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BY EMAIL

Cooperative Capital Markets Regulatory System

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Dear Sirs/Mesdames:

RE: Comments regarding the proposed Cooperative Capital Markets Regulatory System and related legislation

TMX Group Limited ("TMX Group") appreciates the opportunity to comment on the proposed Cooperative Capital Markets Regulatory System ("CCMRS") and the related proposed Capital Markets Act ("CMA") and regulations. We urge regulators to use all efforts to ensure that the CCMRS will have a net positive impact on the Canadian market. Even small changes to a regulatory framework can be disruptive and have unintended negative consequences, whether those changes are of a substantive, procedural or transitional nature. The changes proposed under the CCMRS must result in a Canadian market that remains attractive to all participants, both domestic and global. This is the primary lens TMX Group applied in considering the CCMRS proposal.

TMX Group continues to be supportive of efforts to make Canada's capital markets more efficient and brings a unique perspective to the CCMRS comment process through our central and multifaceted role in Canadian capital markets. Our interests are aligned in maintaining the integrity and stability of the financial system, preserving fair, efficient and competitive capital markets and ensuring appropriate management of systemic risks. Efficient and intelligent regulation helps ensure capital market global competitiveness and a strong national economy. We have a strong, vested interest in ensuring that the legislation can achieve its intended objectives.

While TMX Group is supportive of efforts to harmonize securities regulation across Canada, we have a number of concerns with respect to the proposal. We are commenting on two main areas:

i. efficiency and level playing field concerns generally, particularly concerns regarding interface and transition; and

ii. derivatives regulatory framework.

We believe that efforts should be taken now to ensure that the CMA and its regulations provide a sound framework for the regulation of securities and derivatives in this country. This is an important juncture for regulators to ensure that Canadian regulation serves as a platform to position us on the global stage. This opportunity should not be missed.

Unless otherwise defined, capitalized terms used herein have the meanings given to them in the CMA.

(i) Efficiency and Level Playing Field Concerns

Interface and Transition

Issuers and other Capital Markets Participants

Capital markets participants continue to need certainty with respect to the future of the fundamental capital markets legal framework in order to feel comfortable operating in the market and engaging in longer range planning and decision-making. We continue to urge the participating jurisdictions to publish guidance regarding how and to what extent they intend the Authority to work with securities regulators in the non-participating provinces and territories, the Bank of Canada, the Office of the Superintendent of Financial Institutions and any other relevant regulators following implementation of the CCMRS. We note that the commentary published with the CMA regulations (the "CCMRS Regulation Commentary") states that the interfacing provisions are to come. We urge the participating jurisdictions to prioritize the regulations regarding how the CCMRS will interface with non-participating jurisdictions at this point in the process. In particular, a statement regarding whether the participating jurisdictions intend to participate in the passport system is key to assessing the functionality of the CCMRS.

Recognized and Exempted Entities

We thank the participating jurisdictions for providing a high level summary of the proposed transition approach. However, we request further clarification regarding the transition of our recognized and exempt entities to the CCMRS. We note that the proposed transition approach indicates that if an entity is recognized by more than one predecessor regulator, regulatory staff will work with the entity to harmonize existing recognition orders, and that if an entity is subject to both recognition orders and orders that exempt it from recognition, the orders exempting the entity from recognition will be revoked and only the recognition order would continue. We note that certain of our regulated entities have requirements set out in their exemption orders that are not included in their recognition orders. We request clarification that regulatory staff will also work to harmonize the applicable requirements in our existing recognition orders and exemption orders to ensure an appropriate level of oversight by the Authority. We also note that TMX Group has made undertakings to certain existing securities regulators, in both participating jurisdictions and non-participating jurisdictions, and we request clarification regarding the transition of these undertakings to the CCMRS.

We continue to be extremely concerned about the consequences of the CCMRS on the lead regulator model set out under the Memorandum of Understanding Respecting the Oversight of Exchanges and Quotation and Trade Reporting Systems and the cooperative model set out under the Memorandum of Understanding Respecting the Oversight of Certain Clearing and Settlement System. We note that these memoranda of understanding are of critical importance to the efficient functioning of exchanges and clearing and settlement systems in Canada. The lead regulator model has been beneficial to TMX Group and the capital markets by reducing unnecessary regulatory duplication while maintaining an appropriate level of regulatory oversight. We remain concerned about the impact on market participants and our operations if the CCMRS no longer ensures a lead regulator model in respect of our exchanges and clearing agencies.

Regulatory Authority over Marketplaces

Novel Definition of Marketplace

The definition of marketplace is well understood in Canadian securities law, is substantially harmonized among the Canadian Securities Administrators ("CSA") jurisdictions and is not an open-ended definition. The types of entities that are currently understood to be marketplaces are exchanges, quotation and trade reporting systems and alternative trading systems ("ATS").[1] The introduction of open-ended terms such as prescribed marketplaces and designated marketplaces in paragraphs (d) and (e), respectively, of the definition of marketplace[2] is a substantive change to the law that requires further clarification from the participating jurisdictions, particularly regarding the additional activities and entities these paragraphs are intended to capture.[3]

Although we understand the need for flexibility regarding the regulation of marketplaces, the participating jurisdictions have not provided the rationale for adding both prescribed marketplaces and designated marketplaces to the definition of marketplace. Our understanding

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[1] We note that the definition of marketplace in section 1.1 of National Instrument 21-101 *Marketplace Operation* ("NI 21-101") is substantially harmonized across Canada and that the guidance in Part 2 and Part 3 of Companion Policy 21-101CP ("21-101CP") indicates that in Canada there are three types of marketplaces: exchanges, quotation and trade reporting systems and ATSs. We note that the participating jurisdictions have proposed to adopt NI 21-101 and 21-101CP with minimal changes.

