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BY E-MAIL

Cooperative Capital Markets Regulatory System
commentonlegislation@ccmr-ocrmc.ca

Dear Sirs/Madames:

RE: Comments regarding the proposed Cooperative Capital Markets Regulatory System and related legislation published September 8, 2014

TMX Group Limited ("TMX Group") welcomes the opportunity to comment on the proposed Cooperative Capital Markets Regulatory ("CCMR") system and the related proposed legislation – the Provincial Capital Market Act ("PCMA") and the federal Capital Markets Stability Act ("CMSA"). TMX Group is supportive of all efforts to make Canada's capital markets more efficient. With respect to the PCMA, while it is difficult to assess its potential impact without the proposed regulations, we have provided preliminary comments and requested further clarity below. In our view, the proposed CMSA raises a number of significant issues. We are particularly concerned about the potential impact the proposed legislation may have upon Canada's global competitiveness. While we have included our most substantial concerns with suggested amendments in the text of this letter, we have also sought further clarity and addressed numerous additional issues in the attached Appendix.

TMX Group

TMX Group's key subsidiaries operate cash and derivative markets for multiple asset classes, including equities, fixed income and energy. Toronto Stock Exchange, TSX Venture Exchange, TMX Select, Alpha Exchange, The Canadian Depository for Securities Limited ("CDS"), Montréal Exchange ("MX"), Canadian Derivatives Clearing Corporation ("CDCC"), Natural Gas Exchange Inc. ("NGX"), BOX Options Exchange, Shorcan, Shorcan Energy Brokers, Equicom and other TMX Group companies provide listing markets, trading markets, clearing facilities, data products, and other services to the global financial community. TMX Group is headquartered in Toronto and operates offices across Canada (Montréal, Calgary and Vancouver), in key U.S. markets (New York, Houston, Boston and Chicago) as well as in London, Beijing, Singapore and Sydney.

TMX Group brings a unique perspective to review of the proposed legislation through its central role in Canadian capital markets. Its interests are aligned with regulators as it is important for its business that Canadian capital markets remain stable and efficient and that they continue to be globally competitive. TMX Group's interests are also aligned with capital market participants as its business relies upon their continued confidence and participation in Canadian capital markets. As the owner of Canada's major clearing agencies and exchanges, TMX Group is likely more directly impacted by the proposed legislation, particularly the CMSA, than any other market participant. As such, TMX Group is uniquely positioned to comment on the legislation and has a strong vested interest in ensuring that the legislation can achieve its intended objectives without unnecessarily obstructing capital market efficiency.

Comments

TMX Group supports regulators' stated objectives of fostering more efficient and globally competitive capital markets in Canada, facilitating capital raising, protecting investors and enabling Canada to play a more empowered and influential role in international capital markets regulatory initiatives. TMX Group recognizes that there are aspects of the proposed legislation that will assist with achieving these objectives, but feel that there are others that may impede their achievement. Our primary concerns with respect to the proposed CCMR system relate to the following:

I. Impact upon capital market efficiency
II. Broad powers of the Authority
III. Level playing field concerns
IV. Impact upon international equivalence

Throughout the letter we have set out specific issues and recommendations on how to improve the proposed CCMR system to better achieve its objectives. Generally, we have recommended: (i) that regulators provide greater clarity to the markets on a number of issues through either amendments to the legislation, regulations or published guidance; (ii) that powers granted to the Authority be reduced to be more consistent with powers granted to comparable foreign systemic risk regulators; (iii) that regulators ensure that foreign entities are subject to the same level of regulatory oversight as domestic entities, particularly where domestic regulation is stricter than foreign regulation; and (iv) that coordination and interface mechanisms among various regulators be explicitly considered and set out in the legislation.

I. Impact Upon Capital Market Efficiency

The proposed CCMR system represents a major overhaul of the existing system of securities and systemic risk regulation in Canada. These changes may lead to considerable uncertainty in Canadian capital markets for a long period as markets wait for clarity regarding the regulations, how the Authority will interact with other regulators and further interpretive guidance and jurisprudence with respect to the many new or amended regulations.

