ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

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To the Council of Ministers

Dear Sirs/Mesdames:

The Canadian Bankers Association (**CBA**) works on behalf of 60 domestic banks, foreign bank subsidiaries and foreign bank branches operating in Canada and their 280,000 employees. The CBA advocates for effective public policies that contribute to a sound, successful banking system that benefits Canadians and Canada's economy.

On August 25th, 2015, the provincial and territorial Ministers responsible for securities regulation in British Columbia, Ontario, Saskatchewan, New Brunswick, Prince Edward Island and the Yukon (the **Participating Jurisdictions**) issued a revised consultation draft of a provincial/ territorial *Capital Markets Act* (the **CMA**) along with draft initial regulations under the CMA (the **Initial Regulations** and, together with the CMA, the **Proposed Provincial Legislation**). The consultation draft of the CMA was initially published for comment in September 2014 along with the proposed federal *Capital Markets Stability Act* (the **CMSA**) which, together, create the legislative framework (the **Framework**) that underpins the Capital Markets Regulatory Authority (the **CMRA**).

GUIDING PRINCIPLES AND OBJECTIVES

As the CBA has noted previously to the Participating Jurisdictions, the banking industry has always been supportive of initiatives intended to unify and rationalize capital markets regulation across Canada. Our support for a harmonized approach is premised on the understanding that the result is to attain a more efficient and effective regulatory framework for the capital markets in Canada. The stated purpose of the Cooperative Capital Markets Regulatory System (the **CCMRS**) includes fostering more efficient and globally competitive capital markets in Canada, facilitating the raising of capital from Canadian and foreign investors through more integrated markets governed by innovative, responsive and flexible regulation and providing increased protection for investors. Section 1 of the CMA indicates its purposes as, in part, providing "protection to investors from unfair, improper or fraudulent practices" and "to foster fair, efficient and competitive capital markets".

We also believe that certain principles that underpin the Ontario *Securities Act* (**OSA**) should be included in the CMA, such as requiring "timely, open and efficient administration and enforcement" of the legislation and ensuring that "business and regulatory costs and other

restrictions on the business and investment activities of market participants should be proportionate to the significance of the regulatory objectives to be realized". These principles are often applied by regulatory authorities and market participants when considering the appropriate scope of new rules and regulations, requests for exemptive relief and appeals of regulatory decisions.

Our support for a harmonized regulatory framework is also based on an expectation that the CCMRS should maintain or improve the status quo. Consequently, compliance costs should not increase and the conditions under which market participants conduct business and serve their clients should not be less favourable than they are today.

The CCMRS initiative represents a significant step forward. However, certain proposed regulatory changes raise material concerns for the CBA because they appear to go beyond the process of harmonization by introducing new regulation or by selecting the most onerous form of regulation in respect of a particular policy area from among different approaches currently applied by the Participating Jurisdictions. We appreciate the opportunity to provide comments on this consultation and invite the Participating Jurisdictions to engage with the CBA and its member banks (and their subsidiaries, where applicable) in discussions throughout the process. The CBA would be pleased to arrange such meetings.

Given the potentially large impacts that the CCMRS may have on all market participants, it is imperative to ensure that the responsibilities and authority of the CMRA are coordinated with those of existing federal regulatory bodies (such as the Bank of Canada, the Office of the Superintendent of Financial Institutions (**OSFI**) and the Financial Consumer Agency of Canada (**FCAC**)), as well as securities authorities in the non-Participating Jurisdictions, in order to minimize legal uncertainty and market disruption when the CMRA becomes operational.

In responding to this public consultation, we note the difficulty in assessing the Proposed Provincial Legislation in the absence of (a) the revised CMSA; (b) governance and constituting instruments for the CMRA; (c) detailed guidance on how the CMRA's broad discretion would be exercised; (d) clarification on how the CMRA would coordinate and interact with non-Participating Jurisdictions; (e) an understanding of the relationship and coordination amongst regulators at all levels of government, including the Bank of Canada, OSFI and the FCAC at the federal level; (f) implementation legislation of the Participating Jurisdictions; and (g) transitional provisions referred to in Part 16 of the CMA. In light of the magnitude of the proposed changes and the absence of these key items, we believe that market participants would benefit from an additional comment period once the entire regime has been proposed. A second comment period would also allow market participants to consider the comments of other participants, which would be particularly valuable given the extent of the proposed changes.

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We have set out below some of our members' key concerns with the Proposed Provincial Legislation. Our fundamental concerns with the Proposed Provincial Legislation are the absence of the equivalent of section 35.1 of the OSA (the **Financial Institutions Exemption**) and the proposed regulatory framework for over-the-counter (**OTC**) derivatives. We would welcome further dialogue with the Participating Jurisdictions on these two issues. In addition, we have included in Appendix A to this letter further detailed comments that are more technical in nature.

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FINANCIAL INSTITUTIONS EXEMPTION

General Comments

As noted above, our members continue to support efforts that would achieve a unified and rationalized approach to capital markets regulation in Canada that is more efficient and effective, with lower compliance costs for capital markets participants, more robust and consistent enforcement and protection for investors and faster decision-making. The CCMRS should not impose new requirements on market participants, which create a more difficult environment in which to conduct their business and serve their clients relative to the status quo. We are therefore opposed to the CCMRS decision not to carry forward the Financial Institutions Exemption under the Proposed Provincial Legislation.

We believe that it is inappropriate to fold a fundamental change in the regulation of financial institutions in Ontario into the broad release of Proposed Provincial Legislation. The decision not to carry forward the Financial Institutions Exemption requires extensive analysis and consultation to fully appreciate the consequences for Canadian banks.

The absence of a Financial Institutions Exemption in the Framework would have a material negative impact on how banks, and their affiliated trust companies, conduct their businesses, primarily in Ontario as their principal place of business. In turn, this would adversely affect how banks would be able to serve their customers – institutional, commercial and retail – to achieve their economic objectives. Despite the broad potential for market disruption, the Participating Jurisdictions have not articulated a policy rationale for adopting the more restrictive registration requirement as the basis for harmonization among jurisdictions, rather than adopting the approach currently applied in Ontario, where the majority of the affected economic activity is conducted. Nor has a full impact assessment been conducted to evaluate the impact of changing a provincial regulatory regime which has been working effectively for decades. We strongly recommend that the Financial Institutions Exemption be maintained unless the Participating Jurisdictions can demonstrate that the decision not to carry it forward under the Proposed Provincial Legislation would be beneficial and not detrimental to the capital markets.

Historical Reliance on the Financial Institutions Exemption

Most Canadian banks have historically relied on the Financial Institutions Exemption as a basis for selling certain types of securities and savings products to customers nationally. The Financial Institutions Exemption originated with the Hockin-Kwinter Accord (the **Accord**). Under the Accord, the government of Ontario and the federal government agreed that OSFI will regulate the securities-related activities of federal financial institutions that are carried on directly by the institution. Such activities include a number of securities dealing activities carried on directly by Canadian banks today, including all money market activities, secondary market trades in corporate debt securities, and portfolio management and investment counseling services. The intent of the Accord is reflected in law: the Securities Dealing Restrictions (Banks) Regulations under the *Bank Act* (the **Bank Act Dealing Regulations**) permit banks to deal in the above noted securities and products in Canada, while the Financial Institutions Exemption provides that Canadian banks are exempt from the dealer registration requirements with respect to activities which are otherwise permitted under the banks' governing legislation (namely, the *Bank Act*).

While the Accord was not entered into by provinces other than Ontario, it is important to note that at that time there were no equivalent dealer registration requirements applicable to banks in the other provinces. At the time of the Accord, Ontario and Newfoundland were the only provinces that had a "universal" registration regime that required all market intermediaries to

register as a dealer, or rely on an exemption from registration, to trade in securities. In all other provinces, there was a broad "exempt market" where banks and other unregistered intermediaries could trade in securities under dealer registration exemptions that aligned with prospectus exemptions in National Instrument 45-106, including the exemption for trades with accredited investors. It was therefore less pressing to implement the Accord in provinces without "universal" registration requirements. Following registration reform and the adoption of National Instrument 31-103 (**NI 31-103**) in 2009, Ontario extended the exemption for federally regulated financial institutions it had agreed to under the Accord by adding section 35.1 to the OSA.

Canadian banks have therefore relied on the Accord, as formalized by section 35.1 of the OSA and the Bank Act Dealing Regulations, to sell various securities and savings products to customers, without reference to provincial registration requirements. The Financial Institutions Exemption is particularly important in this regard because the majority of the securities dealing businesses that are carried on directly by Canadian banks are situated and managed in Ontario. The harmonization approach, in the interest of achieving consistency across the greatest number of Participating Jurisdictions, does not recognize the historical context and importance of the Financial Institutions Exemption, or the rights afforded to Canadian banks under the Bank Act Dealing Regulations, and makes a significant change to the securities regulatory regime applicable to Canadian banks.

Expected Impacts on Banks' Businesses and Customers

In their commentary on the reason for excluding the Financial Institutions Exemption, the Participating Jurisdictions note that this exclusion is consistent with the current securities legislation of the Participating Jurisdictions, other than Ontario. As most Canadian banks primarily conduct their securities trading activities from Ontario, the absence of the Financial Institutions Exemption would have a disproportionate impact on the banks' businesses and clients. The importance of avoiding disruption to established and valid securities trading activities by Canadian banks – representing a disproportionate share of market activity - outweighs the merits of a harmonization approach that primarily emphasizes adopting regulatory approaches that are consistent across the greatest number of Participating Jurisdictions. It is critical that a full impact assessment is considered by the regulators before proposing such significant policy changes. We further submit that the magnitude of the change warrants a separate public consultation process with sufficient time to allow for a comprehensive analysis by market participants.

We have set out in Appendix B to this letter some examples of the types of expected impacts on banks' businesses and the consequential impact on their customers' ability to achieve their business objectives.