[2] Pursuant to the CMA, "market place" means:

(a) an exchange;
(b) a person who is not an exchange but who
    (i) constitutes, maintains or provides a market or facility for bringing together buyers and sellers of securities,
    (ii) brings together the orders for securities of multiple buyers and sellers, and
    (iii) uses established non-discretionary methods under which the orders interact with each other, and the buyers and sellers entering the orders agree to the terms of a trade;
(c) a dealer who executes a trade of an exchange-traded security outside a market place described in paragraph (a) or (b);
(d) any other person who constitutes, maintains or provides a market, facility or system for trading in securities or derivatives and is prescribed to be a market place or is within a class of persons prescribed to be market places; or
(e) any other person who is designated under subsection 95 (2) to be a market place, but does not include a person who is designated, or is within a class of persons who are designated, under subsection 95 (1) not to be a market place, or who is within a class of persons who are prescribed not to be market places.

[3] We acknowledge that the September 2014 Consultation Draft: Summary of Comments Received and Ministerial/Regulatory Reponses (the "Summary of Comments") states that derivatives trading facilities will be captured under paragraph (d) of the definition of marketplace and that to the extent that the definition of marketplace is broadened by paragraph (d), details will be set out in regulation and will be subject to comment under Part 15 of the CMA. We submit, however, that further guidance regarding paragraphs (d) and (e) of the definition of marketplace is still required.

is that prescribed marketplaces will be prescribed by regulation, while designated marketplaces will be designated by a decision of the Authority. We request that the participating jurisdictions provide guidance regarding paragraphs (d) and (e), particularly regarding why it is necessary for the definition of marketplace to be broadened by both regulation and a decision of the Authority, and whether the categories of marketplaces in (d) and (e) are intended to be mutually exclusive or may overlap.

Unclear Distinction between Recognized Exchanges, Designated Marketplaces and Other Marketplaces

Similar to the definition of marketplace, the regulation of marketplaces is currently well understood and articulated in Canadian securities law.[4] While we acknowledge that the Summary of Comments indicates that no immediate change to the regulation and oversight of marketplaces is contemplated, we submit that the concept of categorizing marketplaces as either recognized exchanges, designated entities or other marketplaces under Part 3 of the CMA is a new concept that has not been clearly articulated by the participating jurisdictions.[5] We request clarification regarding why these categories are necessary and the distinction between these categories. In particular, we request guidance with respect to the amount of oversight the Authority will have over marketplaces in each category and the anticipated regulatory requirements for marketplaces in each category.

We think it is important that the participating jurisdictions provide guidance in a regulation regarding how quotation and trade reporting systems and ATSs will be categorized pursuant to sections 9, 17 and 21 of the CMA. We note that the Summary of Comments states that at launch ATSs will be regulated as "other" marketplaces pursuant to section 21 and that the CMA Regulation Commentary states that quotation and trade reporting systems will be recognized and regulated as an exchange. However, this guidance should be included in a regulation so that any change to the regulatory approach for these entities is subject to public comment. Additionally, we request confirmation that orders and decisions regarding marketplaces made by the Authority pursuant to sections 9 and 17 will be made public.

We submit that further guidance regarding the significance of a marketplace being prescribed, designated, recognized or other is required in order to ensure the requirements imposed on each type of marketplace are transparent and to ensure that marketplaces are regulated on a level playing field. We submit that this guidance should be set out in a regulation so that any changes to the current approach regarding the regulation of marketplaces is subject to public comment.

Drafting Comments

We also suggest the following, more specific, issues regarding the definition and regulation of marketplaces be addressed in regulation or a revised draft of the CMA:

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[4] We note that Part 4 of 21-101CP articulates the factors to be considered when recognizing an exchange or quotation and trade reporting system and Part 3 describes the requirements applicable to ATSs. The concept of a "designated" marketplace or an "other" marketplace is not described.

[5] We acknowledge that the Summary of Comments states that designated entities and other marketplaces are not subject to an equivalent to section 13 of the CMA, but we submit that the participating jurisdictions have not articulated the difference between designated marketplaces under section 17 and other marketplaces under section 21.

1. We note that the term quotation and trade reporting system is not defined for the purposes of the participating jurisdictions because it is not defined in the CMA, nor is it defined in NI 21-101 or any other proposed CMA regulation. Therefore, it is not clear that the Authority has the authority to recognize quotation and trade reporting systems, unless it is intended that such entities will be persons engaged in prescribed activities pursuant section 9(1)(e) of the CMA. If so, we submit that this should be specifically set out in CMRA Regulation 21-501 *Certain Capital Markets Participants* ("CMRA Regulation 21-501").

2. It is not clear whether a marketplace that is designated to be a marketplace pursuant to section 95(2)(j) of the CMA (and therefore will fall within paragraph (e) of the definition of marketplace) will also be a designated marketplace pursuant to section 17(1)(f) of the CMA, or whether these are two distinct concepts of designation.

3. Similar to paragraph 2 above, it is not clear whether a marketplace that is prescribed to be a marketplace pursuant to regulation (and therefore falls within paragraph (d) of the definition of marketplace) will be regulated as an "other" marketplace pursuant to section 21 of the CMA, or whether it is possible for a marketplace to be a prescribed marketplace for the purposes of the definition of marketplace and also a designated marketplace pursuant to section 17(1)(f) of the CMA.

4. We request clarification regarding the significance of adding language to section 9(1)(b) stating that the Authority may recognize "a person as" an exchange, but not adding similar language to section 9(1)(a) regarding self-regulatory organizations or section 9(1)(d) regarding auditor oversight organizations.

5. We would also request clarity as to the definition and regulation of a self-regulatory organization ("SRO"), which is not clear from the CMA.

