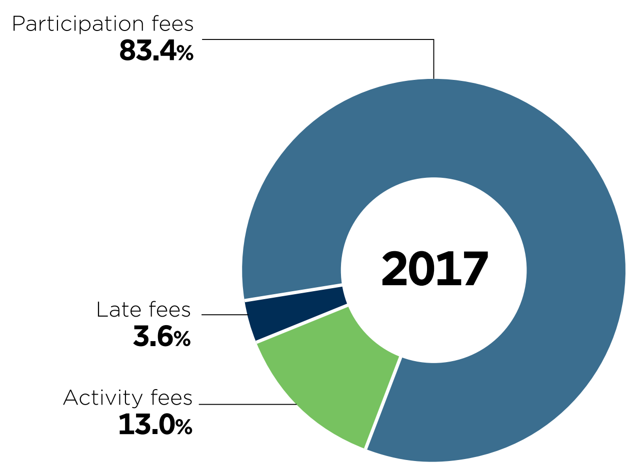
- **Participation fees** are charged for a participant's use of Ontario's capital markets. They cover the cost of a broad range of regulatory services that cannot be practically or easily attributed to individual activities of market participants. Fees are calculated using an increasing tiered structure based on average market capitalization for issuers and revenues for registrants. Specified regulated entities are charged participation fees based on their market share or a fixed rate. The basis for calculating participation fees is on a market participants' most recent fiscal year. The timing of participation fee revenue affects our cash flow. For more information, see the Liquidity and financial position section.
- **Activity fees** are charged when market participants file documents, such as prospectuses and other disclosure documents, registration applications and applications for discretionary relief, and are set to reflect the costs associated with providing the related services. Activity fees are also charged for requests, such as making changes to a registration or searching for records. Activity fees are flat-rate fees based on the estimated direct cost for the OSC to review documents and respond to requests.
- **Late fees** are charged when market participants submit filings after applicable filing deadlines, and/or are late paying the fees related to a filing.

Revenue

Total revenues of $124.8 million were up $4.9 million (4.1%) from 2017. Total revenues for the year exceeded plan by $9.0 million (7.8%), mainly due to higher participation and activity fees. Participation fees account for 55.4% of the variance against plan, activity fees account for 26.7%, and miscellaneous revenue and interest income together account for the remaining 17.9%.

(Thousands)	% of 2018 Revenue	2018	2017	Change	% Change
				Favourable / (Unfavourable)	
Participation fees	84.1%	$ 104,502	$ 99,726	$ 4,776	4.8%
Activity fees	12.6%	15,648	15,471	177	1.1%
Late fees	3.3%	4,080	4,319	(239)	-5.5%
Total fees	**100.0%**	**$ 124,230**	**$ 119,516**	**$ 4,714**	**3.9%**
Miscellaneous		77	168	(91)	-54.2%
Interest income		512	243	269	110.7%
Total revenues		**$ 124,819**	**$ 119,927**	**$ 4,892**	**4.1%**





The following is a discussion of the significant changes in Revenue components.

Participation fees

Variance from prior year: Total participation fee revenues were $4.8 million (4.8%) higher in 2018 compared to 2017 as a result of market growth, mainly from registrants.

Variance from current year plan: Participation fee revenues were $5.0 million (5.0%) higher than the 2018 plan. Registrant participation fees were $5.8 million (9.3%) higher than plan due to increased registrant income which drives higher fees. Issuer participation fees were $0.8 million (2.0%) under plan, as the expected growth across fee tiers assumed in the budget did not materialize in the actual results.

2019 plan: The 2019 plan for participation fees totals $102.5 million: $36.3 million from issuers, $64.7 million from registrants and $1.5 million from marketplaces and other entities. This represents a $2.0 million (1.9%) decrease from 2018 actual results and a $3.0 million (3.0%) increase from the 2018 plan. The plan is lower than 2018 actual results as capital market growth assumptions are lower in 2019.

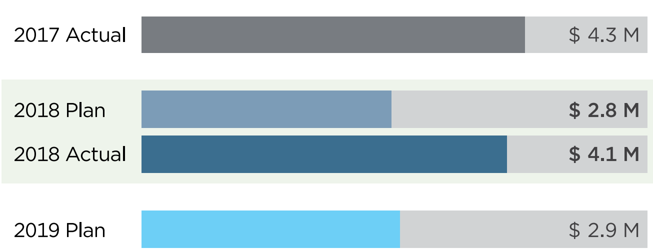
Activity fees

Variance from prior year: Activity fee revenues were $0.1 million (1.1%) higher this year than the prior year, primarily due to higher prospectus filings from investment funds.

Variance from current year plan: Activity fee revenues were $2.4 million (18.2%) above plan for the current year. The main reason for the increase is due to a higher volume of prospectus filings from investment funds and exemptive relief applications.