Key areas that would be affected include liquidity of the corporate debt market in Canada, such as repurchase agreements and other transactions linked to corporate bonds, and the ability of commercial parties to effectively hedge commercial risk. We also note that certain counterparties prefer to transact with banks as more stable counterparties with assigned credit ratings, rather than transact with broker/dealers. There are also a number of banks' principal trading activities that would be adversely impacted. In addition, there would be adverse impacts on the banks' affiliated trust businesses. As outlined above, more time is required to determine with certainty all of the consequences of the proposed policy change.

Absence of Policy Rationale for Excluding Financial Institutions Exemption

In their commentary, the Participating Jurisdictions have not articulated any policy rationale for the exclusion of the Financial Institutions Exemption from the Proposed Provincial Legislation. Further, we are not aware of any detrimental market impacts, investor protection concerns or abusive practices that have arisen as a result of the inclusion of section 35.1 in the OSA. The commentary by the Participating Jurisdictions notes that banks may continue to rely on a number of registration exemptions in the Initial Regulations or apply for exemptive relief as permitted under the CMA. We respectfully submit that these options would not support an effective transition to the CCMRS for banks. Registration exemptions in the Initial Regulations may not be in place for all trading activities carried on by banks. The registration exemptions currently available under the Initial Regulations do not provide an exemption for all products which Canadian banks are permitted to deal in under the Bank Act Dealing Regulations. For example, if Canadian banks had to rely on the registration exemption for short term debt instruments, certain products traditionally categorized as money market securities could only be sold to "permitted clients" as such term is defined under the Initial Regulations. This significantly restricts the availability of such products through traditional bank distribution channels. Other products which Canadian banks are permitted to trade in under the *Bank Act*, like corporate debt securities, have no applicable exemption from the dealer registration requirements other than the Financial Institutions Exemption.

Where registration exemptions are available, reliance upon the exemptions would still impose significant compliance burdens on banks, contrary to the objective of attaining a more efficient capital markets regulatory regime. While the granting of exemptive relief on a case-by-case basis is an appropriate way to address ad hoc issues as they arise, it is not an effective way to address the varied securities trading activities that Canadian banks and affiliated trust businesses have offered to their clients over several decades in Ontario.

It is an established practice of Canadian banks to engage in certain securities related activities. These activities are permitted under the *Bank Act*, and are comprehensively regulated and overseen by OSFI. With respect to activities where consumer protection is a relevant factor, the banks are regulated and overseen by the FCAC. Therefore, the application of the Proposed Provincial Legislation to banks' securities trading activities, which are already permitted and limited by the *Bank Act*, and regulations thereunder, and regulated by OSFI and FCAC, creates additional layers of regulation without evidence that such regulation is necessary. Moreover, our understanding and expectation have been that an objective of the CCMRS is to harmonize existing regulations and not to change how activities conducted under federal or provincial jurisdiction are regulated.

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REGULATION OF OTC DERIVATIVES

General Comments

The stated approach in the Initial Regulations with respect to derivatives regulations that are still in development is to maintain the status quo, although it is noted that some changes to the status quo are inevitable given the differences between the current derivatives regimes in Participating Jurisdictions. As with the proposed removal of the Financial Institutions Exemption, the CMA approach to the OTC derivatives activities of banks is a substantial departure from existing practices, particularly in Ontario, and involves a number of complex market reform considerations that we do not believe should be included in what is intended to

be a harmonization of provincial securities rules through the CMA.

To the extent that market reforms relating to the OTC derivatives activities of banks are to be undertaken, such an initiative should be pursued within the context of the current deliberations among federal and provincial regulatory authorities, including OSFI, under the auspices of the Canadian OTC Derivatives Working Group, given that banks are regulated at the federal level and to ensure that the views of the non-Participating Jurisdictions are also taken into account. Implementation of the CCMRS is already a complicated process with many important facets to be considered. Proposing to also include changes that would have a material adverse impact on the banks' OTC derivatives activities as part of the CCMRS initiative does not allow for adequate review and discussion of the policy objectives and potential consequences.

Regulation of OTC Derivatives as Securities

Our overarching concern with the CMA approach is that it could undermine the development of a national model for OTC derivatives regulation by the Canadian OTC Derivatives Working Group. Further, we do not believe that regulating the OTC derivatives activities of banks in a similar fashion to regulating the trading of securities is appropriate given that they are fundamentally different types of products:

- in the case of securities markets, there is perceived to be an informational imbalance between issuers and investors, which raises the need for prospectus level disclosures, and trades between investors are effected by intermediaries, which raises the need for registration;

- by contrast, in the case of OTC derivatives, the terms of the contract are negotiated by the parties to it and set out the details of the specific transaction. In other words, OTC derivatives are bilateral contracts, typically between two sophisticated parties. They do not involve an issuer, an investor or an intermediary.

In addition, the OTC derivatives activities of banks are directly overseen by OSFI, and its existing system of federal oversight has worked well. As a consequence, Canada has been recognized as having the strongest regulatory framework in the world for banks for eight consecutive years by the World Economic Forum. To our knowledge, no public policy concerns have been raised with the existing regulatory framework for the OTC derivatives activities of Canadian banks.

Impacts of the CMA Approach

The proposed treatment of the OTC derivatives activities of banks represents a substantial market reform, particularly in Ontario, that raises a wide range of public policy considerations (e.g. whether registration should be imposed; whether prospectus level disclosures are required; whether documentation obligations must be imposed on clients to ensure that specific exemption requirements can be maintained). These changes would have a number of disruptive implications, including (i) increasing the costs and limiting the access for Canadian clients that seek important products in key areas such as hedging (e.g. interest rate swaps; foreign exchange); (ii) the erosion of the competitive position of Canadian banks vis à vis their international peers; and (iii) impairing liquidity of Canadian markets as the regulatory burden of trading OTC derivatives increases in the Participating Jurisdictions, leading some foreign market participants to trade in jurisdictions with less complex regulatory structures.

Recommended Approach to the OTC Derivatives Activities of Banks

The Participating Jurisdictions have suggested that one of the goals of the CMA is to minimize

its impact on stakeholders. As noted above, however, the proposed changes in the CMA to adopt more stringent registration and prospectus requirements than are in place today particularly in Ontario, together with the application of the Outbound Distribution rule (as discussed below), represent a substantial market reform initiative, rather than a technical harmonization exercise.

To the extent that there is a need to review the OTC derivatives activities of banks, we believe that this type of major market reform should be undertaken as a separate public policy process, with its own set of consultations. This type of process would allow for the already strong existing federal regulatory regime that applies to the OTC derivatives activities of banks to be leveraged to respond to any specific regulatory gaps or concerns that may be identified. In our view, this approach would allow for the harmonization of securities rules under the CMA to proceed in the least disruptive manner possible on its own separate track.

Having said that, we have set out below our views on the registration and prospectus requirements as proposed in the CMA. If our recommended approach to derivatives regulation is not accepted, we offer below suggestions directed at the derivatives rules proposed in the Proposed Provincial Legislation. Further below, we also offer our views on CMA rules on civil liability, administration and enforcement, and market conduct in the derivatives context.

Registration Requirements

The Initial Regulations do not maintain the status quo in respect of registration requirements because they adopt the approach that currently applies only in certain Participating Jurisdictions, which is that an exemption is required if not dealing with "qualified parties" (or "permitted clients"). Given that the major Canadian participants in OTC derivatives transactions are Ontario-based banks, and that most Canadian derivatives activity is cross-border activity with these and other Ontario counterparties, it would actually maintain the status quo more effectively to adopt the Ontario approach, which is to participate in the process of developing derivatives-specific registration requirements through the Canadian OTC Derivatives Working Group.

The CMA prohibits a person from acting as a dealer, adviser or large derivatives participant unless registered in accordance with the regulations and in the category prescribed. The requirement applies to entities and to the individuals that act on behalf of the entity. In addition, new NI 31-103 provides in section 1.2(2) that in Alberta and a Participating Jurisdiction a reference to "securities" in NI 31-103 includes "derivatives" unless the context otherwise requires. By deeming OTC derivatives to be securities, new NI 31-103 has the effect of requiring registration in one of the existing categories of registration in order to deal in or advise with respect to derivatives, unless, presumably, the exemption under the CMRA Regulation 91-501 disapplies the derivatives registration requirement contained in the CMA. It also has the effect of making the exemptions in Part 8 applicable to derivatives (other than exchange contracts), although many of them would not be relevant to derivatives in any event.

The result of the proposed changes, in conjunction with the absence of the Financial Institutions Exemption and the Outbound Distribution rule (discussed below), is that Canadian banks would be required to either rely on the proposed exemptions and deal only with permitted clients or qualified parties worldwide, become registered as investment dealers or advisers, apply for exemptions to enter into transactions with their counterparties who are not qualified parties or permitted clients or not offer OTC derivatives, such as foreign exchange forwards for hedging purposes, to commercial clients that are not permitted clients or qualified parties. While the exemptions in NI 31-103 apply to derivatives, none of the categories of exemption is particularly

apt for OTC derivatives or they do not provide any exemption that would not already be covered by the qualified party or permitted client exemption. In our comments below on the prospectus requirements for OTC derivatives, we set out our concerns regarding the qualified party/permitted client exemption and provide recommendations to address this issue.

Section 22 of the proposed CMA introduces a fourth registration category of large derivatives participants (**LDP**) that is to be subject to registration regulations, which have yet to be drafted. If the policy rationale for introducing this registration category is to manage systemic risk, it should be addressed through the CMSA subject to determining whether existing prudential measures are inadequate. Careful consideration should also be given to the impact of an LDP registration category on foreign derivatives market participants. The Participating Jurisdictions should note the experience in the U.S. where foreign market participants are limiting trading with U.S. market participants so as not to have to register in the Major Swap Participant category under the Commodity Futures Trading Commission's rules; few entities are registered in this category. Such a consequence in Canada would have a significant detrimental effect on market liquidity and, without knowing the detail of this registration category, we caution that it may not be necessary or effective.

If our above-noted recommended approach to derivatives regulation is not accepted, we also request the following:

- the registration regime applicable to OTC derivatives be delayed until such time as the Canadian Securities Administrators have finalized and implemented their registration regime specific to OTC derivatives;
- clarification as to whether advisors are exempt if they advise with respect to transactions with qualified parties or permitted clients;
- confirmation in the CMA or Initial Regulations that banks' proprietary trading activities would not trigger the registration requirement; and
- confirmation in the CMA or Initial Regulations that banks are not obligated to report legal entity identifiers of individuals who may in the future be eligible to obtain them, given global privacy and data confidentiality laws applicable to individuals.