6. In section 12(d) of the CMA, we do not believe that the language "or posted for trading" is necessary, as a security that is posted for trading is covered in section 12(c). We acknowledge that this language appears to be based on section 21(5)(c) of the *Securities Act* (Ontario), but we note that similar language is not included in section 27(1)(f) of the *Securities Act* (British Columbia). Adopting the British Columbia approach in this circumstance would be sufficient.

7. Recognized exchanges should be removed from section 4(4) of CMRA Regulation 21-501 regarding the requirement to set an auditor panel. While this requirement was based on section 21.9(3) of the *Securities Act* (Ontario), such language is antiquated and exchanges have relied on SROs to perform this function for many years.

Decision-Making Powers

Broad Power of the Chief Regulator to Regulate Marketplaces

The broad decision-making power regarding marketplaces given to the Chief Regulator pursuant to sections 12, 20 and 21(2) of the CMA requires further clarification by the participating jurisdictions. We note that similar powers are granted in existing securities

legislation in British Columbia and Ontario,[6] however, existing securities legislation gives these powers to the securities commission, not to the executive director of the commission. We submit that this decision-making power should remain with the Authority, as giving this power to the Chief Regulator is a substantive change in the law that has not be explained by the participating jurisdictions. If this power is to remain with the Chief Regulator, it is very important that the participating jurisdictions issue guidance regarding the anticipated regulatory requirements for marketplaces that are recognized, designated or other in order to clarify the scope of decisions that the Chief Regulator is authorized to make under these provisions. Such clarity will ensure that the regulation of marketplaces is transparent and efficient for customers, as well as that marketplaces are regulated on a level playing field.

We request clarification regarding why the decision-making power set out in section 12 with respect to recognized exchanges and sections 20 and 21(2) with respect to designated marketplaces and other marketplaces, respectively, differs. While we acknowledge that these powers appear to be based on the powers set out in sections 21(5) and 21.0.1 of the *Securities Act* (Ontario) with respect to recognized exchanges and ATSs, until the participating jurisdictions provide more clarity regarding the categorization of marketplaces, it is not clear why the decision-making power over the various categories of marketplace is different.

Broad Decision-Making Powers over all Recognized and Designated Entities

Even if the powers set out in sections 12, 20 and 21(2) are given to the Authority instead of the Chief Regulator, we submit that the extremely broad regulatory powers granted pursuant to these sections to make decisions regarding aspects of many entities' businesses should be limited. We note that sections 12 and 20 are not just applicable to marketplaces, they grant extremely broad powers to control all recognized entities and designated entities and to substitute its view in areas that are, and should remain, matters of business discretion and choice. Specifically, sections 12, 20 and 21(2) provide that:

> If the Chief Regulator considers that it would be in the public interest to do so, he or she may make any decision respecting the following:
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> (a) a by-law, regulatory instrument, policy, procedure, interpretation or practice of a recognized entity, designated entity or other market place;
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> (b) the manner in which a recognized entity carries on business;
>
> (c) the trading of securities or derivatives on or through a recognized exchange, designated entity or other market place;
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> (d) a security or derivative listed or posted for trading on a recognized exchange; or
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> (e) issuers whose securities are listed or posted for trading on a recognized exchange in order to ensure that they comply with capital markets law.

[6] See sections 21(5), 21.0.1 and 21.2.1(1) of the *Securities Act* (Ontario) regarding recognized exchanges, ATSs and quotation and trade reporting systems, respectively, and section 27(1) of the *Securities Act* (British Columbia) regarding recognized exchanges and quotation and trade reporting systems.

While we recognize that similar provisions are currently in force in the *Securities Act* (Ontario)[7] we believe that these provisions could be tapered (particularly subsections (b) through (d)), as they are unnecessarily broad, particularly given that many of these entities do not pose systemic risk to our markets.

We respectfully submit that a regulator should oversee regulated entities by drafting the regulations with which they must comply and exposing proposed regulations to a formal review process, including public comment, which requires input from many stakeholders. This process results in regulations that are thoroughly analyzed and provides certainty, predictability and a level playing field among similar entities. As discussed above, there are currently no standards or procedures set out as to how the Chief Regulator would make these decisions. These decisions should be subject to the regulation-making process set out under Part 15 of the CMA. We also request confirmation that decisions made by the Chief Regulator pursuant to sections 12, 20 and 21(2) will be made public, which we believe is important in order to ensure transparency regarding how such entities are regulated.

Record Collection Requirements

Expansive Powers of Collection

The CMA sets out broad record collection powers, including for purposes of conducting policy analysis. The breadth of the types of records that would be captured in this provision is exceptionally broad and we query whether it is appropriate for the Authority to have unlimited discretion to collect any type of record for conducting policy analysis.[8] Under the CMA and its regulations, regulated entities provide the Authority with extensive records. While the Authority may have the ability to make regulations regarding collection of records – for example, the regulations regarding reporting of over-the-counter ("OTC") derivative transactions – having a broad power to collect any record from any entity at any time and in any form, appears excessive. Further, non-routine requests may require extensive IT searches and coding resources, which should not be imposed upon entities without a cost-benefit analysis. We respectfully submit that, at a minimum, a process should be designed to structure how the Authority will determine the records that would be appropriate to collect, constraints with respect to record collection and how this will be communicated to market participants.

Protection of Confidential Information

Due to the broad record collection powers set out in the CMA, TMX Group submits the CMA should be amended to specify that information provided by marketplaces and clearing agencies to the Authority may be excluded from disclosure under applicable freedom of information and protection of privacy legislation if the Authority determines that the confidence of such information should be maintained. We note that this exclusion is currently provided in section 153 of the *Securities Act* (Ontario). We acknowledge that the Summary of Comments states that the approach to access to information remains under development and that it is anticipated that

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[7] See sections 21(5) (exchanges), 21.0.1 (ATSs) and 21.2(3) (clearing agencies).