2019 plan: The 2019 plan for activity fees totals $14.1 million, representing a $1.5 million (9.6%) decrease from the 2018 actual results and a $0.9 million (6.8%) increase from the 2018 plan. The lower budget expresses uncertainty on the level of issuer and registrant activity fees and is considered prudent.

Late fees



Variance from prior year: Late fee revenues were $0.2 million (5.5%) lower than the prior year primarily as a result of a lower volume of late filings of registrant documents.

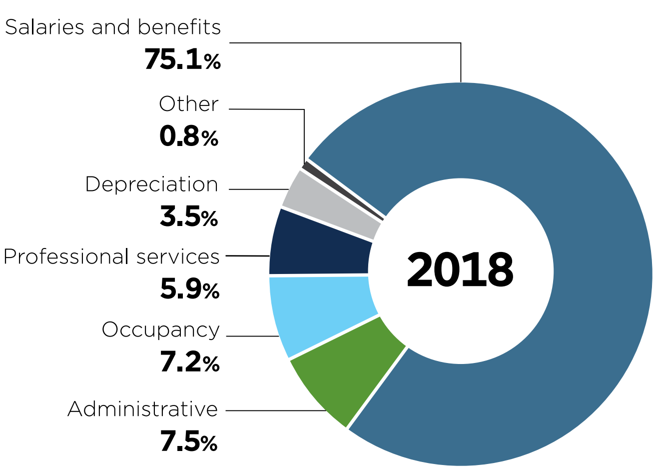
Variance from current year plan: Late fee revenues were $1.3 million (46.4%) higher than plan for the current year. This is primarily due to higher late exempt distribution filings.

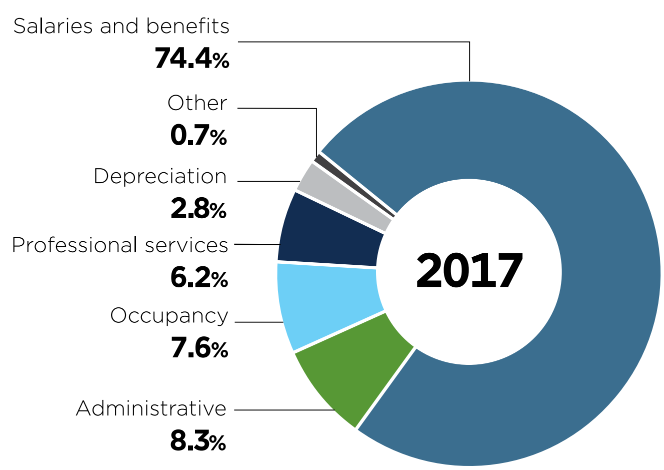
2019 plan: The 2019 plan for late fees totals $2.9 million. This represents a $1.2 million (29.3%) decrease from the 2018 actual results and a $0.1 million (3.6%) increase from the 2018 plan. This is lower than the 2018 actual revenue due to the uncertainty of late filing volumes.

Expenses

In 2018, our total expenses were $112.4 million, up $2.3 million (2.1%) from $110.1 million in 2017 (excluding Recoveries). The year-over-year increase is mainly attributable to higher Salaries and benefits costs as a result of additional positions hired in priority areas and higher Depreciation from capitalized technology purchases during the year. These increases are partially offset by underspending in Administrative costs due to lower data subscriptions and information technology maintenance requirements. Other areas of underspending include Occupancy and Professional services.

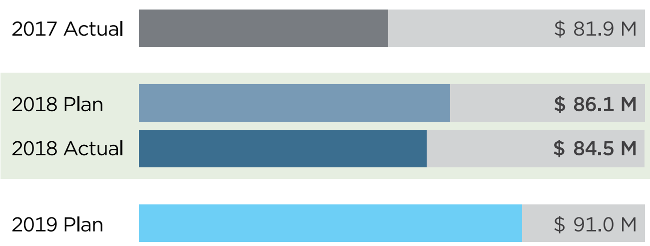
(Thousands)	% of 2018 Expenses	2018	2017	Change	% Change
				Favourable / (Unfavourable)	
Salaries and benefits	75.1%	$ 84,476	$ 81,864	$ (2,612)	-3.2%
Administrative	7.5%	8,448	9,085	637	7.0%
Occupancy	7.2%	8,083	8,353	270	3.2%
Professional services	5.9%	6,584	6,863	279	4.1%
Depreciation	3.5%	3,907	3,112	(795)	-25.5%
Other	0.8%	883	805	(78)	-9.7%
	100%	**$ 112,381**	**$ 110,082**	**$ (2,299)**	**-2.1%**
Recoveries of enforcement costs		(854)	(160)	694	433.8%
Recoveries of investor education costs		(1,475)	(1,471)	4	0.3%
Recoveries from insurance proceeds over loss on asset disposal		(521)	—	521	100.0%
Total expenses (net of recoveries)		**$ 109,531**	**$ 108,451**	**$ (1,080)**	**-1.0%**





The following is a discussion of the significant changes in Expense components.