Prospectus Requirements

There is authority under section 41 of the CMA to designate certain derivatives to be securities for purposes of the CMA or specific provisions of it. In reliance on this power, section 2(2) of the Derivatives Regulation states that "all OTC derivatives that are not otherwise securities" are prescribed under section 41 of the CMA to be securities for the purpose of Part 5 of the CMA and related Regulations, thereby making all OTC derivatives subject to the prospectus requirements, including CMRA Regulation 41-501 *Prospectus Requirements and Exemptions* unless exempted by the Derivatives Regulation or otherwise. The Derivatives Regulation would exempt trades where each party is a "permitted client" or a "qualified party".

The application of prospectus rules to derivatives could have adverse consequences for banks. We believe it is against the clear intention of the CMA to apply the prospectus requirement to derivatives, unless the particular product is a retail investment product that is more security-like than OTC derivative-like. As stated in "The Capital Markets Act – A Revised Consultation Draft" document, the section 41 power is to prescribe classes of derivatives to be securities, such as "derivatives sold as retail investment products". This power should not be used to essentially read the distinction between derivatives and securities out of the CMA for the purposes of the prospectus requirements.

This prospectus requirement is problematic for Canadian banks for two main reasons. First, in order to rely on the exemption, banks would likely need to amend documentation to obtain qualified party or permitted client representations from counterparties and/or would have to conduct the due diligence required to ensure counterparties have that status. As banks' experiences with implementing the OTC derivatives trade reporting rules demonstrate, there are significant challenges associated with obtaining such representations from clients, especially those located outside of Canada. Certain foreign market participants are hesitant to invest in understanding the Canadian rules and meeting Canada-specific requirements. Clients are fatigued by the burden of regulatory compliance in a multiplicity of jurisdictions, and non-Canadian clients and hedging counterparties are increasingly weighing the burden of complying with Canadian-specific regulations in deciding whether to continue transacting with Canadian banks. In the CMRA context, these challenges are exacerbated by the fact that the CMRA would be a new regulator which entails a certain amount of uncertainty for market participants and further, would be operating alongside multiple existing federal and provincial regulators that have their own – often different – rules. Furthermore, while OTC derivatives trade reporting rules do not currently present a barrier to trading because banks are permitted by exemptive relief to continue trading while attempting to obtain required documentation from their counterparties, the proposed registration and prospectus requirements would have the effect of prohibiting banks from trading until they obtain the required qualified party or permitted client representations, which could disrupt access to derivatives markets.

Second, it appears that banks would be prohibited from offering bank hedging products to their small and medium sized commercial clients. Because the prospectus requirements are effectively impossible to comply with, essentially the activity is prohibited unless a discretionary exemption from the CMRA is obtained. This would have an adverse impact on both banks' businesses and that of their commercial clients if they are unable to satisfy their hedging needs. We believe that the right approach (and the one consistent with principles of administrative law) would be to delay implementation of any rules with respect to distribution of disclosure documents until the specific regulations are developed. Absent a delay in the disclosure document rules, we request that the Initial Regulations include exemptions for OTC derivatives transactions that are entered into "in the normal course of business" and/or for the purposes of hedging by the client.

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OUTBOUND DISTRIBUTIONS

Pursuant to CMRA Policy 71-601, the CMA proposes to adopt the British Columbia securities regulatory regime (**BC Regime**) regarding sales of securities by an issuer or selling shareholder to purchasers located outside Canada (an **Outbound Distribution**). As described in more detail below, adopting the BC Regime would be extremely disruptive to the operation of the Canadian banks' global issuance programs and would impede the ability of the Canadian banks and other Canadian market participants to raise capital outside Canada. The existing BC Regime applies to issuers or selling shareholders that are headquartered in or have certain other connections to British Columbia. Accordingly, the Canadian banks and the majority of Canada's multinational issuers are not currently subject to the BC Regime.

Under the BC Regime, an issuer that proposes to issue securities in an Outbound Distribution must either file a Canadian prospectus or rely on an available prospectus exemption under which purchasers outside Canada become subject to the attendant Canadian resale restrictions

that will apply to those securities. The BC Regime differs dramatically from the approach taken by Ontario and other Canadian jurisdictions, which allows issuers to generally conduct any type of public or private Outbound Distribution without preparing and filing a Canadian prospectus or relying on an exemption. In such cases, the purchasers outside Canada are not subject to resale restrictions, so long as it is reasonable to conclude that the securities will be held by good faith purchasers outside Canada.

Adoption of the BC Regime would impose new and, in our view, unnecessary restrictions on the ability of Canadian market participants to make public offerings in the United States, Europe and other foreign jurisdictions. While certain exemptions would be available under the proposed rules, they would not apply to certain of the banks' current Outbound Distributions, including certain unlisted and/or private deals. In addition, even where an exemption may otherwise be available, in the context of a public retail offering, the requirement for purchaser certifications and acknowledgements and the filing of detailed issuer reports may not be feasible. Furthermore, in many cases any requirement to legend securities in connection with the resale restrictions would not be possible, as legended or restricted securities cannot be traded through the foreign exchanges or markets on which those securities would trade.

In summary, adopting the BC Regime would constitute the adoption of a new and unwarranted regulatory regime, imposing additional burdens on issuers and investors that would force them to change their longstanding and well-established financing and investing practices, without any demonstrated corresponding investor protection benefit. We urge the Participating Jurisdictions to reconsider their decision to propose the BC Regime or adopt sufficiently broad prospectus exemptions relating to Outbound Distributions so that Canadian banks and other Canadian market participants would not be forced to make unnecessary and prejudicial changes to the practices and procedures they currently follow.

While the Initial Regulations would provide for statutory exemptions and policy guidance for determining when a transaction or activity may be considered outside the scope of a trade or distribution subject to the CMA, these may not be particularly relevant or practical in the context of derivatives. As a result, this would extend the CMRA's authority to cross-border activity with counterparties outside of Canada, thereby requiring market participants to obtain qualified party or permitted client representations from counterparties worldwide and in turn magnifying the potential market disruption discussed above. We note that other jurisdictions may have lower thresholds to determine which counterparties may enter into a transaction.[1] OTC derivatives typically provide for restrictions on transfers, negating any policy concern regarding potential resale to counterparties in Participating Jurisdictions.

With respect to derivatives, given the different nature by which derivatives are contracted between counterparties as compared to how securities are distributed to investors and our concerns above about the proposed expansion of prospectus requirements to derivatives, we recommend that derivatives be clearly exempted from CMRA Policy 71-601. Any policy concerns about banks engaging in derivatives transactions with counterparties outside of

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[1] For example, under s. 1a(18) of the U.S. *Commodity Exchange Act*, a corporation with net worth of $1m, which enters into each transaction in connection with its line of business or to manage the risk associated with an asset or liability owned or incurred by it in the conduct of its business, may enter into a foreign exchange forward as an "eligible contract participant". Alternatively, a counterparty that is not an "eligible contract participant" may enter into a foreign exchange forward if it has the ability to deliver and accept delivery and will enter into the transaction in connection with its line of business. However, under the CMA, the same corporation in the U.S. trading with a Canadian bank would be required to meet the more stringent qualified party or permitted client thresholds. This places Canadian banks at a competitive disadvantage relative to our global peers.

Canada should be raised in the context of the ongoing discussions among the federal and provincial authorities on the Canadian OTC Derivatives Working Group.

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INTERACTION BETWEEN THE AUTHORITY AND NON-PARTICIPATING JURISDICTIONS

It is unclear how the CMRA would interact with the non-Participating Jurisdictions. As banks, and their subsidiaries, operate on a national basis, the ability to maintain efficient access to provincial markets is a key issue for our members. Banks have adopted their policies, practices and systems to serve their clients within the current regulatory regime. It will be very important to ensure that the CMRA becoming operational does not undermine the smooth functioning of the capital markets and its participants, including investors, issuers and financial intermediaries. For example, the "principal regulator" model currently in place has been very effective, and it would be helpful to have a similar model in place between the CMRA and the non-Participating Jurisdictions. As the timeline approaches for the CMRA becoming operational, every effort should be made to ensure a seamless transition from the current securities regulatory regime to the CMRA regime, including with respect to the interaction with non-Participating Jurisdictions.

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STATUS OF EXISTING EXEMPTIVE RELIEF ORDERS

We note that the Participating Jurisdictions have issued a document entitled Summary of Proposed Transition Approach (**Summary**) clarifying how discretionary relief would be treated for certain activities by market participants. It is still unclear, however, how existing exemptive relief orders for other types of activities not set out in the Summary would be treated under the CCMRS, especially given the absence of the transitional provisions in Part 16 of the CMA. The Summary states that decisions of a predecessor regulator would become decisions of the CMRA and those decisions would have effect in all Participating Jurisdictions, including exemptive relief decisions. The Summary, however, also provides that the Chief Regulator and the CMRA would have the ability to vary or revoke decisions of predecessor regulators to resolve any discrepancies between decisions made in different Participating Jurisdictions. This Summary, coupled with the omission of the transition provisions from Part 16 of the CMA, creates uncertainty as to whether existing exemptive relief would be grandfathered under the CMA. It is also unclear whether market participants would have a positive obligation to notify the CMRA of every relief order upon which they are relying. In order to facilitate a seamless transition to the CMRA and avoid business disruption to market participants, the transitional provisions should ensure that existing exemptive relief continues under the CMA.

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CIVIL LIABILITY, ADMINISTRATION AND ENFORCEMENT, AND MARKET CONDUCT

The CBA supports robust and consistent enforcement of the rules and regulations applicable to capital markets in Canada. However, some of the civil liability, administration and enforcement, and market conduct provisions in the CMA deviate in meaningful ways from the current framework. Given the magnitude of the CCMRS initiative, we strongly believe that substantive

provisions of existing securities laws should not be altered, except as required to implement the CCMRS. It would be better to undertake a full assessment of the proposed civil liability, administration and enforcement, and market conduct provisions separately, once the Framework and supporting regulations have been finalized and the CCMRS has been fully operational for some time. There is a need for additional consultation in order to fully consider the implications of the expansion of current definitions, the lack of necessary defined terms, novel enforcement mechanisms, constitutional issues, and due process issues. We have set out below those proposed provisions and changes that are of primary concern to us.