[8] Section 187 of the CMA requires that at the request of the Authority, a market participant or other person must, at the time and in the form that the Authority specifies, provide it with the records and information it requires for the purposes of

(a) monitoring activity in capital markets or detecting, identifying or mitigating systemic risks related to capital markets; or

(b) conducting policy analysis related to the Authority's mandate and the purposes of this Act.

carve-outs from freedom of information disclosure under the applicable regimes will be proposed in implementation legislation. We submit, however, that this carve-out should be set out in the CMA itself to ensure that it is consistent across all participating jurisdictions and to ensure that the Authority has jurisdiction to determine whether information should be maintained in confidence.

TMX Group's regulated entities are subject to broad requirements to provide sensitive business information under our recognition and exemption orders and securities legislation. We submit that the interest of non-disclosure of such information outweighs the desirability of adhering to the principle that such information be available for public inspection. We note that this principle is set out in 21-101CP, which the participating jurisdictions are proposing to adopt. This principle is integral to ensuring that all regulated entities are able to communicate candidly with securities regulators and should be included in the CMA.

Enforcement of Decisions made by SROs

TMX Group supports IIROC's position that the decisions an SRO makes after conducting a hearing should be permitted to be filed with the superior court pursuant to section 199 without first being reviewed by the Tribunal pursuant to sections 13 and 89(1)(a) of the CMA. We understand that IIROC has the ability to directly file hearing panel decisions in the courts of Alberta, Quebec and the territories under applicable securities legislation and that IIROC has used this ability to successfully collect fines from registrants at a higher rate than in jurisdictions where it does not have this ability. We are concerned that the current CMA requirement for an SRO's decision to be reviewed by the Tribunal before such decision may be filed with the court pursuant to section 199 creates unnecessary delay, complexity and costs around the enforcement of these decisions. The ability of an SRO to enforce its decisions can have a direct impact on investor protection, and as such we believe that the amendment to section 199 of the CMA proposed by IIROC would contribute to the orderly functioning of the capital markets.

(ii) Derivatives Regulation

TMX Group has a number of specific concerns with respect to the regulation of derivatives under the CCMRS. Below we have detailed our concerns with respect to: (i) meeting the G-20 commitments; (ii) exclusions from the derivatives definition; (iii) lack of clarity with respect to how certain categories will be regulated and what/who they are intended to capture; and (iv) certain aspects of the trade reporting and dealer regulation requirements.

Meeting Canada's G-20 Commitments

At the Pittsburgh Summit in 2009, the G-20 leaders committed to the following: "[a]ll standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties ..."[9] In June 2010 in Toronto, the G-20 leaders reaffirmed this commitment, and expressly stated an objective to increase standardization in OTC derivatives markets.[10] To address these commitments, the CSA published proposed National Instrument 94-101 *Mandatory Central Counterparty Clearing of Derivatives* ("NI 94-101") and CSA Consultation Paper 92-401 *Derivatives Trading Facilities*

[9] CSA Consultation Paper 91-401 on Over-the-Counter Derivatives Regulation in Canada. Online at: https://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20101102_91-401_cp-on-derivatives.pdf.

[10] Financial Stability Board, Implementing OTC Derivatives Market Reforms, 25 October 2010. Online: http://www.financialstabilityboard.org/wp-content/uploads/r_101025.pdf, p.12.

("CP 92-401"), among other reforms. Canadian regulators have stated their desire to ensure that Canadian regulations are aligned and harmonized with international standards.[11] We believe that in order for Canada to meet its G-20 commitments further changes are necessary to encourage standardization and mandatory platform trading and clearing, and to ensure that systemic risk issues in Canada are adequately addressed.

Unlike in the U.S., Canadian derivatives legislation and regulations do not contain a broad requirement that futures products be traded on an exchange and cleared. This issue could be addressed through either the CMA/securities acts of the non-participating jurisdictions or through the CSA derivatives proposals.

Below we have set out:

- how futures products are defined and treated in the U.S.;
- why proposed Canadian regulations may not meet Canada's G-20 commitments to the extent that they should; and
- a suggested approach to remedy the situation.

Futures Definition and Treatment

Pursuant to the Commodity Exchange Act[12] ("CEA"):

> it shall be unlawful for any person to offer to enter into, to enter into, to execute, to confirm the execution of, or to conduct any office or business anywhere in the United States, its territories or possessions, for the purpose of soliciting, or accepting any order for, or otherwise dealing in, any transaction in, or in connection with, a contract for the purchase or sale of a commodity for future delivery (other than a contract which is made on or subject to the rules of a board of trade, exchange, or market located outside the United States, its territories or possessions) unless—
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> (1) such transaction is conducted on or subject to the rules of a board of trade which has been designated or registered by the Commission as a contract market or derivatives transaction execution facility for such commodity;
>
> (2) such contract is executed or consummated by or through a contract market; and
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> (3) such contract is evidenced by a record in writing which shows the date, the parties to such contract and their addresses, the property covered and its price, and the terms of delivery"[13]

[11] In the introduction to NI 94-201 and CP 92-401 respectively, the CSA stated that "[a]lthough a significant market in Canada, the Canadian OTC derivatives market comprises a relatively small share of the global market and a substantial portion of transactions entered into by Canadian market participants involve foreign counterparties. It is therefore important that rules developed for the Canadian market are aligned with international practice to ensure that Canadian market participants have access to the international market and are regulated in accordance with international principles to the extent appropriate." The CSA went on to say "[o]ur goal is to harmonize, to the greatest extent appropriate, the determination of mandatory clearable derivatives or classes of derivatives across Canada and with international standards."

[12] 7 U.S.C. §1 et seq.

[13] CEA, section 6(a).