Salaries and benefits



For details on the composition of the Salaries and benefits expenses incurred, see Note 15 of the financial statements.

Variance from prior year: Salaries and benefits were $2.6 million (3.2%) higher this year than the prior year. This was a result of an increase in the average number of positions and salary increases implemented at the beginning of the year. For the 2018 fiscal year, the OSC added seven permanent new positions for priority areas within the OSC.

Variance from current year plan: Salaries and benefits were $1.6 million (1.9%) lower than plan for the current year. This was mainly due to delays in filling vacant positions.

2019 plan: The 2019 plan for Salaries and benefits totals $91.0 million. This represents a $6.5 million (7.7%) increase from the current year actual results and a $4.9 million (5.7%) increase from the 2018 plan. The increase reflects the full year cost of 2018 staff additions and new additions in 2019 to support key initiatives including the data management program and emerging regulatory issues such as Fintech and cryptocurrencies.

Administrative

For details on the composition of Administrative expenses incurred, see Note 16 of the financial statements.

Variance from prior year: Administrative expenses were $0.7 million (7.0%) lower this year than the prior year. This was a result of a decrease in spending on data subscriptions, lower information technology maintenance as a result of deferred projects and lower commission expenses due to a lower number of hearings.

Variance from current year plan: Administrative expenses were $2.9 million (25.7%) lower than plan for the current year. This was primarily the result of lower spending on data subscriptions and information technology maintenance services.

2019 plan: The 2019 plan for Administrative expenses totals $12.1 million. This represents a $3.7 million (44.0%) increase from 2018 actual results and a $0.8 million (7.1%) increase from the 2018 plan. This is mainly due to additional maintenance costs for new information technology initiatives, including some costs deferred from 2018. The initiatives being deferred to 2019 are mainly due to flooding incidences during the year that resulted in a reprioritization of initiatives.

Occupancy

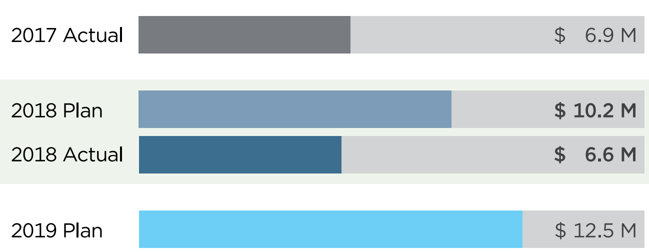
Variance from prior year: Occupancy expenses were $0.3 million (3.2%) lower this year than the prior year as a result of a general decrease in base rent and rent charges relating to property taxes.

Variance from current year plan: Occupancy expenses were consistent with the plan of $8.1 million.

2019 plan: The 2019 plan for Occupancy expenses totals $8.1 million. Occupancy expenses are expected to remain relatively flat due to the new lease effective September 1, 2017. The term is for 10 years ending August 31, 2027 and contains two consecutive options to extend the term for a period of 5 years each. The lease was approved by the Minister of Finance under the *Financial Administration Act* section 28. The OSC's lease commitments are outlined in Note 11 of the financial statements.

During 2018, the OSC continued leasing space to the CSA IT Systems Office and the Government of Canada on a cost recovery basis through a sublease agreement, including all renovation and lease costs. The amount of lease costs spent and subsequently recovered from these organizations in 2018 is $0.8 million ($0.8 million in 2017).

Professional services



Variance from prior year: Professional services expenses were $0.3 million (4.1%) lower this year than the prior year. This was mainly due to underspending on information technology projects which have been deferred to the following year as a result of the flooding incidences.

Variance from current year plan: Professional services expenses were $3.6 million (35.3%) lower than plan for the current year. This is due to underspending on information technology projects which have been deferred to the following year and lower enforcement related professional services.

2019 plan: The 2019 plan for Professional services expenses totals $12.5 million. This represents a $5.9 million (89.4%) increase from the current year actual results and a $2.3 million (22.5%) increase from the 2018 plan. This is mainly due to higher planned spending on information technology projects.

Depreciation

Variance from prior year: Depreciation expense was $0.8 million (25.5%) higher than the prior year due to capital asset additions as a result of flooding during the year that damaged technological equipment.

Variance from current year plan: Depreciation expense was $0.4 million (11.4%) higher than plan for the current year due to higher capital purchases as a result of flooding.

2019 plan: The 2019 plan for Depreciation expense totals $4.5 million. This represents a $0.6 million (15.4%) increase from the current year actual results and a $1.0 million (28.6%) increase from the 2018 plan. This is mainly due to an increase in capital expenditures towards information technology projects and facility rehabilitation.