CIVIL LIABILITY

Shift of onus to director or expert

In an action against a director or expert, sections 119(3) and 121(3) of the CMA shift the onus to the director or expert to show that a reasonable investigation was conducted. In our view, it is neither necessary nor desirable to shift the onus to the defendants in these matters. This shift would increase the complexity and costs of defending securities class actions, as it would likely encourage plaintiffs to name directors and experts as a matter of course. These provisions would make it significantly easier for a plaintiff to sue a dealer that has given a fairness opinion, for example, without any factual basis for believing that the opinion is inaccurate. This change is of particular concern to our members who provide fairness opinions and other types of analysis in a variety of circumstances that could give rise to liability. We therefore recommend that the changes proposed to sections 119(3) and 121(3) of the CMA not be adopted.

Expanded statutory rights of action

Section 120(2) of the CMA expands the right of action for misrepresentation in a directors' or officers' circular to permit the plaintiff to sue an expert whose consent was filed in respect of the circular. Section 131(2) of the OSA only permitted the right of action against any director or officer who signed the circular. This is a significant change that would affect our members' dealer subsidiaries that provide fairness opinions, or other expert analysis, in circulars.

Section 122 of the CMA expands the current right of action for misrepresentation in an offering memorandum to apply to any document given to an investor in the course of a prospectus exempt distribution. This provision is overly broad, as it appears to capture a wide range of documents including, for example, the charts and promotional literature on an investment advisor's desk. Section 122 of the CMA also removes the requirement that the purchaser acquired the security "during the period of distribution". We are concerned that this might open the door to "primary market" rights of action in respect of securities that may be sold on the secondary market. As well, section 122 expands the prospective defendants to include any person who signs the disclosure document, or may subsequently become required to sign a disclosure document, in a prospectus exempt jurisdiction which, in some cases, could capture underwriters. Although the Participating Jurisdictions noted in response to comments that "unlike a prospectus offering, the right of action under section 122 is not available against underwriters involved in the private placement distribution", there may be some risk that underwriters could be named as defendants if they sign the disclosure document, or subsequently become required to sign a disclosure document, in a prospectus exempt distribution. For these reasons and consistent with the principle that the CCMRS initiative should focus on harmonizing existing legislation and regulation and not introduce new or more broadly onerous requirements, the proposed expansion of the right of action for misrepresentation under sections 120 and 122 should not be adopted.

Liability for insider trading
The CMA incorporates the British Columbia approach to liability for insider trading, which provides that a person found to have contravened the CMA insider trading provisions is liable to anyone who purchased the security at the relevant time. In contrast, section 134(6) of the OSA only makes the insider trader liable to the counterparty in the transaction. Section 115 of the CMA mandates increased fines for contraventions of the insider trading, tipping, recommending, and front-running provisions in sections 62 to 67 of the CMA.

The CMA expands liability for insider trading while at the same time eliminating the defence in section 175(3) of the OSA General Regulation, which allows a dealer or other financial services organization that is seeking to rely on the existence of "reasonable policies and procedures", such as ethical walls, designed to prevent contraventions of the insider trading rules (the **Policies and Procedures Defence**). In practice, this has operated akin to a "burden shift": where a respondent establishes the existence of reasonable policies and procedures, the plaintiff in a civil case or the prosecution in a quasi-criminal case must establish that these policies and procedures were insufficient, or were otherwise circumvented or undermined. This provision is an important procedural protection and, in our view, should be carried forward to the CMA. If it is not brought forward, registrants would be subjected to increased exposure to civil and quasi-criminal liability in the conduct of their day-to-day business, despite the fact that they took reasonable steps to implement appropriate policies and procedures to prevent the contravention of the insider trading rules.

In addition, OSC Policy 33-601 (**OP 33-601**) includes guidelines that a number of full service investment dealers follow in order to satisfy the requirements of the exemption contained in subsection 175(1) of the OSA. The policies and procedures established pursuant to subsection 175(3) of the OSA in many instances represent the industry standard with respect to the restrictions on trading and/or research in the context of a merger or acquisition. The CMA does not contain the equivalent of OP 33-601. Without OP 33-601, there would be an inconsistent approach to ethical walls put in place by investment dealers which could harm investors and create an unlevel playing filed. We strongly recommend that OP 33-601 be updated to reflect current industry standards and its equivalent be included in the CMA.

We also have concerns with respect to the definition of "special relationship" in section 7 of the CMA. In regard to large issuers in particular, the inclusion of all employees of an issuer and its subsidiaries and affiliates (rather than just directors, officers and other key individuals) for the purposes of the insider trading and tipping prohibitions creates an unduly broad web of potential liability for various market participants, especially as it relates to the "chain of tippees" analysis. This is problematic when coupled with the significant penalties arising from the broad vicarious liability approach introduced in sections 83 and 114 of the CMA. Section 83 provides that, subject to certain exceptions, a person contravenes capital markets law if the person's employee acting within the scope of his or her employment, or the person's agent acting within the scope of the agent's authority, contravenes capital markets law. Similarly, section 114 provides that, subject to certain exceptions, in a prosecution for an offence under capital markets law, it is sufficient proof of the offence to establish that it was committed by the accused's employee acting within the scope of his or her employment, or the accused's agent acting within the scope of the agent's authority. Extension of vicarious liability principles to the regulatory sphere exposes organizations to significant quasi-criminal liability and significant penalties for non-conduct failures (e.g., an inadvertent gap in a compliance program rather than separate problematic conduct by the organization) as a result of virtually automatic vicarious liability for employee conduct. Moreover, an employer may implement and properly monitor appropriate procedures and controls intended to avoid employee misconduct. Seeking to hold

an employer vicariously liable for the conduct of a rogue employee, even though appropriate procedures and controls are in place, is unduly harsh. We recommend that the CMRA adopt an approach consistent with the approach currently contained in the OSA.

The CMA approach is also problematic because it may encourage class actions for insider trading, either as stand-alone proceedings or in other securities class actions. Plaintiffs' counsel in securities class actions may incorporate this cause of action, particularly alongside claims alleging failure to make timely disclosure, against insiders who traded during the proposed class period in an effort to exceed the damages caps in Part 13 of the CMA, even if the CMRA is not investigating the defendant or does not have any reason to believe that the insider trading provisions have been breached. The result is that plaintiffs may frequently allege that directors and officers of issuers and underwriters have breached the insider trading laws, notwithstanding that they have no evidence or basis to support the allegation other than a publicly disclosed trade during the class period. We encourage the Participating Jurisdictions to reassess the expansion of the civil right of action for insider trading beyond its current form in the OSA.

ADMINISTRATION AND ENFORCEMENT

Expanded review, investigation and search powers

Part 11 of the CMA includes a range of expansive review, investigation and search powers that could become disruptive and onerous for banks' operations. These expanded powers include:

- Section 102 of the CMA, which gives the Chief Regulator the power to order that a market participant provide to the Chief Regulator any information, record or other thing in the market participant's possession or control. Unlike section 11 of the OSA, this section provides that the Chief Regulator may require the market participant to provide an affidavit verifying any information or record. It is our view that this requirement is unnecessary as our members already have a requirement to respond to requests for information;

- Section 103 of the CMA, which gives reviewers designated by the Chief Regulator broad powers to enter the business premises of any market participant to review the market participant's business and conduct. These powers appear to be more extensive than those under section 20(4) of the OSA. In particular, the CMA gives the reviewer the specific power to use any computer or electronic device, or other system, on the premises in order to examine the information contained on that system;

- Section 103 of the CMA also gives the Chief Regulator certain authority over "market participants," including the authority to review business conduct, require a market participant to provide information and records, and to make enquiries of any person under review, including its employees, agents, officers, directors and control persons. The term "market participant" includes persons exempted from the registration requirement as well as those distributing securities in reliance upon prospectus exemptions. As a consequence, dealers that rely on registration exemptions to trade or distribute derivatives (including the qualified party and permitted client exemptions) would be subject to this authority. Foreign counterparties may exit Canadian capital markets rather than be subject to the Chief Regulator's authority, which would be detrimental to the liquidity available in the markets. Moreover, this authority is likely to be difficult to enforce for such institutions;

- Subsection 103(3) of the CMA requires a market participant to provide information "in the form ... specified" by the Chief Regulator. This portion of the provision may become onerous for market participants, who may be ordered to produce records in a manner that is not within the scope of how the information is produced in the normal course of business. Although our members seek to cooperate with the securities regulators when requests are made for records, there may be some limitations in providing documentation in the form requested by the Chief Regulator. Accordingly, subsection 103(3) should simply be limited to the requirement to provide records and not prescribe the form of the record without further discussion with industry on this issue;

- Subsection 104(1) of the CMA has added in the term "as the Chief Regulator considers expedient", presumably, for the purpose of conferring discretion. We recommend that this portion of the subsection be removed as it is overly broad. Orders by the Chief Regulator ought to be authorized solely for the purpose of the administration or enforcement of capital markets law and regulation and not simply because the Chief Regulator deems it "expedient"; and

- Section 104(8) of the CMA, which allows the Chief Regulator to make a search order in support of an investigation unless the search relates to a dwelling house. This power does not appear to be curtailed, other than by the broad investigatory purposes set out in section 104(1) of the CMA. Under section 13(4) of the OSA, only a judge had the power to make a search order. We recommend that the same oversight provision contained within subsection 13(4) be incorporated into the CMA in order to protect the fundamental legal rights of market participants.