TMX Group is particularly concerned that the following factors will negatively impact capital market efficiency:

a. Duplication and lack of coordination
b. Potential termination or amendments to lead regulator model and existing memoranda of understanding
c. Excessive and duplicative information collection
d. Lack of a clear plan regarding regulatory changes

Below we discuss these issues and offer potential solutions.

a. Duplication and Lack of Coordination

Duplicative Regulations and Regulators

TMX Group is concerned that requirements under the CMSA unnecessarily duplicate, and potentially conflict with, certain TMX Group entities' existing obligations pursuant to recognition orders and regulations by non-participating provinces and the Bank of Canada. There may also be duplication between the CMSA and the PCMA.[1]
For those entities that are based in and/or recognized in a non-participating province and/or by the Bank of Canada, such as NGX, CDCC, MX and CDS, the system introduces the possibility of an unnecessary layer of regulatory oversight with respect to their business, products, practices and counterparties if deemed systemically important. Even for those entities recognized by the Authority under the PCMA and subject to, for example, clearing agency recognition requirements under the PCMA, they may also be recognized by the same Authority as a clearing house under the CMSA and be subject to a second recognition order from the same regulator. In practice, for CDS, for example, the CCMR system may require recognition as a clearing agency by the Authority under the PCMA, designation as a systemically important clearing house by the Authority under the CMSA, recognition as a clearing house by the Autorité des marchés financiers, and designation by the Bank of Canada under the *Payment Clearing and Settlement Act*[2]. This would neither simplify the regulatory oversight CDS is subject to nor provide additional protection to the capital markets and may have a subsequent negative impact on the market participants it serves because of additional costs and complexity without any clear incremental benefit.

Certain TMX Group entities that appear likely to be captured under the CMSA must already submit proposed rule changes to multiple regulators and approvals can already take up to several months and sometimes years, which creates uncertainty, limits responsiveness, diverts resources and ultimately makes Canada's capital markets less attractive. Additional regulation under the CMSA will only exacerbate this issue.

Regulations enacted under provincial securities law in non-participating jurisdictions or the PCMA in participating jurisdictions may overlap or conflict with the CMSA. The powers of the Bank of Canada under the PCSA to designate and regulate the operations

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[1] For example, under the PCMA the Chief Regulator may make any decision respecting a clearing agency's by-laws, policies, procedures, interpretations or practices and the manner in which the entity carries on business. Under the CMSA, the Authority may prescribe, prohibit or restrict a systemically important clearing house's policies and procedures for risk management and internal controls, margin and collateral.
[2] S.C. 1996, c. 6, Sch. ("PCSA").

of clearing and settlement systems that pose systemic risk may also overlap or conflict with the CMSA.[3] Orders from the Authority may conflict with orders from other regulators. It is unclear which would take precedence. There is duplication among regulations and regulatory authorities and little clarity regarding co-ordination. While the Memorandum of Agreement Regarding the Cooperative Capital Markets Regulatory System provides that the Authority will use its best efforts to negotiate and implement an interface mechanism with non-participating provinces, as discussed below, there is little guidance in either this Agreement or the legislation as to how this will occur. It is possible to envision the Authority asserting jurisdiction and a non-participating regulator disagreeing. The risks are exacerbated by the fact that the definitions in the PCMA and CMSA are not harmonized. The risk that jurisdictional issues could hold up business matters may deter participation in Canadian capital markets due to the uncertainty of unpredictable delays and uncertainty with respect to which regulations may be applied.

Lack of Coordination

The Authority governing the CMSA is comprised only of the Minister of Finance and representatives from the provinces opting into the CCMR system. We understand that the CMSA does address some forms of coordination, but these provisions do not provide sufficient clarity or comfort with respect to this issue. We note in particular that pursuant to the CMSA:

- the Chief Regulator may designate persons or classes of persons to exercise powers referred to in the designation for the purposes of the administration and enforcement of the Act;[4]
- the Authority requires the Bank of Canada's concurrence before designating a clearing house as systemically important and before making related regulations;[5] and
- "[in] fulfilling [its] mandate, the Authority must coordinate, to the extent practicable, its regulatory activities with those of other federal, provincial and foreign financial authorities so as to promote efficient capital markets, to achieve effective regulation and to avoid imposing an undue regulatory burden."[6]

TMX Group is supportive of the Authority's intentions as set out in the quotation above, but we are concerned that the objectives of coordination may not be realized because the powers granted to the Authority do not explicitly require it to coordinate and political differences may make coordination challenging at times. The Authority, for example, may collect any information from any person without the necessity of coordinating with other regulators first and may impose wide-ranging regulations upon any entity without the need to coordinate with other regulators. The intended objectives set out in the quotation above will be challenging to enforce because of the way the CMSA is otherwise structured throughout. It is important for there to be specific, mandatory requirements to coordinate and greater detail regarding how coordination will work set out in the legislation. Securities regulators in Alberta and Quebec in particular collect considerable information and have considerable insight into the entities under their jurisdiction. Formally involving those regulators under the CMSA would lead to better and more efficient regulation. Our suggestions below provide further detail.