CSA shared costs

CSA shared costs incurred by the OSC are included in Professional services expenses. As a member of the CSA, the OSC pays a portion of the costs to operate the CSA's office and joint CSA projects. In 2018, total CSA spending on shared projects was $1.9 million ($1.9 million in 2017). The OSC contributed $0.7 million ($0.8 million in 2017). CSA shared costs incurred by the OSC are included in Professional services expenses.

CSA project costs are allocated to each CSA member based on the population of its jurisdiction as a percentage of all participating jurisdictions. The OSC's percentage is 38.6% (38.5% in 2017). All CSA projects, including developing harmonized securities policies and rules, are coordinated through a central secretariat. In 2018, the OSC contributed $0.5 million ($0.4 million in 2017) to support the CSA Secretariat.

Recovery of investor education costs

During the year, the OSC recorded $1.5 million in Recoveries of investor education costs from Funds held pursuant to designated settlements and orders. These recoveries are reviewed by the Audit and Finance Committee and are approved quarterly.

Subparagraph 3.4(2)(b)(ii) of the *Securities Act* (Ontario) states that enforcement monies may be designated "for use by the Commission for the purpose of educating investors or promoting or otherwise enhancing knowledge and information of persons regarding the operation of the securities and financial markets."

Liquidity and financial position

A discussion of our liquidity, cash flows, financing activities and changes in our financial position

Liquidity

Cash

At March 31, 2018, the OSC held $58.9 million in Cash ($42.3 million in 2017) and $20.0 million in Reserve fund assets ($20.0 million in 2017), for a combined total of cash and cash equivalent resources available of $78.9 million ($62.3 million in 2017).

We hold enough Cash, Reserve fund assets and credit access to ensure liquidity for our forecast cash requirements.

At March 31, 2018, the OSC had current assets of $65.0 million ($48.7 million in 2017) and current liabilities of $16.5 million ($16.7 million in 2017) for a current ratio of 3.9:1 (2.9:1 in 2017). The higher current ratio is mainly due to the increase in our Cash balance as described below.

The OSC uses multi-year forward-looking operational forecasts to anticipate potential future cash requirements. In 2018, the OSC did not draw on the line of credit, however $17.0 million of the reserve fund was used and replenished.

The OSC's Cash position increased $16.6 million (39.2%) from 2017 as a result of an operational surplus in 2018 adjusted by investments in property plant and equipment. In 2018, Excess of revenue over expenses was $15.3 million ($11.5 million in 2017), and the year-end surplus was $55.8 million ($40.6 million in 2017).

Cash flows

In 2018, Cash flows from operating activities produced an inflow of $18.8 million ($14.4 million in 2017). In 2018, the OSC paid $2.2 million ($1.3 million in 2017) towards Property, plant & equipment investments.

Approximately 75% of our revenues are received in the last quarter of each fiscal year, while expenses are incurred relatively evenly over the fiscal year. This timing difference typically results in negative cash balances from the second quarter to the beginning of the fourth quarter of each fiscal year. The OSC currently has two key tools to manage temporary negative cash positions: a $20.0 million general operating reserve and a $52.0 million revolving line of credit, both as approved by the Minister of Finance.

In 2018, we used $17.0 million in Reserve fund assets and $0 ($75 thousand in 2017) of our revolving line of credit to fund operations. We restored the $20.0 million in Reserve fund assets in early January 2018 when most registrant participation fees were received.

The agreement for the current line of credit expires on June 30, 2018. The OSC received approval from the Minister of Finance to renew the line of credit for an additional two years, up to the same maximum of $52.0 million as the current line of credit.

Financial instruments

The OSC uses Cash and Reserve fund assets to manage its operations. Both are recorded at fair value. See Note 3(a) of the financial statements for the OSC's accounting policies related to financial instruments.

The OSC acts as a custodian of Funds held pursuant to designated settlements and orders, and Funds restricted for CSA Systems operations and redevelopment. Both are recorded at fair value. Funds restricted for CSA Systems operations and redevelopment includes investments of $115.3 million. The OSC is not exposed to significant interest rate, currency or liquidity risks from these investments because they are short-term in nature, redeemable and all balances are denominated in Canadian dollars. For a complete analysis of the risks relating to these financial instruments, see Note 4 of the financial statements.

Trade and other receivables, Trade and other payables and accrued liabilities are recorded at amortized cost, which approximates fair value given their short-term maturities. For more information on Trade and other receivables, see Note 5 of the financial statements. For more information on Trade and other payables (including accrued liabilities), see Note 10 of the financial statements.

The OSC is not exposed to significant interest rate, currency or liquidity risks.

Financial position

The following is a discussion of the significant changes in our Statement of Financial Position.

Trade and other receivables

Trade and other receivables were $3.7 million ($4.8 million in 2017). The decrease of 22.9% was primarily due to a reduction in revenue accruals, HST recoverable and amounts owing from the CSA.