Commodity Futures Trading Commission ("CFTC") rules for designated contract markets (i.e., exchanges) state that "[t]ransactions executed on or through the designated contract market must be cleared through a Commission-registered derivatives clearing organization…"[14]

The term "futures contract" is not defined in the CEA. However, section 1a(27) of the CEA provides that the term "future delivery" does not include any sale of any "cash commodity for deferred shipment or delivery." This constitutes the fundamental definitional divide between "futures" contracts and "forward" contracts, which are excluded from regulation under the CEA.

The CFTC has developed a working definition of a "futures contract" as "an agreement to purchase or sell a commodity for delivery in the future: (1) at a price that is determined at initiation of the contract; (2) that obligates each party to the contract to fulfill the contract at the specified price; (3) that is used to assume or shift price risk; and (4) that may be satisfied by delivery or offset."[15] This working definition is grounded in case law. It is notable that while futures contracts are required to be on exchange and cleared, unlike the most comparable term used in the CCMRS regulations, the definition itself does not already assume that the product is an exchange-traded derivative. A contract is considered to be a futures contract based on the characteristics set out above and required to be on exchange and cleared if it meets the definition, regardless of the term chosen to label the product.[16] Indeed, it is the fact that an instrument is traded on an exchange that makes its trading legal, not what makes it a futures contract. Thus, it is a violation of the CEA to trade a futures contract off-of-a designated contract market or subject to its rules.

The term "commodity" is intended to be broad and is defined as "[w]heat, cotton, rice,… and all other goods and articles…, and all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in..."[17]

There are no exemptions for particular entities or types of transactions from the requirement that futures be traded on exchange and cleared unless a transaction is considered to be a forward or can be structured as a swap. With respect to retail clients, it is not possible to structure a transaction as a swap to avoid the requirement to trade the product on an exchange. CEA section 2(a)(2)(c)(2)(D) Retail Commodity Transactions, requires that "any agreement, contract, or transaction in any commodity that is— (I) entered into with, or offered to (even if not entered into with), a person that is not an eligible contract participant[18] ["ECP"] or eligible commercial entity[19]; and (II) entered into, or offered (even if not entered into), on a leveraged or margined

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[14] CFTC rule 38.601.

[15] CFTC Glossary, at http://www.cftc.gov/ConsumerProtection/EducationCenter/CFTCGlossary/index.htm#F

[16] See, for example, Commodity Futures Trading Commission v. Co-Petro Marketing Group, Inc., 680 F.2d 573, 580 (9th Cir. 1982) ("Co-Petro"). Also, In re The Andersons, Inc., CFTC Docket No. 99-5 stating that "[t]he transaction must be viewed as a whole with a critical eye toward its underlying purpose without regard to whatever self-serving labels the instrument might bear."

[17] CEA, section 2(a)(1).

[18] Includes financial institutions, state or foreign regulated insurance companies, investment companies, commodity pools with assets exceeding $5,000,000, corporations, etc. with assets exceeding $10,000,000 (or with a net worth exceeding $1,000,000 if it enters into a risk management agreement), an employee benefit plan, a broker or dealer, an investment bank holding company, a futures commission merchant, an individual who has invested greater than $10,000,000 or $5,000,000 if it enters into a risk management agreement, an investment advisor, or other person that the CFTC determines to be eligible. See CEA, section 1a(18).

[19] Includes: (i) certain ECPs that have a demonstrable ability to make or take delivery of the commodity or incur related price risk or are dealers for such entities; (ii) ECPs, other than natural persons or certain government entities, that regularly enter into transactions to purchase or sell commodity or derivatives agreements and either (a) in the case of a collective investment vehicle who participants include persons other than qualified eligible persons, accredited investors or qualified purchasers, control at least $1,000,000,000 in assets or (b) is one of a group of

basis, or financed by the offeror, the counterparty, or a person acting in concert with the offeror or counterparty on a similar basis." The agreement, contract, or transaction need not be considered a contract of sale of a commodity for future delivery.[20]

Canadian Regulations

Currently in Canada, there is no general requirement that futures trade on exchange or be cleared. And with respect to the retail market, instead of requiring derivatives sold to this market be on exchange and cleared, they may in some cases be required to be sold with a prospectus. In the future, it appears that the only way that a derivative might be subject to mandatory clearing and platform trading would be through the final versions of NI 94-101 and CP 92-401. The Introduction to NI 94-101 suggests that regulators will prioritize reviewing derivatives subject to mandatory clearing in other jurisdictions first. However, because the structure of what has been proposed with respect to mandatory determinations mirrors only the treatment of swaps and not futures, we are concerned that treatment of futures products will be ignored in the review.[21] The CSA has suggested the same approach in CP 92-401.[22]

One consequence of this is that many products which are currently sufficiently standardized and liquid to be exchange traded and cleared, and mandated to be exchange traded and cleared in the U.S., may continue to trade in the bilateral market in Canada and avoid appropriate regulatory oversight which discourages the right market model. They may never be reviewed for mandatory clearing/trading by Canadian regulators because they will not receive attention from international regulators. Because such instruments are already classified as futures products in other countries, they will already be subject to mandatory clearing and trading. These differences between the Canadian and foreign derivatives regimes result in complexities that may create unnecessary barriers to cross-border trade. It is unclear why such inconsistencies would continue to exist, particularly given Canada's recent G-20 commitments.

Suggested Approach

Rather than using the term "exchange-traded contract", which describes a standardized contract that is already traded on an exchange and cleared, regulations should instead use a term with a definition comparable to futures contracts that is then required, pursuant to the CMA, to be traded on an exchange and cleared. This would mean that many products that are clearly

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persons under common control having at least $100,000,000 in total assets; or (iii) "an agricultural producer, packer, or handler…in connection with the line of business of the agricultural producer, packer, or handler." CEA sections 1a(17) and 2(a)(2)(c)(2)(D)(iv).