Moreover, Part VI of the OSA prescribes limits on the confidentiality and disclosure of information relating to an investigation, whereas the CMA does not include these same protections. Instead, the Chief Regulator may make an order restricting disclosure, but does not appear to be required to do so. We are concerned that these expansive powers would lead to overlapping regulation of banks' activities. Banks are already subject to oversight and regulation by OSFI and the federal Department of Finance. As such, we encourage the Participating Jurisdictions to provide exemptions in the Proposed Provincial Legislation from these provisions for banks as they are already subject to the similar authority of OSFI. Market participants that are not subject to registration because they qualify as qualified parties or permitted clients also should be exempt from the Chief Regulator's authority.

Alternatively, we recommend that the Participating Jurisdictions include a provision in the CMA to the effect that, where an investigation involves obtaining information from a bank, the Chief Regulator must first attempt to obtain information through cooperation with the bank and OSFI, and only resort to exercising these powers to enter and access the bank's records – including by searching the bank's computer systems – as a last resort. We hope to work cooperatively with the Chief Regulator in respect of its review, investigation and search obligations, and want to ensure that these powers would not be exercised in a manner that becomes unduly onerous for our members.

We are also concerned that the failure to incorporate limits on confidentiality creates constitutional issues for market participants that are compelled to provide evidence to an investigator, particularly in circumstances where a foreign regulator seeks to obtain the compelled evidence from the Chief Regulator and the foreign jurisdiction does not contain protections similar to those in Canada with respect to compelled evidence. We recommend that

the CMA include similar limits on the disclosure of information as contained within the OSA.

Expanded cease-trade powers and removal of protections around freeze orders
The CMA gives various persons the power to issue cease-trade orders that may be broader than those under current Ontario securities law. For example, section 87 of the CMA permits the Tribunal to make a cease-trade order in respect of a security or a derivative, with or without notice, on the basis that, for example, the CMRA becomes aware of information that is likely to cause unusual fluctuations in the market price of the security or derivative. The CMA also adds a provision that gives the Tribunal the right to order, if a bank has control of another person's derivatives, that the bank liquidate those derivatives and retain the proceeds.

Under section 87 of the CMA, the Tribunal may order that all trading in a derivative cease based on a number of factors. A cease-trade order can be made without notice or an opportunity to be heard for 15 days after which an opportunity to be heard must be given to those directly affected. Since "trading" with respect to a derivative includes not only entering into a transaction, but also amending it or terminating it, and because this provision is not restricted to exchange traded derivatives or those that trade over a market place or a facility, it has a potentially broad application. The ability of banks to hedge their exposures to the subject underlying interest could be compromised by such an order. We would expect that the Tribunal would exercise this power sparingly and in appropriate circumstances, given the potential consequences of this power. We recommend that the application of this power be limited to exchange traded derivatives and those standardized derivatives that trade on a marketplace.

Our members are also concerned that the CMA removes some of the existing protections around freeze orders. For example, the OSA requires the Ontario Securities Commission (**OSC**) to apply to court as soon as possible to extend a freeze order, whereas section 91(7) of the CMA permits the Tribunal to extend the order on application by the Chief Regulator and after a hearing. Any application by the Chief Regulator to extend a freeze order under this section should be made on notice to the affected parties and the affected parties should be given the opportunity to make submissions at the hearing. In addition, section 126(2) of the OSA provides that a freeze order that names a bank applies only to the branch(es) of the bank named in the freeze order, while the CMA is silent. This provision should be carried forward to the CMA.

Under section 91, on an application from the Chief Regulator, the Tribunal can on certain specified grounds relating to the regulation of capital markets make certain orders that require persons to undertake a number of actions relating to the freezing of funds, securities, derivatives or other property. Because of how broadly the power is expressed, in the derivatives context, it could extend to preventing a counterparty to transactions with a bank or a bank with respect to its counterparties from terminating transactions or dealing with its collateral. It is very important that the provision be clarified to the effect that such an order cannot prevent a party to an eligible financial contract (as defined in the *Payment Clearing and Settlement Act* (Canada)) from exercising its close-out rights, including its right to deal with collateral on a termination event or event of default. The potential for an order to interfere with such rights may preclude banks from netting exposures for capital purposes, thereby adding significant cost for market participants. By providing for such a power, the CMA could undermine the reductions in exposure (and hence reductions in systemic risk) achieved through legally effective netting and collateral arrangements. Further, this power may affect the certainty level of netting and collateral opinions prepared by the International Swaps and Derivatives Association. While the safe harbours in insolvency legislation might override this power in the context of an insolvency of a particular counterparty, the netting and collateral rights also have to be enforceable outside of insolvency. Any uncertainty about the ability of counterparties to net and exercise their close-

out rights would compromise the ability of Canadian financial institutions to mitigate systemic risk, would increase their regulatory capital costs for their derivatives transactions and would cause foreigner counterparties to consider other markets in which to transact because of these obstacles, all of which are contrary to objectives of a more unified and rationalized regulatory system.

MARKET CONDUCT

Record retention of seven years
Section 54 of the CMA provides that market participants must keep records necessary for the proper recording of business transactions and financial affairs and of the transactions executed on behalf of others, as well as reasonable records to demonstrate compliance with capital markets laws, for seven years. While the OSA is silent as to what constitutes a "record", the CMA has adopted an expansive definition: record includes anything containing information, regardless of its form or characteristics. Thus, a wide variety of documents and communications, including voicemail and audio recordings, would likely constitute records under the CMA. The expansive definition is overly onerous on our members, particularly with respect to the requirement to maintain voicemail and audio recordings. The provision ought to be restricted to electronic and/or physical documents or prescribe a separate period specifically for records maintained in different formats.

The record retention provision is a departure from the status quo in Ontario, as the OSA does not impose a minimum record-keeping period on market participants. We urge the Participating Jurisdictions to limit the application of section 54(2) regarding the duration of records retention to registered firms in accordance with section 11.6(1) of NI 31-103. Alternatively, we request that the Participating Jurisdictions permit a transition period to allow market participants to implement measures to comply with this requirement. In addition, we seek clarification from the Participating Jurisdictions as to whether the seven year retention requirement applies retroactively or only to records that come into existence after the CMA takes effect.

Front-running offence
The CMA provides for a more specific and well-defined front-running offence than the current Ontario equivalent and includes derivatives as part of the prohibition on front-running. Section 130(2) of the CMA provides that a person who breaches the front running provisions in section 67 of the CMA must pay the "investor", within the meaning of section 67, an amount equal to the benefit or advantage received as a result of the contravention. This is a new cause of action in Ontario securities law. Given the broad definition of "person" in the CMA, we recommend that the Participating Jurisdictions adopt the defences outlined in section 4.1(2) of the Investment Industry Regulatory Organization of Canada's (**IIROC**) Universal Market Integrity Rules. This section includes, among other defences, a general defence if the individual trading had no actual knowledge of the client order.

Market conduct rules in the derivatives context
In addition to the above-noted concerns regarding the provisions relating to records retention and front-running offences which also apply in the derivatives context, we note that there are particular concerns when applying market conduct rules to derivatives trading. While banks and their securities dealer subsidiaries have existing policies and procedures to deal with existing market conduct rules that apply to securities trading, developing policies and procedures for derivatives trading is, relative to securities trading, more difficult given the nature of derivatives markets. Many of the market conduct provisions in Part 9 of the CMA deal with actions that affect the "market price" for a "derivative" or that deal with information or trading with respect to

an "underlying interest" of a derivative, which can obviously be a wide variety of interests. In this context, we have set out specific comments below on sections 55, 59, 62 and 66 of the market conduct rules in the CMA.

Section 55 – Duty of Fair, Honest and Good Faith Dealing
Section 55 imposes a duty on "registrants" to deal with "clients" fairly, honestly and in good faith and to meet other requirements. In the absence of a Financial Institutions Exemption, those banks that are compelled to become registrants would be subject to this duty as it now applies and will continue to apply to registered broker-dealers. The reference to *clients* is unclear in the context of OTC derivatives transactions. Because banks are often dealing with other dealers or financial intermediaries and the transactions are bilaterally negotiated, there is not necessarily a party that could be described as the client or, indeed, each party may be a client of the other. As we note earlier in our submission, any proposals to further regulate OTC derivatives should be determined as part of the broader federal-provincial deliberations being undertaken by the Canadian OTC Derivatives Working Group chaired by the Bank of Canada, rather than through various regulatory amendments that extend securities regulations to derivatives via the Proposed Provincial Legislation.

The introduction of an express statutory duty to act "fairly" could give rise to negative unintended consequences. The banker-customer relationship is not a fiduciary relationship in the normal course nor do duties of good faith apply to the negotiation of transactions at common law (although they apply to some extent to the exercise of contractual discretionary rights). We note that the existing provision on which section 55 is modelled is not considered to import a fiduciary duty into the relationship. It is unclear at this time whether a breach of such a duty in the context of an executory contractual relationship such as exists with OTC derivatives would potentially affect the validity or enforceability of the contract.

In order to address these concerns, we recommend the following:

- the reference to "client" be clarified by defining it to include only counterparties that are not a financial institution or another registrant, including large and sophisticated non-financial entities;
- it be made explicit in section 55 that the duty does not import fiduciary duties or a duty to determine the suitability of a transaction for a counterparty; and
- the provision should include an express statement that breach of the duty does not provide a basis for challenging the validity or enforceability of a contract between the registered dealer and its counterparty or client. The common law duty of good faith in Canada can address any contractual effects of the breach of such a duty. Also, it would be useful to include a provision similar to section 59(2) precluding any statutory right of action for damages and to extend it to preclude the remedies of rescission or declarations that the contract was void, voidable or otherwise unenforceable.

Additionally, it is unclear what the purpose of the phrase "and meet such other standards as may be prescribed" is intended to achieve. As it is drafted, it is vague and ambiguous, which results in uncertainty in the market place. We recommend that this phrase be removed from section 55 of the CMA.

Section 59 – Misleading Statements
Section 59 prohibits a "person" from making a statement it knows or reasonably ought to know is materially false or misleading and would reasonably be expected to have a significant effect on the market price or value of a "derivative" or "underlying interest of a derivative".