For more information on Trade and other receivables, see Note 4 and Note 5 of the financial statements.

Prepayments

Prepayments totaled $2.4 million ($1.5 million in 2017). The increase is primarily due to Occupancy costs which were paid in advance for one month.

Funds held pursuant to designated settlements and orders

The Commission may impose monetary sanctions for breaches of Ontario securities law. The sanctions reflect what the Commission believes is appropriate for the circumstances, regardless of a respondent's ability to pay. This practice is intended to deter others from contravening the *Securities Act* (Ontario).

The OSC may designate funds under settlement agreements and orders from enforcement proceedings to be allocated as the Board of the OSC determines. This includes allocating money to harmed investors, where an allocation can be reasonably made, and for investor education. Funds not designated when settlements are approved or when orders are made must be paid to the Consolidated Revenue Fund of the Government of Ontario.

In 2018, $60.4 million in orders was assessed ($164.0 million in 2017). Included in the $60.4 million in orders assessed by the OSC are five orders for which the respondents were required to make payment directly to harmed investors, totaling $48.4 million ($148.1 million in 2017). While this amount is considered for our enforcement sanctions statistics, it does not form part of the Funds held pursuant to designated settlements and orders balance as the amounts owing are paid from respondents to investors directly and not by the OSC. The OSC recorded $6.1 million of orders in Funds held pursuant to designated settlements and orders ($7.9 million in 2017).

As authorized by its Board, the OSC distributed $1.1 million ($3.1 million in 2017) to harmed investors and $1.8 million ($1.4 million in 2017) to the OSC for the recovery of investor education costs.

In 2014, the Board authorized a payment of $2.0 million to the Canadian Foundation for the Advancement of Investor Rights (FAIR Canada). In 2017, the OSC concluded an agreement with FAIR Canada that allows FAIR to draw from the OSC's endowment contribution to cover operating expenses up to $0.5 million per year.

On July 14, 2016, the OSC established the Whistleblower Program (the "Program"). Under the Program, whistleblowers may be eligible for awards of between 5% to 15% of total monetary sanctions imposed and/or voluntary payments made, if their information leads to an administrative proceeding where these amounts total $1 million or more. The maximum amount of the award has been set at $1.5 million where monetary sanctions and/or voluntary payments are not collected and $5 million where these amounts have been collected. Whistleblowers will be paid out of Funds held pursuant to designated settlements and orders.

At March 31, 2018, the accumulated balance of designated funds was $42.1 million ($38.0 million in 2017). Of this amount, $40.9 million was held in cash ($36.5 million in 2017) and $1.2 million was deemed as being receivable ($1.5 million in 2017). After considering funds set aside for possible allocation to harmed investors, $31.6 million ($14.3 million in 2017) of the funds on hand is available for distribution. The increase in funds on hand for distribution in 2018 is mainly due to funds pending approval for distribution in 2017 which were approved in 2018.

For more information on Funds held pursuant to designated settlements and orders, see Note 6 of the financial statements.

Collecting monetary sanctions

While the OSC actively works to collect outstanding sanction amounts, material differences between sanction assessments and collections have persisted since we began imposing monetary sanctions. Historically, collection rates from market participants have been much higher than from respondents sanctioned on matters related to fraud – where assets are typically non-existent or inaccessible. Collections of monetary sanctions remain fairly consistent with the prior year.

Total settlements and orders assessed during the year amounted to $60.4 million ($164.0 million in 2017) of which $48.4 million ($148.1 million in 2017) were paid or payable directly to investors.

We continue to look for ways to improve our collections rates, including reviewing the experiences of other public and private sector organizations to identify methods that can be used by the OSC. We actively pursue collections using internal and external resources. In fiscal 2018, an external collections firm was retained under a contingency arrangement to provide debt collection legal services to collect unpaid monetary sanctions.

A list of respondents who are delinquent in paying monetary sanctions to the Commission is available on the OSC website at **www.osc.ca**.

The table below shows the collection rates on sanction amounts for the last two years.

Fund held pursuant to designated settlements and orders

(Thousands)

2017	**Assessed***	**Collected**	**% Collected**
Settlements	$ 7,890	$ 7,856	99.6%
Contested hearings**	8,009	50	0.6%
Total	**$ 15,899**	**$ 7,906**	**49.7%**
2018	**Assessed***	**Collected**	**% Collected**
Settlements	$ 6,086	$ 5,681	93.3%
Contested hearings	5,967	—	0.0%
Total	**$ 12,053**	**$ 5,681**	**47.1%**

* Does not reflect amounts paid directly by respondents to investors.

** During 2018, the 2017 assessed contested hearings balance was reduced by $4.8 million as the respondent fulfilled their obligation by paying investors directly. This has resulted in a revised collection rate for 2017.