[20] CEA, section 2(a)(2)(c)(2)(D)(iii). Note that spot and forward transactions are still exempt from this requirement (CEA, section 2(a)(2)(c)(2)(D)(ii)). The Securities Exchange Commission ("SEC") has implemented similar requirements. Section 6(h) of the Securities Exchange Act of 1934 states that "[i]t shall be unlawful for any person to effect transactions in security futures products that are not listed on a national securities or a national securities association registered pursuant to section 15A(a)" and section 6(l) states that "It shall be unlawful for any person to effect a transaction in a security-based swap with or for a person that is not an eligible contract participant, unless such transaction is effected on a national securities exchange…" See also SEC v. Sand Hill Exchange, et al. for an example of an SEC enforcement action.

[21] NI 94-101 states that "[t]he Committee's goal is to harmonize the determination process in Canada with the relevant international standards on clearing determinations, which provide for: 1) a framework for consultation among authorities on mandatory clearing determinations, and 2) where practicable, an expeditious review of derivatives that are subject to a mandatory clearing determination in another jurisdiction."

[22] CP 92-401 states that "[t]he Committee is monitoring and will continue to monitor developments in the marketplace in respect of the trading mandate that has recently come into effect in the U.S. for certain interest rate and credit derivatives. The Committee will closely gauge the level of adoption and the consequences, intended or otherwise, of the DTF-trading mandate on OTC derivatives markets."

sufficiently standardized to be subject to mandatory exchange trading and clearing would not need to go through an intensive review process for a determination, but would automatically be presumed to be futures (and therefore subject to mandatory exchange trading and clearing). We also believe that, consistent with U.S. regulations, retail investors should not be permitted to trade either swaps or futures unless they are on exchange and cleared.

This proposed approach would ensure that Canadian regulations better meet Canada's G-20 commitments, ease doing business cross-border because of a more consistent approach with the U.S. and more efficiently utilize limited regulatory resources which may not be sufficient to examine all possible derivatives products in Canada for a determination under the final versions of NI 94-101 and CP 92-401. Given the substantial efforts made by the CSA to put in place regulations regarding clearing agency requirements, mandatory derivatives clearing and platform trading, we assume that the benefits to the market resulting from trading through exchanges and clearing transactions through clearing agencies are well understood. Requiring all futures to be exchange traded and cleared would also encourage greater standardization of derivatives rather than permitting growth in the trading of unstandardized derivatives in the OTC market.

The Financial Stability Board ("FSB") noted in a report (the "FSB Report") regarding OTC derivative market reform which set out recommendations regarding implementation of the G-20 commitments, that:

> [t]he proportion of the market that is standardised should be substantially increased in order to further the G-20's goals of increased central clearing and trading on organised platforms, and hence mitigate systemic risk and improve market transparency… To promote the G-20's vision for greater use of these safer channels, authorities must ensure that appropriate incentives for market participants to use standardised products are in place. In particular, authorities should counter incentives that market participants may have to use non-standardised products solely to avoid central clearing and trading requirements… Increased standardisation of contractual terms and operational processes should lead to ….greater availability of reliable pricing data for such products…facilitating automated processing of transactions; increasing the fungibility of the contracts which enables greater market liquidity; improving valuation and risk management; increasing the reliability of information; [and] reducing the number of problems in matching trades.[23]

The FSB Report recognizes the possibility that a desire to avoid mandatory platform trading and clearing may drive demand for bespoke products. "Dealers also may benefit from higher profits on bespoke products, and they may therefore be incentivised to create bespoke products to maintain greater opacity in pricing than they would otherwise be able to if the products were centrally cleared and traded on organised platforms."[24] In our view, it is likely that a product that is considered not sufficiently standardized for platform trading or clearing may be inappropriately complex for the retail market. Simply regulating an OTC derivative like a security and providing more documentation, through a prospectus or other form of documentation, to a retail investor regarding a highly complex product likely will not adequately address the potential risks posed.

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[23] Financial Stability Board, Implementing OTC Derivatives Market Reforms, 25 October 2010. Online: http://www.financialstabilityboard.org/wp-content/uploads/r_101025.pdf at pp. 1, 3, 4, 12.
[24] FSB Report, pp. 20-21.

One of the primary goals of the CCMRS is to promote financial stability. Increased derivatives standardization, mandatory platform trading and mandatory clearing have been recognized as among the key ways to achieve this goal. We respectfully submit that the Authority and/or the CSA should continue to make changes in the area of derivatives regulation to promote financial stability.

Consistency in Exclusions from the Derivatives Definition

The CMA jurisdictions have asked whether the Authority should regulate market conduct in all types of Exempt Derivatives or whether some or all types of Exempt Derivatives should be entirely excluded from capital markets regulation.[25] The CCMRS Regulation Commentary notes that "[t]he definition of 'derivative' in the CMA is broad enough to include some contracts and instruments that are not typically considered to be derivatives and for which full [dealer or adviser] regulation under the CMA may not be appropriate. Part 2 [Exempt Derivatives] of CMRA Regulation 91-501 [Derivatives and Strip Bonds ("CR 91-501")] proposes to tailor the application or regulatory requirements by exempting Exempt Derivatives from the prospectus and registration requirements."[26] Essentially these same exemptions apply to trade reporting and will likely apply to rules relating to mandatory clearing, segregation and portability and derivatives trading facilities. We believe that under the CMA, Exempt Derivatives should be excluded from the definition of derivative, particularly the commodity Exempt Derivatives,[27] as this approach would be consistent with the approach taken in the U.S., which exempts forward contracts from all regulation by the CFTC. Forwards are generally used for commercial rather than speculative purposes and as they involve physical delivery of the commodity, unlike financial derivatives, they do not pose broader systemic risk concerns. If it is unnecessary to report these transactions to regulators pursuant to CMRA Regulation 91-502 *Trade Repositories and Derivatives Data Reporting* ("CR 91-502") and unnecessary to register dealers dealing in such contracts pursuant to CR 91-501, it also would seem unnecessary to regulate these products if they trade on an exchange or clear through a clearing agency. They pose no additional risks on an exchange or through a clearing agency than they would through dealer trades or other bilateral trades.