This prohibition is very broad and would require implementation of policies and procedures similar to what dealers would have in place with respect to securities. However, this provision is much more vague in its application to derivatives and specific policies may be difficult to develop. There is nothing in the provision currently to suggest that the person making the statement must be aware of the specific derivative. For example, it would potentially apply to a bank if an analyst makes a misleading press statement about the market for a relatively rare or illiquid commodity or about a particular producer of such a commodity, even though the bank or that producer does not participate in the derivatives markets and is unaware of any specific derivatives transactions but is aware that there is a derivatives market with the commodity as the underlying interest. It might also provide a ground for a counterparty to argue that a contract should be rescinded, as Section 59(2) precludes actions for damages, but not for rescission or declarations that a contract is void, voidable or otherwise unenforceable. In addition, there is not necessarily a market price or value for OTC derivatives, so it is unclear how the provision could be applied.

These practical concerns about the application of Section 59 arise from our more general concern that the Proposed Provincial Legislation seeks to equate derivatives with securities when stipulating the regulatory requirements. Extending these requirements to OTC derivatives goes beyond harmonization of existing regulations and should be excluded. As we have noted here and in regard to other proposed regulatory changes, the broad inclusion of OTC derivatives without separate consultation and assessment of the impacts, could have material adverse consequences for derivatives activities in Canada and the economic benefits associated with derivatives transactions.

Section 62 – Market Manipulation
Section 62(1) of the CMA deals with "market manipulation" and prohibits a person from (among other things) participating in any act or course of conduct relating to a derivative or underlying interest of a derivative that results in or contributes to an artificial price or value for a derivative. The term "underlying interest" is defined very broadly. Read literally, this provision could potentially catch an option or warrant (a derivative) on shares in a private company (the underlying interest) where the bank is a lender to that company and has received equity sweeteners as part of the loan arrangements. The inclusion of an underlying interest of a derivative in this provision seems to make it potentially broader than might have been intended. Similar to our recommendation for section 59 above, the reference to derivatives or the underlying interest of a derivative should be removed from section 62. Concerns of the Participating Jurisdictions about these instruments should be brought to the Canadian OTC Derivatives Working Group so that any possible remedies can be assessed within the broader deliberations about possible regulation of OTC derivatives.

Section 66 – Insider Trading
Section 66 of the CMA sets out the restrictions on insider trading and tipping. This prohibition is broader than section 76 of the OSA in that section 66 applies to a "purchase or trade" as compared to a "purchase or sale" of a security, with "trade" having the expanded meaning discussed below. The change in definition invites uncertainty in an area that has been defined through years of case law by the courts and the securities regulators. We recommend that the CMA adopt the more restricted "purchase or sale" phrase as contained in section 76 of the OSA.

The prohibition is also broader in that it applies to securities and "related financial instruments", a concept that includes not only derivatives but also "agreements, arrangements, commitments or understandings" that affect a person's "economic interest" in a security, namely the right to

receive a benefit or exposure to risk. Once again, the expansive definition is vague and overly broad, which would result in uncertainty as to what properly falls within the definition. We recommend that the CMA adopt a provision similar to the language contained within the OSA.

The front-running prohibitions in section 67 of the CMA have also been expanded specifically to capture derivatives.

The expanded concepts in sections 66 and 67 would capture a broader range of transactions and require amendments to internal policies and procedures, including possibly more restrictive information walls and restricted list procedures, to avoid information obtained by one division of the bank from tainting its other activities. These prohibitions may also operate to restrict unduly entering into, rolling, amending or terminating certain types of derivatives contracts where the entity may have undisclosed material information regarding an issuer whose securities form part of or are otherwise connected to the underlying interest, even in circumstances where the relationship between the issuer or security and the instrument is tenuous. Therefore, we recommend more tailored defences under section 68 of the CMA, such as an expanded "legal obligation" defence that permits a party to trade, amend, roll, etc., in accordance with the terms of a contract, or even a non-documented arrangement or practice, entered into or agreed to prior to acquiring knowledge of the undisclosed material fact or material change. This should also include circumstances where a party has the discretion to disagree, although in practice the party would not generally do so.

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EXCHANGE TRADED DERIVATIVES

Currently, the only Participating Jurisdictions that have the concept of an exchange contract are British Columbia and Saskatchewan. For the other Participating Jurisdictions this would be a significant shift in the treatment of exchange traded derivatives. In Ontario, for example, under the proposed derivatives regulations, "exchange contract" would include commodity futures contracts and commodity futures options currently regulated under the *Commodity Futures Act* (Ontario) (**CFA**) as well as exchange traded equity and other options that are currently regulated as securities under the OSA.

Since the CFA is proposed to be repealed, subject to the enactment and coming into force of the CMA, all of the registration exemptions contained in the CFA would be revoked. For example, the unsolicited trade exemption, hedger exemption and exemption for banks providing incidental advice would all be repealed. To the extent that Canadian banks and/or their affiliates relied on these exemptions in the past, this would be a significant change. In order to facilitate a smooth transition to the CCMRS, we recommend that the CFA exemptions be carried forward into the final version of the Proposed Provincial Legislation. We also recommend that the CMA clarify that banks can trade futures for their own account without relying on another exemption, such as the hedger exemption or the exemption for trades through a registered dealer.

Exchange contracts would be subject to the market conduct provisions applicable to derivatives in the CMA. Please see above our comments regarding the market conduct rules in the CMA.

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TRADE REPOSITORIES AND DERIVATIVES DATA REPORTING

We note that, generally speaking, CMRA Regulation 91-502 (**TR Rule**) is similar to the existing trade reporting regime in Ontario, Quebec and Manitoba. We assume that, before the Initial Regulations are adopted, the TR Rule would be revised to be consistent with the November 2015 proposed amendments to the trade reporting rules in Ontario, such as those relating to legal entity identifiers.

The first draft of the CMSA allowed for the adoption of trade data reporting obligations at the federal level. We had hoped that the trade reporting requirements for Canadian banks would be part of the federal regime so that banks, which operate on a national model, would be subject to one set of requirements consistently across the country. The proposed CMA regulation, however, does not recognize any distinction between Canadian banks and other "dealers". Hence, banks would continue to be subject to potentially inconsistent trade reporting requirements as between the Participating Jurisdictions and the non-Participating Jurisdictions. They would continue to have to solicit representations from clients as to their local counterparty jurisdiction in order to provide access to the correct jurisdictions. We believe that the better approach would be to exempt banks and other federally regulated financial institutions from the trade reporting requirements in the TR Rule, and place the trade reporting obligations of these institutions in the CMSA. The trade reporting requirements should be harmonized across the CMA and the CMSA to facilitate standardized reporting and ensure a level playing field for all market participants.

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In closing, we reiterate our support for unified and rationalized capital markets regulation across Canada. We do, however, have significant concerns regarding the Proposed Provincial Legislation as discussed above, where certain proposed changes go beyond harmonization to introduce additional regulation or to adopt the more stringent and costly version of a regulation currently in place among the Participating Jurisdictions.

We recognize that there are differing views among the Participating Jurisdictions regarding the necessity of the Financial Institutions Exemption. At the very least, we believe that the legislation that will be introduced in Ontario in order to implement the CCMRS should include a "grandfathering" provision for section 35.1 of the OSA that maintains the Financial Institutions Exemption until such time as the CCMRS is fully operational. This would allow regulators and market participants more time to fully assess the impacts and potential negative unintended consequences arising from the absence of the Financial Institutions Exemption. Further, both regulators and market participants would benefit from having the final federal CMSA, as well as the implementation proposals for the CMRA, in place as they are carrying out the impacts assessment.

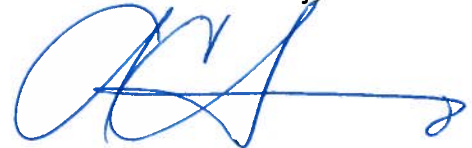
Furthermore, in the absence of detailed information regarding how the rules and oversight powers of the Participating Jurisdictions would be coordinated with those of the federal Department of Finance and the relevant federal regulatory agencies, as well as those of the securities authorities in the non-Participating Jurisdictions, we continue to be concerned about the significant potential for duplicative or conflicting regulation and enforcement of the securities and derivatives trading activities of the Canadian banks and their subsidiaries and affiliates.

Finally, in light of the magnitude of the proposed changes and the absence of key aspects of the regime, we believe that market participants would benefit from an additional comment period

once the entire regime has been proposed. A second comment period would also allow market participants to consider the comments of other participants, which would be particularly valuable given the extent of the proposed changes.

We would be pleased to meet with representatives of the ministries of finance and securities regulatory authorities in the Participating Jurisdictions to discuss our concerns and recommendations. Please do not hesitate to contact me with any questions regarding our comments.

Yours truly,



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APPENDIX A

List of Provisions and Changes of Concern to CBA Members

Provision / Change	Comment
Registrants – Dealers and Advisers	
Investment fund manager (**IFM**) and non-resident IFM definition and registration requirements	The CMA adopts the Ontario model regarding the definition of and registration requirements for IFMs. Ontario currently requires IFM registration in Ontario if any fund managed by the IFM has security holders in Ontario. In contrast, the current British Columbia approach requires provincial IFM registration only if the firm carries out some business activities in British Columbia. Regarding non-resident IFMs, s.8 of Regulation 31-501 adopts the approach taken in Ontario, Quebec and Newfoundland, which is that the registration requirement applies to any non-resident IFM that solicits investors or sells fund securities to investors located in these jurisdictions, subject to certain narrow exemptions. We recommend adoption of the British Columbia model, as it most closely aligns with the familiar "passport" model of registration and activity and is more appropriately grounded in the IFM / non-resident IFM needing to have a meaningful connection with the jurisdiction. We also note that the CMA approach would have an impact on financial institutions that currently operate or distribute investment funds in Ontario in reliance on the Financial Institutions Exemption.
OSC Rule 35-502, s.7.6 The registration exemption for a non-resident adviser to advise the pension fund of an affiliate has not been carried forward under the CMRA.	Please confirm that the reason this exemption is not being carried forward is that advice provided by a non-resident adviser to an affiliated pension plan would not generally be considered registerable activity.
NI 31-103, s.8.12 The exemption from dealer registration for trades in mortgages now carves out trades in syndicated mortgages.	As this change would affect banks that previously traded syndicated mortgages in reliance on the Financial Institutions Exemption, such trades should be retained in the exemption.
The following provisions of NI 31-103 now extend to "related financial instruments": • Exemption from adviser registration available in respect of the provision of "generic advice" now applies to generic	Further to our comments in the letter accompanying this Appendix, expansion of NI 31-103 to derivatives, as is being proposed in sections 8.25(2), 13.5 and 13.6, should be addressed outside of this initiative to create the