Reserve fund assets

Since 2001, the OSC has held $20.0 million in Reserve fund assets, as approved by the then Minister of Finance, to guard against revenue shortfalls or unexpected expenses, or to cover discrepancies between timing of revenue and expenses. Our primary investment consideration is protection of capital and liquidity. The OSC records Interest income generated by the Reserve fund assets with general operations. The Reserve fund assets are segregated as a Reserve operating surplus to reflect their restricted use.

For more information on Reserve fund assets, see Note 8 of the financial statements.

Property, plant & equipment

Property, plant & equipment decreased 8.8% to $11.4 million ($12.5 million in 2017). The decrease is the result of higher depreciation on assets compared to purchases during the year.

For more information on Property, plant & equipment, see Note 9 of the financial statements.

Trade and other payables

Trade and other payables decreased 1.2% to $16.5 million ($16.7 million in 2017). The decrease is due to the timing of vendor payments.

For more information on Trade and other payables, see Note 10 of the financial statements.

Pension liabilities

Pension liabilities of $4.1 million ($3.8 million in 2017) represents future defined benefit obligations for supplemental pension plans for present and past Chairs and Vice-Chairs. The OSC's related expenses for the year were $0.4 million ($0.4 million in 2017).

For more information on the supplementary pension plan and related defined benefit obligation, see Note 12(b) of the financial statements.

Funds restricted for CSA Systems operations and redevelopment

The core CSA National Systems (CSA Systems) are hosted and operated by CGI Information Systems and Management Consultants Inc. (CGI). The CSA Systems include the System for Electronic Document Analysis and Retrieval (SEDAR), System for Electronic Disclosure by Insiders (SEDI) and the National Registration Database (NRD). The CSA is redeveloping the CSA Systems and is planning to develop and implement a new marketplace surveillance and analytical system to improve market analytics capacity. Market participants are required to use the CSA Systems to file regulatory documents, such as prospectuses and other disclosure documents, report trades by insiders, file registration information and submit fee payments.

The OSC, Alberta Securities Commission, British Columbia Securities Commission and l'Autorité des marchés financiers are principal administrators (PAs) of the CSA Systems. The OSC has been appointed the Designated Principal Administrator – Operations (DPA). As DPA, the OSC oversees the custody and financial management of the system fees collected relating to CSA Systems used by market participants. The CSA IT Systems Project Office, which is housed at the OSC, manages the CSA Systems business relationships with third-party technology providers.

The funds included in Net assets held for CSA Systems redevelopment may be used to fund the operations of the CSA Systems, enhance the systems, reduce systems fees, offset shortfalls in system fee revenue related to operation of SEDAR, SEDI and NRD, and fund the operations of the DPA and the CSA IT Systems Project Office.

In June 2016, the PAs signed an agreement with CGI to replace the core CSA National Systems with one system to support existing and future requirements for the benefit of market participants. Services in the scope of the agreement include software acquisition, application development, systems integration and application support. Redevelopment began in a multi-year phased approach beginning in fiscal 2017. The PAs have certain rights to terminate the agreement, with and without cause, as set out in the agreement.

For more information on CSA National Systems contractual arrangements and financial results, see Note 7 and Note 17(a) of the financial statements.

During the year, the OSC changed the application of its accounting policy for CSA Systems from the recognition of *"Net assets held for CSA Systems operations and redevelopment"* to *"Funds restricted for CSA Systems operations and redevelopment".* This change was made to provide users of OSC's financial statements with more relevant information as it recognizes only the elements for which the OSC holds and manages for CSA Systems (cash and investment and a corresponding liability for those elements). Although the use of the CSA Systems surplus funds is governed by the four PAs, each having one vote on CSA Systems matters, the OSC's role is essentially that of custodian over these funds. Accordingly, the total balance reflected in the Statement of financial position as Non-current asset and an equal offsetting Non-current liability is cash and investments of the CSA Systems of $137.8 million ($134.9 million in 2017) rather than total net assets. Comparative balances have been adjusted from $151.7 million in 2017 to $134.9 million to reflect this change.

For more information on the judgment exercised with respect to the appropriate accounting treatment of these surplus funds, see Note 2(d) of the financial statements.

2019 Strategy

Our plans and budget for fiscal year 2019

Statement of Priorities

Every year, the OSC publishes a Statement of Priorities for the current fiscal year. It sets out the specific areas we will focus on to fulfil our mandate. The public has an opportunity to comment on the draft document before the Statement of Priorities is published and delivered to the Minister of Finance.

The Statement of Priorities is our cornerstone accountability document.

On March 29, 2018, the OSC published its 2019 OSC Draft Statement of Priorities – Request for Comments. The draft Statement of Priorities was open for public comment until May 28, 2018 and is available on the OSC website at **www.osc.ca**. The final Statement of Priorities will be published on the OSC website in July 2018.