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[3] See also Section II.a Systemic Risk Definition below.

[4] CMSA, ss. 36 and 37.

[5] CMSA, s.22.

[6] CMSA, s.6(2).

Suggestions for Improvement

TMX Group proposes the following changes to the CCMR system to address the concerns set out above:

(i) Systemic risk regulation that clearly coordinates the work of existing regulators to the greatest extent possible, rather than duplicating existing regulatory functions;

(ii) Streamlining regulation of certain entities, products or activities if they are deemed systemically important (*i.e.*, so that they are regulated by a minimum of regulators);

(iii) Setting out more specific detail regarding how the Authority will coordinate with the securities regulators in the non-participating provinces and with the Bank of Canada; and

(iv) Setting out clear distinctions or limitations in the legislation to clarify which aspects of systemically important entities, products or activities are regulated by particular regulators.

Both the US and the European Union have applied a coordinated regulatory approach to systemic risk that minimizes regulatory overlap and explicitly incorporates and recognizes the abilities of existing regulators. For your reference, as examples of how such suggestions could be and have been implemented, we have set out some of the ways in which these jurisdictions have applied the suggestions above.

United States

In the United States, the Financial Stability Oversight Council ("FSOC") is the systemic risk regulator and is charged with monitoring systemic risk and coordinating responses.

(i) The FSOC operates under a committee structure, chaired by the Secretary of the Treasury, that is designed to promote shared responsibility among the member agencies and use the expertise that already exists at each agency.

(ii) The FSOC is not empowered with the resources and jurisdiction to act as a primary regulator. It acts through existing regulators rather than creating an additional layer of regulation.

(iii) Its general duties involve collecting and coordinating data, facilitating information sharing and coordination among federal and state financial regulators, monitoring domestic and financial regulatory proposals and developments, identifying gaps in financial regulation, making recommendations to Congress about ways to enhance financial stability, designating certain systemically important entities and making recommendations to member agencies on supervisory priorities and principles.[7]

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[7] See Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub.L. 111–203, H.R. 4173 (the "Dodd Frank Act"), s.112(a)(2).

(iv) The Council consists of 10 voting members including the Federal Reserve, the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC"), among others.[8]

(v) In the United States, if a financial market utility designated as systemically important by the FSOC is subject to the jurisdictional supervision of more than one agency (i.e., the SEC and CFTC), then the agencies must agree on one agency to act as the Supervisory Agency and if they cannot agree, the FSOC will decide.[9]

(vi) Throughout Titles I and VIII of the Dodd-Frank Act, numerous provisions set out how the FSOC or Federal Reserve will work with or rely upon other regulatory agencies.

Europe

In Europe, the European Systemic Risk Board (the "ESRB") is responsible for macro-prudential oversight. The European System of Financial Supervision ("ESFS") consists of the ESRB and three "micro-supervisory authorities" ("ESAs"): the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority ("ESMA").

The ESRB itself has no legal personality. The ESRB issues warnings, and where it deems necessary, recommendations either of a general or a specific nature to the European Union as a whole, to one or more Member States, to one or more of the ESAs or to one or more of the national supervisory authorities. It also monitors compliance with such warnings and recommendations. Recipients of recommendations (*i.e.*, other regulators) must act on the recommendations or provide an adequate justification in case of inaction. As in the United States, the powers granted to the systemic risk regulator are significantly more limited than those granted to the Authority under the CMSA.