Provision / Change	Comment
advice regarding "related financial instruments" and provides that registration is not required in respect of the provision of advice that does not purport to be tailored to the needs of the recipient (s.8.25(2)); • Restrictions on certain managed account transactions (s.13.5); and • Related and connected issuer disclosure (s.13.6).	CCMRS so that the distinct aspects of trading and advising in derivatives can be properly assessed as part of a holistic review.
Issuers	
Adoption of MI 51-105 – Issuers Quoted in the U.S. OTC Markets	The purpose of MI 51-105 is to impose regulatory oversight on issuers that trade on the OTC securities markets in the United States, but are not listed on a Canadian or U.S. stock exchange. If certain conditions are met, MI 51-105 transforms OTC issuers (i.e., issuers with a class of securities quoted on an OTC market in the United States, including the "pink sheets" or grey market, unless the issuer also has a Canadian or U.S. stock exchange listing) into reporting issuers, despite possibly having no public company disclosure record or desire to create or maintain one. In addition to imposing reporting issuer requirements on the issuer and its insiders involuntarily (at significant expense to the issuer, ultimately borne by its shareholders), once an issuer has been designated as an OTC issuer, it is subject to a number of unique requirements, including resale restrictions being imposed on its shareholders. These requirements continue so long as the issuer remains an OTC issuer, even if it already is a conventional reporting issuer, or later becomes a conventional reporting issuer. The regulatory burden that MI 51-105 imposes on issuers that are not listed on a Canadian or U.S. stock exchange is unfair and disproportionate to the regulatory objective that was sought to be achieved. The CMRA should not carry forward MI 51-105 and should instead pursue other, and more appropriate, means of addressing any perceived abuses that arise as a result of trading U.S. OTC quoted securities in Canada.
CMRA Regulation 51-501 requires non-reporting issuers that are corporations, partnerships and trusts formed or governed under the laws of	An issuer's securities may start trading on the "pink sheets" or "grey market" U.S. OTC markets without the issuer's knowledge or consent. For this

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Canada or a CMR jurisdiction, whose securities are listed or quoted on foreign marketplaces, to file certain information within ten days after the date of the listing or quotation.	reason, we propose that any requirement to file information relating to a new listing or quotation should be triggered by the issuer's actual knowledge of a listing or quotation, and not the fact of becoming listed or quoted itself.
Prospectus Requirements	
CMA, s. 37 S. 37 outlines the delivery requirement for prospectuses and prescribed offering documents. The equivalent section 71(1) of the OSA includes a carve-out from the delivery requirement if the dealer has previously delivered a prospectus.	A similar carve-out should be included in s. 37 of the CMA, whereby if a person has already delivered the prospectus or prescribed offering document to the purchaser, then the person should not be required to deliver that same document again.
Civil Liability, Enforcement and Market Conduct	
CMA, s.62 S.62(1) provides that a person must not, directly or indirectly, engage in, or participate in, any act, practice or course of conduct relating to a security, derivative or underlying interest of a derivative that results in or contributes to a false or misleading appearance of trading activity in a security or derivative or an artificial price or value for a security or derivative. S.62(2) provides that a person must not, directly or indirectly, attempt to engage or participate in the conduct described in subsection (1).	Contrary to s.126.2(1) of the OSA, the CMA provision does not appear to require knowledge (or constructive knowledge) of the consequences of the misrepresentation; that is, the person making the statement need not know that the statement would result in or contribute to a misleading appearance of trading activity. This proposed change should be revised to be consistent with s. 126.2(1) of the OSA.
CMA, s.70(b) This section provides that a person must not, in relation to a trade, engage in an unfair practice, including taking advantage of another person's inability or incapacity to reasonably protect his or her own interest because of, among other things, ignorance regarding a decision to trade in a security or derivative.	In our view, the inclusion of ignorance is inappropriate. A person cannot avoid liability for violating a law merely because he or she was ignorant of its content. Similarly, a person should not be able to plead ignorance in connection with a decision to trade in a security or derivative.
CMA, s.72(2) This section provides that a person must not make a statement about something that a reasonable investor would consider important in deciding whether to enter into, or maintain, a trading or advising relationship with the person if the statement is false or misleading or omits information that is necessary to prevent it from being misleading in the circumstances in which it is made.	The use of "false or misleading" departs from the current use of "untrue" in s.44(2) of the OSA, thereby broadening the scope of this provision.
CMA, s.77 This section is the anti-reprisal or "whistleblower"	We recommend a requirement for employees to report a specific instance of potential misconduct

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provision. It essentially provides that an employer must not take disciplinary or other retaliatory measures against an employee because the employee provides information or expresses an intention to provide information to the employer, the Authority, a recognized self-regulatory organization or a law enforcement agency respecting an act of the employer or a director, officer or employee of the employer that the employee reasonably believes is contrary to capital markets law or a by-law, policy or other regulatory instrument of a recognized self-regulatory organization. Reprisals are also prohibited because the employee testifies or expresses an intention to testify in any proceeding of the Authority or a recognized self-regulatory organization or a judicial proceeding in relation to such information.	internally at least once before reporting to the Authority, a recognized self-regulatory organization or a law enforcement agency. We are concerned that the absence of this requirement could negatively impact the effectiveness of market participants' internal reporting, escalation and compliance systems. This requirement would assist in preserving internal reporting systems and communication, both within compliance departments and between compliance departments and business lines, and fostering these relationships so that issues would be addressed proactively. We note that the previous draft of the CMA limited this provision to whistleblowing in relation to capital markets law but the revised draft expands the scope to include by-laws, policies or other regulatory instruments. We recommend that the Participating Jurisdictions narrow the scope of this provision to capital markets law.
CMA, s.89(1)(l) This provision permits the Tribunal to make an order, after a hearing, that a person is prohibited from acting in a management or consultative capacity in connection with activities in the securities or derivatives market if the Tribunal considers that it is in the public interest to do so.	Please define the terms "management" and "consultative capacity" in this context.
CMA, s.89(1)(r) This provision permits the Tribunal to make an order, after a hearing, that a person is prohibited from voting or exercising any other right attaching to a security at a meeting specified in the order.	Temporary orders should not be permitted to prohibit a person from taking such actions. Pursuant to s.89(5), an order under s.89(4) expires no later than 15 days after the day on which it is made. Prohibiting a person from exercising rights attached to a security at a meeting, even on a purportedly temporary basis, would result in a de facto final order if the meeting were held during the 15 days when the order is in effect. It is also inconsistent with s.161 of the British Columbia Securities Act, which does not have a provision equivalent to s. 89(1)(r).
CMA, s.89(4) This provision gives the Chief Regulator – rather than the Tribunal – the power to make most of the orders prescribed in section 89(1), without giving an opportunity to be heard, if the Chief Regulator considers that a delay in making an order could be	This provision is an expansion of the powers in s.127(5) the OSA, which only permit the OSC to make certain orders. Moreover, the CMA gives this broad power to the Chief Regulator. It may be more appropriate to give this power to the Tribunal, notwithstanding that the affected party

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prejudicial to the public interest.	may be deprived of the opportunity to be heard. We are concerned that this provision would permit temporary orders requiring a market participant to submit to an audit or review of its practices and procedures (per s. 89(1)(m)) without the opportunity to be heard. This power is inconsistent with a temporary order. By the time a permanent order is granted, the audit or review may already be complete. Thus, a temporary order may become a de facto permanent order, with no opportunity for the market participant to be heard.
CMA, s.90(2) This provision gives the Tribunal the power to order that a person who has contravened capital markets law compensate or make restitution to one or more persons.	Please clarify the scope of what is intended by this power. If the level of restitution or compensation rises to the level of damages, then it may ultimately usurp the role of the courts in some securities litigation. It also has the potential to significantly change the risk profile and settlement dynamics for persons or companies who are the subject of parallel Tribunal and Court proceedings, as is often the case. The power to order compensation or restitution should only be made in coordination with a disgorgement order under s.90(1) to avoid a duplicative penalty from being assessed.
CMA, s.95 This section allows the Authority to make designation orders removing or according status. In particular, s.95(2)(j) permits the Authority to make an order designating a person to be a market place if the Authority considers that it would be in the public interest to do so. CMA, s.95.1 This provision allows the Authority, if it considers that it would be in the best interest to do so, to make an order that an exchange be recognized for the purposes of a regulation or any provisions of a regulation, or a market place be designated for the purposes of a regulation or any provisions of a regulation.	Designating a person to be a market place could have an impact on best execution. Dealers and advisors would have to enter into agreements with these designated market places in order to satisfy their best execution obligation, creating an operational burden. Dealers and advisors would need time to put such agreements in place and could be exposed to liability from investors who might argue that such an agreement was not in place, thereby preventing the investor from receiving the most advantageous execution terms reasonably available.
CMA, s.100(6) This provision allows the Tribunal to make a further decision on new material if there is a significant change in the circumstances.	In the interests of protecting natural justice, the Tribunal's ability to make a further decision on new material or if there is a significant change in the circumstances should only be permitted after the affected parties have been given an opportunity to