2019 Budget approach

Our regulatory framework needs to remain current and responsive to the continuing evolution of market structures and products and be supportive of capital formation in Ontario. The OSC must carefully balance the desire to improve access to capital with the need to retain appropriate investor protections. The 2019 Statement of Priorities sets out the OSC's key priorities to meet these challenges.

Achieving these priorities is a key driver of the proposed increases to the 2019 OSC Budget over 2018 as this will require focused investments in the following areas:

Deliver strong investor protection

- Publish regulatory reforms that address the best interests of the client – (Client Focused Reforms)
- Publish regulatory actions needed to address embedded commissions
- Advance retail investor protection, engagement and education through the OSC's Investor Office

Deliver effective compliance, supervision and enforcement

- Protect investors and foster confidence in our markets by upholding strong standards of compliance with our regulatory framework
- Increase deterrent impact of OSC enforcement actions and sanctions by actively pursuing timely and consequential enforcement cases involving serious securities laws violations

Deliver responsive regulation

- Work with fintech businesses to support innovation and capital formation through regulatory compliance
- Implement the orderly transfer of syndicated mortgage investments to OSC oversight
- Address opportunities to reduce regulatory burden while maintaining appropriate investor protections
- Review the effectiveness of the disclosure requirements regarding women on boards and in executive officer positions (WOB) to determine if there is a need for further action
- Actively monitor and assess impacts of recently implemented regulatory initiatives

Promote financial stability through effective oversight

- Enhance OSC systemic risk oversight
- Promote cybersecurity resilience through greater collaboration with market participants and other regulators on risk preparedness and responsiveness

Be an innovative, accountable and efficient organization

- Develop a strategic OSC workforce approach focused on skills recruitment and development
- Enhance OSC business capabilities
- Work with Capital Markets Regulatory Authority (CMRA) partners on the transition of the OSC to the proposed CMRA

As a result, the budget reflects an increase in expenses of 7.9% from the 2018 budget and 15.9% from 2018 spending. The key reasons for this increase are:

- Approval of new positions to support the investments noted above,
- Professional services to support key technology initiatives to modernize enforcement, case management and other technological tools, and
- Enhance OSC collection efforts of uncollected monetary sanctions owing from respondents.

The budget also includes resources for work toward the implementation of the CMRA.

As the complexity of the capital markets environment increases, multi-year investments in data and information systems are necessary to continue providing data driven, risk-focused, evidence-based regulatory oversight. Accordingly, the capital budget has increased compared to 2018 spending, reflecting costs towards a significant data management program initiative and technology infrastructure replacements. Capital funding is also required to support facilities rehabilitation within the existing OSC premises.

2019 Plan

	2017–2018	2017–2018	2018–2019	2018–19 Budget to 2017–18 Budget		2018–19 Budget to 2017–18 Actual	
(Thousands)	**Budget**	**Actual**	**Budget**	**$ Change**	**% Change**	**$ Change**	**% Change**
				Favourable/(Unfavourable)		Favourable/(Unfavourable)	
Revenues	$ 115,781	$ 124,819	$ 119,990	$ 4,209	3.6%	$ (4,829)	-3.9%
Expenses	117,657	109,531	126,916	(9,259)	-7.9%	(17,385)	-15.9%
Excess (deficiency) revenue over expenses	**$ (1,876)**	**$ 15,288**	**$ (6,926)**	**$ (5,050)**		**$ (22,214)**	
Capital Expenditures	**$ 2,735**	**$ 3,384**	**$ 9,948**	**$ (7,213)**		**$ (6,564)**	

For more information on the 2019 planned budget amounts for significant revenue and expense line items, see the Revenue and Expenses sections of this MD&A.

Critical accounting estimates

Judgments, estimates and assumptions related to preparing IFRS financial statements

Preparing financial statements consistent with IFRS requires that management makes judgments, estimates and assumptions that affect reported amounts of assets and liabilities for the date of the financial statements, as well as reported amounts of the revenues and expenses for the periods.

These judgments, estimates and assumptions are considered "critical" if:

- They require assumptions about highly uncertain matters when made, or
- We could reasonably have used different judgments, estimates or assumptions in the period, or
- Related changes are likely to occur between periods that would materially affect our financial condition, changes in our financial condition or results of our operations.

Judgment was used to determine the appropriate accounting treatment for the Recoveries of investor education costs and Funds restricted for CSA Systems operations and redevelopment.

Sources of estimation uncertainty primarily consisted of the supplemental pension plan defined benefit obligation pension liabilities, Funds held pursuant to designated settlements and orders, and Recoveries of enforcement costs.

For more information on judgments and sources of estimation uncertainty that impact the OSC, see Note 2(d) of the financial statements.

Risks and risk management

Risks and uncertainties facing us, and how we manage these risks

Risk can relate to threats to the OSC's strategy or operations, or failure to take advantage of opportunities. The OSC seeks to fully address or mitigate the strategic and business risks that are most likely to impair achievement of our mandate.