Lack of Clarity

Certain terms relating to derivatives regulation were introduced in the proposed CMA with little clarity or context with respect to their definition, necessity and application. For example, large derivatives participant, designated derivative and prescribed derivative. While TMX Group may have concerns with respect to requirements that may be imposed upon these types of entities and instruments and which specific entities and instruments are so designated, it is difficult to provide meaningful feedback without further information. We understand that further criteria with respect to the definition of a large derivative participant will be set out at a later date. However, it is unclear that further guidance will be set out with respect to how an entity or product becomes prescribed or designated. The brief discussion with respect to these terms in the CMA commentary provides little clarity with respect to this matter. We believe that criteria should be set out to reduce the risk that the uncertainty in the law may lead to excessively cautious commercial behavior and disincentives to invest in Canada. Because it is unclear whether a new product or entity could be designated or prescribed, participants and recognized entities

[25] CCMRS Regulation Commentary, p. 78.
[26] *Ibid.*, p. 77.
[27] The exclusion set out in section 25(d) of CR 91-502.

may avoid entering into such businesses in Canada as the consequences and costs of doing so are too uncertain.

The distinction between derivative and security also requires further clarification. As the CCMRS Regulation Commentary notes, "[t]he definitions of 'security' and 'derivative' in the CMA are not mutually exclusive. A product may fall under both definitions. For example, an equity option or an investment contract could be both a derivative and a security. The CMA provides flexibility to categorize products to ensure they are regulated under the appropriate regime. At this stage, we have not attempted to categorize all products as either a security or a derivative. In cases where a product is both a security and a derivative, both securities and derivatives requirements would apply." Given the significant implications of categorizing a product as one or the other or both, categorization should be prioritized and clarified in the CMA itself, not on an ad hoc basis. Further, a derivative must not be classified as or regulated as a security unless it essentially has the same characteristics as a security. It is unclear why a derivative would be classified as a security under any other circumstance. While the approach taken by the CMA jurisdictions may be based upon the approach that already exists in certain of the CMA jurisdictions, an opportunity exists to appropriately modernize Canadian laws. As derivatives regulation is already in a state of change and development through the ongoing CSA OTC derivatives reforms, this is a particularly appropriate time to consider certain aspects of derivatives framework.

Trade Reporting Regulations Issues

Below we have set out our concerns with respect to CR 91-502. While we recognize that these concerns relate to sections which are present in existing provincial derivatives data reporting rules, the rules are still being adjusted and we believe these suggestions would improve those rules and are either consistent with current interpretation or not a burden for the market to adjust to.

Block Trades

To ensure a clear understanding that is consistent with international practice with respect to the application of Part 3 in section 25(g) of CR 91-502, which states that Part 3 does not apply to a transaction in a contract or instrument that is "traded on an exchange", we would propose ensuring that the language makes it clear that block trades entered on an exchange are considered to be traded on an exchange. We understand that the provision may currently be interpreted as such, but it would provide greater certainty to the market if that interpretation were clear from the plain language of the regulation.

We understand that the purpose of section 25(g) is that if a derivative is traded on a recognized exchange, the requirement for timely market data is already met, thus making the requirement to report such trades redundant. From a policy perspective, the carve-out should also include any OTC derivatives transactions that: meet or exceed specified volumes, are entered into the exchange, and are subject to the rules of a recognized exchange ("Block Transactions"). Block Transactions are subject to the rules of the applicable recognized exchange, including market surveillance and oversight, and are disclosed to Canadian regulators in the same manner as exchange-traded transactions.

The proposed amendment would not only clarify the interpretation of section 25(g) and better reflect the policy considerations underlying this section, but it would also harmonize with the approach implemented by other foreign commodities regulators. By way of example, pursuant to

the CEA, a Block Transaction is considered to be an exchange transaction so long as it is subject to the rules of a board of trade and ultimately consummated through and recorded by the exchange.[28]

As Block Transactions are considered exchange transactions in other key foreign jurisdictions, we propose that section 25(g) of CR 91-502 be amended to be more similar to the language quoted above to provide comfort that this treatment of Block Transactions may continue across Canadian markets. This will minimize the potential for confusion, particularly in the context of markets that operate on a North American or global basis.

Alternative Trading Systems

The Companion Policy to CR 91-502 makes clear that derivatives trading facilities ("DTFs"), swap execution facilities, multilateral trading facilities and organized trading facilities are not considered exchanges for the purposes of section 25(g) of CR 91-502. Clearly, only those derivatives traded on exchanges, not alternative venues, are intended to be captured by this section. For further clarity, given that a number of specific types of alternative venues are explicitly excluded, ATSs should also be explicitly excluded from this provision.

Novated and Assigned Transactions

Pursuant to CR 91-502, "transaction" means any of the following:

> (a) entering into, assigning, selling or otherwise acquiring or disposing of a derivative;
>
> (b) the novation of a derivative; **...**

In limited circumstances, products that are exchange traded and cleared are assigned and novated by a counterparty, such as in connection with, or a result of, a merger, business acquisition, asset purchase or similar non-recurring transactions between two or more entities. In the context of a business acquisition, the novation occurs off exchange to the acquirer of the business. Pursuant to the definition of transaction, this would require reporting. This may be an issue for both the clearing agency and the other counterparty as neither party may be set up to report because the nature of their trading activities do not normally warrant reporting.