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	be heard in respect of the new material or changed circumstances.
CMA, s.104(4) This provision permits an authorized investigator to compel the production and preservation of information, records or things and the giving of evidence, and summon the attendance of any person.	To better align production obligations with those in civil and other proceedings, and in particular to avoid the potential for overly broad production orders in light of the broad purposes set out in s.103(1), the power to compel production should be limited to information, records or things that are relevant to the scope of the matters under investigation pursuant to s.104(1) and s.104(3).
CMA, s.105 This provision requires the owner or person who is in charge of a place that is entered under s.103(4), s.104(7) or s.104(8), and every person who is in the place, to give all assistance that is reasonably required to enable the designated reviewer to conduct the review or the authorized investigator to conduct the investigation.	This section is overly broad and should be limited to investigations under s.104. Reviews under s.103 should not be included.
CMA, s.117 This provision addresses actions relating to a prospectus or prescribed offering document.	Please clarify the meaning of "prescribed offering document." Neither the CMA nor its Regulations define this term for the purposes of s.117.
CMA, s.119, s.121 and s.123 These sections place the burden of proof on the defendant in connection with an action alleging misrepresentation in a prospectus, prescribed offering document, prescribed disclosure document, take-over bid circular or issuer bid circular.	We are concerned that the reverse burden of proof would lead to greater potential liability in Participating Jurisdictions versus non-Participating Jurisdictions like Quebec and Alberta, which is at odds with the CMA's goal of harmonization.
CMA, s.130(3) This section includes a specific provision for insider trading relating to investment funds.	The similar provision in s.134(3) of the OSA provides that a person or company may be accountable to a mutual fund *in Ontario*. The CMA provision does not incorporate a territorial limitation. A similar territorial limitation should be included in the CMA provision to specify that a person is accountable to an investment fund, other than a prescribed investment fund, in any Participating Jurisdiction.
CMA, ss.138-143 These provisions allow purchasers of securities offered by a prospectus, offering memorandum or other types of prescribed disclosure documents to rescind the purchase in a manner prescribed by regulation.	The drafters state that even though they have replaced the term "written notice" with "notice" throughout the CMA, including in the civil liability provisions, this is not intended to be a substantive change. In each case, notice must be "sent" to the recipient in accordance with s.198 of the CMA. In our view, this change may create unnecessary confusion and potential for disputes.

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	Another issue with the way that the CMA is drafted is that the right of rescission can expand beyond the standard types of securities to which it applies under the current OSA regime. The CMA is clear that it applies to securities purchased under a prospectus, mutual fund securities (s.140 of the CMA) and securities purchased under an offering memorandum (s.21 of Regulation 11-501), but it also leaves the door open to further types of securities to which these rescission rights may apply.
CMA, s.195(1) This section provides that nothing in the CMA shall be construed to affect the privilege that exists between a solicitor and his or her client in relation to information or records that are subject to that privilege.	Please clarify that all forms of legal privilege are protected (e.g., litigation privilege, common interest privilege) and not only solicitor-client privilege.
CMA, s.195(2) This section provides that if a person consents to the disclosure to the Authority of information or a record that is subject to privilege, the consent neither negates nor constitutes a waiver of the privilege and the privilege continues for all other purposes.	This provision should extend to disclosure to the Chief Regulator of information or a record that is subject to privilege.
CMA, s.196(a) This section provides that before the Chief Regulator discloses evidence given under s.104(4)(b), he or she must provide the person who gives the evidence with notice that it may be disclosed and for what purpose, and must give the person an opportunity to be heard, unless the disclosure is made in a proceeding commenced or proposed to be commenced under the CMA or in an examination of a witness.	Please clarify what "or in an examination of a witness" means and the circumstances in which this provision would apply.
CMA, s.196(b) This section provides that before the Chief Regulator discloses evidence given under s.104(4)(b), he or she must provide the person who gives the evidence with notice that it may be disclosed and for what purpose, and must give the person an opportunity to be heard, unless the Tribunal authorizes the disclosure, on an application made without notice by the Chief Regulator, if the Tribunal considers it to be in the public interest.	In our view, disclosure should only be permitted after the hearing of an application made on notice to the affected parties. We are concerned that compelled evidence could be used in an investigation or action in the United States without the ability to plead the U.S. Fifth Amendment because the evidence would have already been disclosed under s.196(b). Compelled evidence would also defeat a person's protection against self-incrimination.

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Removal of OSA costs provisions The CMA does not include the special costs rules in s.138.11 of the OSA that are intended to help deter unmeritorious litigation. This section provides that, despite costs rules in the *Class Proceedings Act* that were designed to promote access to justice, the prevailing party in an action under Part XXIII.1 is entitled to costs in accordance with the applicable rules of civil procedure.	In our view, the better approach would be to adopt the OSA provision – which was recommended by the Canadian Securities Administrators during the design of these civil liability provisions in 2000 – because loser-pays costs rules can help deter frivolous litigation.

APPENDIX B

Business Impacts

Operational/Infrastructure Impact

- Certain Canadian banks conduct their debt securities dealing business at the bank level, not within their dealer affiliate. Unlike their dealer affiliates, Canadian banks rely on the Financial Institutions Exemption, and therefore are not registered as dealers.
- Some of the debt securities traded by banks are exempt from the registration requirements pursuant to Part 8 of NI 31-103 (for example, debt securities issued by the Canadian government). However, other debt securities traded by the bank are not exempt from the registration requirements. Corporate debt securities are the principal type of debt security traded at the bank level for which no exemption from the dealer registration requirement is available.
    - Moreover, many banks also engage in transactions other than simple trades which involve corporate debt securities including repurchase transactions.
- Banks are permitted to deal in these types of debt securities under the Bank Act Dealing Regulations.
- Without a general exemption from the dealer registration requirement, Canadian banks would have to take one of the following steps to continue trading in corporate debt securities or engaging in other transactions involving these types of securities:
    - Register as a dealer; or
    - Transfer this business to a registered broker dealer affiliate.
- Registering the bank as a dealer under a self-regulatory organization like IIROC would be particularly onerous. Canadian banks would be subject to new and stringent controls and policies. In particular, Canadian banks would have to meet IIROC's capital requirements for their existing inventory of debt securities, which we believe would be more onerous than existing bank capital requirements. There would therefore be additional impediments and costs to the capital raising activities of Canadian banks. It would also interfere with OSFI's activities as a prudential regulator of Canadian banks. For these reasons, registering as a dealer is not an option for Canadian banks.
- Transferring the debt securities dealing businesses from the banks to their respective registered dealer affiliate would take significant time and impose additional operational costs:
    - Certain banks book trades in corporate debt securities on different systems than those used by their dealer affiliates. The systems used by their dealer affiliates are not designed to accommodate trades in, or manage inventories of, debt securities. Significant time and cost would have to be invested into the systems used by the dealer affiliates to accommodate corporate debt securities. In addition, every corporate debt security position at the bank would have to be reconciled to the dealer affiliate's system, which is a time-intensive and costly process.
    - As mentioned previously, since the bank dealer affiliates are subject to more stringent capital requirements under the IIROC rules, moving a new book of corporate debt securities to the dealer affiliate would impose additional capital requirements and costs on the Canadian banks' dealer affiliates.
    - Many bank clients only trade in debt securities with the bank. If trading in corporate debt securities and other non-exempt products is moved to the dealer affiliate, each of those clients would have to be on-boarded and verified again by the dealer affiliate. This duplicative effort would create additional costs for the bank, take a significant amount of time, and be an inconvenience to clients.

Customer Impacts

- The Financial Institutions Exemption allows Canadian banks to deal and trade in any product without being registered as a dealer if permitted under the *Bank Act*, including products like corporate debt securities and money market securities.
- While Part 8 of NI 31-103 contains exemptions for products like money market securities, the exemptions include additional conditions, namely the requirement that the sale be made to a 'permitted client.'
- Permitting banks to sell money market securities only to permitted clients significantly restricts the availability of these products to customers:
  - Money market securities, due to their short-term nature and high liquidity, are considered to be low-risk investments. They also tend to offer high rates of return relative to traditional savings accounts and term deposits.
  - For these reasons, money market securities are highly desirable to retail and commercial customers of the bank who wish to purchase low-risk savings products without the need for a financial advisor. Therefore, these products are often sold to such customers outside of registered dealer channels, for example, through bank branches.
  - However, many retail and commercial customers do not meet the net-asset thresholds under the "permitted client" definition. Such products could then only be sold through brokerage businesses and financial advisors. This would fundamentally alter the bank's business model and distribution channels.
  - While certain money market products could be traded under an exemption other than the short term debt exemption under NI 31-103, other money market products, like commercial paper, are subject to the permitted client exemption.
- Certain other high net worth customers, who would otherwise meet the definition of a "permitted client" as well as applicable prospectus exemptions, are interested in purchasing products like corporate debt securities outside of broker/dealer or advisor distribution channels.
- With respect to certain transactions involving corporate debt securities, such as repurchase agreements, many clients view Canadian banks as being a more stable and less risky counterparty than the dealer affiliates. Customers would therefore be less interested in entering into these transactions if they could only be carried out by the dealer affiliates.

OTC Principal Trading Activities

Without more clarity on how the business trigger would be applied to principal trading activities by banks, and without clarity on the definition of a "client" versus a "counterparty", banks may not be able to engage in the following OTC principal trading activities except through a dealer:

- Corporate bonds (registration may be required even when trading with foreign dealer counterparties);
- Equities (this may impact banks' "buyback" business, where a bank sells equity securities off market to the issuer);
- Repurchase agreements (this may impact banks' ability to trade in repurchase agreements that are linked to corporate bonds);
- Investment funds for cash management.

Bank-affiliated Trust Companies

If the Financial Institutions Exemption is not included in the CMA, banks' affiliated trust companies may be required to register as:

- an "adviser" that is "in the business" of advising in securities when making securities investment decisions in its capacity as a trustee, including when delegating investment decisions to a sub-adviser;
- a "dealer" when it acts in connection with the sale of debt instruments for which product-specific registration exemptions are unavailable; and
- an "investment fund manager" if it:
    - administers an investment fund that falls outside of the exemption in section 8.29 of NI 31-103 because it:
        - has a promoter or investment fund manager other than the trust company, and
        - does not commingle the money of different estates and trusts for the purpose of facilitating investment, or
    - acts as the trustee of an investment fund.

Currently, trust companies have discretionary authority to make investment decisions for a trust; even where the investment decisions have been delegated to a registered sub-adviser, the trust company retains the ability to make investment decisions for a trust. Where a trust company is acting as trustee for a trust, the trustee has a fiduciary duty to investors in, or beneficiaries of, the trust. Given the stringent obligations that arise out of a fiduciary duty, we do not see the need for a trust company to be registered under the CMA and subject to all the obligations thereunder.