Strategic risks

The OSC applies International Risk Management Standard ISO 31000 to its enterprise risk management. We do this through a Risk Management Framework, which we adopted in November 2012. The goal of the framework is to embed risk management at key strategic decision points, within all elements of our operations and through all levels of staff. The framework sets out a process for identifying and assessing risks, and highlighting and reviewing controls.

Enterprise Risk Inventory

Information gathered through the risk management process is captured in the OSC's Enterprise Risk Inventory. It includes a "top-down" and "bottom-up" view of the risks and controls within the OSC. The top-down portion describes the environment in which the OSC works, while the bottom-up portion deals with day-to-day operational risks that affect our ability to do our work.

The OSC's Risk Committee reviews the Enterprise Risk Inventory each quarter to identify significant changes in the OSC's risk profile, including any new or emerging risks. This information is reported to Senior Management, the Audit and Finance Committee, and the Board of Directors.

Business risks

The OSC has established policies and processes to identify, manage and control operational and business risks that may impact our financial position and our ability to carry out regular operations. Management is responsible for ongoing control and reduction of operational risk by ensuring that appropriate procedures, internal controls and processes, other necessary actions and compliance measures are undertaken.

Operational risk can include risk to the OSC's reputation. Reputational risk, as it relates to financial management, is primarily addressed through the OSC's Code of Conduct and governance practices established by its Board of Directors (details available at **www.osc.ca**), as well as other specific risk management programs, policies, procedures and training.

Internal audit

OSC Internal Audit is an assurance and advisory service to the Board of Directors and to management. Internal Audit helps the OSC develop, evaluate and improve risk management practices, risk-based internal controls, good governance and sound business practices.

The internal audit function is governed by a Charter approved by the OSC's Board of Directors and by an annual internal audit plan that is also approved by the Board. The Chief Internal Auditor reports the results of internal audits to the Audit and Finance Committee and provides an annual summary of key internal audit findings to the Board of Directors.

Systems risk
The OSC's Information Services group regularly monitors and reviews the OSC's systems and infrastructure to maintain optimal operation. The OSC also performs extensive security and vulnerability assessments annually to highlight potential areas of risk. All findings and key recommendations from these assessments are tracked along with a management response and target remediation date. The results of these assessments and the progress made to address these findings and recommendations are reported to the Audit and Finance Committee and are used to improve security of the OSC systems.

The OSC relies on CSA Systems, which are operated by CGI, to collect most of its fee revenue. The CSA requires CGI to provide an annual third-party audit report (CSAE 3416 – Type II) that reviews and evaluates the internal controls design and effectiveness of the CSA Systems and CGI's outsourcing operations. CGI is also required to have an operating disaster recovery site for operating these systems and to test it annually. The most recent test was performed in March 2018.

The OSC could be contingently liable for claims against, or costs related to, CSA Systems operations. See Note 17 of the financial statements for more information. No material change is expected in the volume of fees collected through these systems.

Business continuity
The OSC has a detailed Business Continuity Plan (BCP) to ensure critical regulatory services can continue if an external disruption occurs. The BCP is continually reviewed and refined, and includes strategies to effectively address various market disruption scenarios.

Financial risk
The OSC maintains strong internal controls, including management oversight, to provide reasonable assurance of financial reporting reliability and preparation of financial statements for external purposes consistent with IFRS. These controls are tested annually through our internal control over financial reporting (ICFR) program.

For fiscal years ending March 31, 2017, 2018 and 2019, we require participants to use their most recent fiscal year as the basis for calculating their participation fees. As a result, actual revenues received may be different than plan, but are not expected to impair our operations.

Legal risk
Occasionally, the OSC is involved in legal actions arising from the ordinary course of business. Settlements from these actions are accounted for when they occur. The outcome and ultimate disposition of these actions cannot currently be determined. However, management does not expect the outcome of any legal actions, individually or in aggregate, to have a material impact on the OSC's financial position.

Internal control over financial reporting (ICFR)

A summary of our ICFR program results

During the year, the OSC's ICFR processes were reviewed and documentation updated where necessary. Operating effectiveness was tested using the framework and criteria established in "Internal Control – Integrated Framework (2013 version)" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Staff performed an evaluation, under the supervision and with the participation of management, of the effectiveness of the OSC's ICFR as at March 31, 2018. Based on this evaluation, the OSC has concluded that the ICFR was operating effectively and that there are no material weaknesses.

There have been no significant changes in controls that occurred during the most recent year ended March 31, 2018, that have materially affected, or are reasonably likely to materially affect, the OSC's ICFR. The Chair and the Director, Financial Management & Reporting, certify the design and effectiveness of ICFR in the Statement of Management's Responsibility and Certification.