The companion policy to CR 91-502 notes that "[e]xchange-traded derivatives provide a measure of transparency to regulators and to the public, and for this reason these transactions are not required to be reported." As all characteristics with respect to which the exchange provides transparency of a transaction of the type described above would remain the same, the same logic that applies to omitting exchange-traded transactions from reporting requirements should apply to omitting assignment and novation transactions of the type described above from reporting.

In the case of an assignment or novation of trades, the only change to the position is the holder of the position. It is unclear from a policy perspective why it would be necessary to report such a trade particularly when occurring in the context of an asset purchase of a business. In addition, the details regarding the assignment of positions are captured by the exchange in its records.

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[28] See the excerpt of section 6(a) of the CEA under the heading *Derivatives Regulation – Meeting Canada's G-20 Commitments – Futures Definition and Treatment*.

Should the exchange be required to report the assignment or novation, it would be unrelated to any previous report, as the original report was not on record with the trade depository. In this case, the benefit to the report of an assignment or novation is vague.

We ask that clarity be provided in either the instrument or the companion policy to permit these assignment and novation transactions to take place without requiring reporting.

Interim Dealer Registration and OTC Derivatives Treatment

We believe that the Authority should refrain from establishing dealer registration rules until the CSA dealer registration regime has been finalized pursuant to the efforts of the CSA OTC derivatives reform committee rather than putting in place a temporary, partial rule now that may be subject to change once the CSA rule, which is also currently in development, is finalized. This would be better for market certainty and national harmonization of derivatives regulation. A temporary dealer registration regime may create unnecessary costs and confusion for dealers that will need to try to comply with both regimes or will need to invest to comply with the CCMRS proposal, but then potentially reverse course to comply with the CSA rule instead once it is finalized. Waiting for a final CSA dealer registration regime would also be consistent with the approach the CCRMS has taken with respect to other OTC derivatives issues such as those relating to mandatory clearing, segregation and portability and derivatives trading facilities. Waiting for the CSA rule would also be consistent with the objectives of maintaining continuity and minimizing disruption for market participants in the transition to the CCMRS.[29]

CCMRS Regulation Commentary notes that "in CMR Jurisdictions, NI 41-101 applies to OTC derivatives because, in CMR Jurisdictions, OTC derivatives are being treated as securities for the purposes of the prospectus requirements until a comprehensive regulatory regime is implemented for OTC derivatives." For the same reasons as noted above – namely confusion and costs that may deter market participants from entering the market – we believe that an interim regime is inappropriate and for the reasons set out under "Meeting Canada's G-20 Commitments", we do not believe that use of a prospectus is the appropriate way to sufficiently address the risks associated with derivatives, nor is it consistent with how they are regulated in other key jurisdictions such as the U.S.

Dealer Regulation

Registered Derivatives Dealers as Local Counterparties

Pursuant to CR 91-502, a "local counterparty" includes, among other entities, a counterparty registered under capital markets law as a derivatives dealer or in an alternative category as a consequence of trading in derivatives. This is not a local counterparty pursuant to proposed Multilateral Instrument 96-101 *Trade Repositories and Derivatives Data Reporting,* which the British Columbia Securities Commission is participating in. It seems unnecessary to call a dealer a local counterparty to a transaction solely because it is registered in a jurisdiction if the transaction has no other connection to the jurisdiction and may create significant additional reporting obligations to regulators in jurisdictions with no connection to the transaction. We believe that this prong of the definition of local counterparty should be removed.

[29] Commentary on Draft Initial Regulations for the Cooperative Capital Markets Regulatory System. August 25, 2011, p. 68

Registration Exemptions for Certain Products When Dealing with Certain Clients

Part 3 [Exchange Contracts] of CR 91-501 proposes, subject to certain conditions, that the dealer registration requirement would not apply to a person in respect of a trade in a non-Canadian exchange contract with a permitted client. Part 4 [Over-The-Counter Derivatives] of CR 91-501 proposes that the registration requirement and the prospectus requirement would not apply in respect of a trade in an OTC derivative where each party to the trade is a permitted client or a qualified party, each acting as principal. These exemptions create an uneven playing field for different types of products (non-Canadian exchange contracts, Canadian exchange contracts and OTC derivatives), with respect to dealings with different classes of market participants (exemption available when dealing with a permitted client only for non-Canadian exchange contracts and when dealing with both a permitted client or a qualified party for OTC products, while no exemption available when dealing with either a permitted client or a qualified party for Canadian exchange contracts). No policy rationale was provided for treating these types of products and clients differently other than the fact that some CMR Jurisdictions had been granting similar exemptions in the past. The underlying policy rationale that might justify such an approach is unclear, especially with regard to Canadian exchange contracts given these products are more highly regulated in Canada than non-Canadian exchange contracts and OTC derivatives. We believe that any registration exemption should apply consistently with respect to all types of products and to the same category of clients.

Absent a clear policy rationale justifying a different approach to registration exemptions based on products and types of clients, we believe that the current proposals create an uneven playing field whereby certain exempt dealers will be incentivized to deal with certain classes of clients, for certain types of products.

TMX Group has thoroughly considered the CCMRS proposal. We appreciate the significance of the CMA and have provided comments with a view to being helpful in its implementation, having at the forefront the health and welfare of the Canadian capital markets. Now is the time to ensure that the CCMRS legislative framework is as robust and competitive as possible. It is vital that we use this opportunity to clearly position Canada for economic success with regulatory underpinnings that will support and foster continued growth in our capital markets. Given the importance of this proposal and the complexity of this transition, it is our strong recommendation that regulators publish for comment a revised CMA and regulations, taking into account comments received during this process. TMX would be pleased to discuss our comments at greater length. Please contact the undersigned if you have any questions regarding our submission.

Respectfully submitted,

Cheryl Graden