The regulatory system for oversight of systemic risk in Europe was based upon a high level report commissioned in November 2008 (the "EU Report"). The EU Report noted that "macro-prudential oversight is not meaningful unless it can somehow impact on supervision at the micro level whilst micro-prudential supervision cannot effectively safeguard financial stability without adequately taking account of macro-level developments."[10] The preamble to the European Regulation further notes that "[t]he participation of micro-prudential supervisors in the work of the ESRB is essential to ensure that the assessment of macro-prudential risk is based on complete and accurate information about developments in the financial system."[11] This statement applies to the Canadian context as well. While the participating provinces would have the benefit of both macro and micro prudential supervision by the Authority pursuant to the CCMR system, the non-participating provinces would not have the benefit of information

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[8] See Dodd-Frank, s. 111.

[9] Dodd-Frank Act, s. 803(8)(B).

[10] REGULATION (EU) No 1092/2010 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board ("Regulation (EU) No 1092/2010"), preamble, s.13.

[11] *Ibid.*, preamble, s.24.

obtained through micro-prudential supervision contributing to systemic risk regulatory decisions by the Authority.

b. Potential Termination or Amendments to Lead Regulator Model and Existing Memoranda of Understanding

TMX Group is extremely concerned about the consequences of the CCMR system on existing cooperative agreements among regulators. It is unclear whether or how (i) the Lead Regulator model set out under the Memorandum of Understanding Respecting the Oversight of Exchanges and Quotation and Trade Reporting Systems and (ii) the cooperative model set out under the Memorandum of Understanding Respecting the Oversight of Certain Clearing and Settlement Systems will continue under the proposed CCMR system; (iii) the Authority will be the successor to the securities regulators from the participating provinces in terms of exempting/recognizing certain registrants including TMX entities; and (iv) whether these MOUs, if they continue, will have to be renegotiated imposing significant costs and inefficiencies. These lead regulator models are of critical importance to the efficient functioning of exchanges and clearing and settlement systems in Canada. We are also concerned that efforts to establish a lead regulator model for clearing agencies may stall under this new system. The lead regulator model has been very beneficial to TMX and capital markets in reducing unnecessary regulatory burden while still maintaining comprehensive regulatory oversight.

TMX Group would support the Authority stepping into the shoes of each of its predecessor regulators – (*i.e.* the securities regulators in each of the participating provinces) and assuming such predecessor's role in any MOU or recognition/exemption order.

c. Excessive and Duplicative Information Collection

While TMX Group supports the goal of enabling information collection for effective oversight, it submits that further parameters should be set around information collection by the Authority under the CMSA. The Authority has been granted extremely broad powers under sections 36 and 37 to designate any person to: (i) review the business and conduct of any person for the purpose of verifying compliance with the Act; and (ii) to require any person to provide any records (defined as any thing containing information, regardless of its form or content) or other things in their possession or control, including filings, reports or other information provided to any other regulatory agency whether within or outside Canada. Such person may also be granted broad powers to enter a place that they have reasonable grounds to believe contains anything that is relevant to the review. Entities that do not comply with requests would be subject to administrative monetary penalties.

Given the extensive information market participants already provide to local securities regulators, the Bank of Canada and OSFI, this power should be limited to impose an obligation upon the Authority to first seek the information internally and from other regulators before seeking that information directly from any person. Under existing regulatory requirements and oversight by securities regulators and the Bank of Canada and through compliance with the Principles for Financial Market Infrastructures ("PFMIs") published by the then Committee on Payment and Settlement Systems (now Committee on Payments and Market Infrastructure) and the Technical Committee of the

International Organization of Securities Commissions, derivatives data reporting regulations and the proposed mandatory derivatives clearing regulations, very extensive information is already being provided to regulators. Requiring capital markets participants (or any other entities as the CMSA allows the Authority to obtain information from anyone) to continuously provide the same data to multiple regulators is inefficient and expensive for everyone. We note in particular that certain reporting requirements require infrastructure development costs to enable reporting.

In the United States, the FSOC is authorized to require any financial market utility (includes clearing agencies) or financial institution (similar to capital markets intermediaries) to submit such information as the FSOC may require for the sole purpose of assessing whether that entity is systemically important, but only if the FSOC has a reasonable case to believe that it meets the standards for systemic importance.[12] The FSOC does not have the authority to impose administrative monetary penalties on entities that do not comply, however. Further, pursuant to a Dodd Frank Act provision titled "Advance Coordination", before requesting any material information from, or imposing reporting or recordkeeping requirements on, any financial market utility or any financial institution engaged in a payment, clearing or settlement activity, the FSOC must coordinate with the primary regulator for such entity to determine if the information is available from or may be obtained by that regulator in the form, format or detail required.[13]

In Europe, before requesting information, the ESRB must first take account of existing statistics produced, disseminated and developed by the European Statistical System and the ESCB. If it is not available or not timely made available, the ESRB may request the information from the ESCB, the national supervisory authorities or the national statistics authorities. If it is still unavailable, it may request the information from the Member State concerned. If the ESRB requests information that is not in summary form, the request must explain why such data on a particular entity is deemed to be systemically relevant and necessary. Before each request not in summary form, the ESRB must consult the relevant European Supervisory Authority to ensure that the request is justified and proportionate.[14]

If the Authority is going to regulate systemic risk nationally and to request information from all entities that fall under its jurisdiction, at a minimum information sharing similar to the process in the US and the European Union should be put in place among regulators to prevent inefficiency and duplication and encourage coordination to the benefit of Canadian capital markets overall.

d. Lack of a Clear Plan Regarding Regulatory Changes

As noted, the proposed CCMR system and related legislation and regulations represent a substantial departure from the existing Canadian regulatory system and will have wide-ranging consequences. While the public is aware that it should expect the publication of initial CCMR system regulations in December, there is still considerable uncertainty with respect to: (i) the timeline for all regulatory proposals and final regulations; (ii) the effect

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[12] Dodd-Frank Act, s. 809(a).

[13] Dodd-Frank Act, s. 809(c)(1).

[14] Regulation (EU) No 1092/2010.

of the proposed CCMR system on existing regulations, rules and national or multilateral instruments; and (iii) how relevant regulators will coordinate.

Capital market participants need greater 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 in the market. While the market awaits clarity, this may cause market participants to postpone transactions in Canada or make use of capital markets in other jurisdictions.

Further, the public has been given the opportunity to comment on the proposed CCMR system and related legislation, but without the regulations and with so many high level issues still unclear, it is difficult to fully assess the proposed legislation and provide meaningful commentary. Once further details are provided, market participants may have considerable additional commentary regarding the legislation itself.

TMX Group suggests that the following specific actions in the near future would provide greater certainty and stability to capital market participants and allow for more constructive commentary in response to further proposed regulations:

(i) Publication of a more detailed timeline of what regulations will be proposed, when they will be proposed and when they will be finalized;

(ii) Publication of guidance regarding the impact of the proposed CCMR system on existing and proposed rules, regulations and instruments (*i.e.* which, if any, will continue to exist, which will be replaced or repealed) as well as more details on proposed changes to enable meaningful comments and consideration;

(iii) Publication of guidance regarding how and to what extent the Authority will work with securities regulators in non-participating provinces, the Bank of Canada, OSFI and any other relevant regulators following implementation of the CCMR system. To the extent further guidance on this matter is being developed in the regulations, these regulations should be prioritized; and

(iv) Postponing the enactment of the CMSA and PCMA until further guidance regarding the matters listed above has been provided to the market and the market has had the opportunity to comment on the proposed legislation with the benefit of the additional guidance.

II. Excessively Broad Powers of the Authority

The scope of the powers granted to the Authority under the CMSA are extremely broad and appear to extend beyond those we believe were intended by the Supreme Court in its national regulator decision[15] and beyond what has been granted to systemic risk regulators in other jurisdictions.

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[15] *Reference re Securities Act*, 2011 SCC 66, [2011] 3 S.C.R. 837.

a. Systemic Risk Definition

We understand that the origin of the CCMR system as proposed was the 2011 Supreme Court decision that found that while the federal government cannot govern all aspects of securities law, as "[t]hese matters remain essentially provincial concerns falling within property and civil rights in the provinces and are not related to trade as a whole," (i) "[t]he need to prevent and respond to systemic risk may support federal legislation pertaining to the national problem raised by this phenomenon..."[16] and (ii) "[b]y analogy with Statistics Canada, it might be argued that broad national data-collecting powers may serve the national interest in a way that finds no counterpart on the provincial plane."[17]

The Supreme Court referred to the following definition of systemic risk in making its decision: "risks that occasion a 'domino effect' whereby the risk of default by one market participant will impact the ability of others to fulfil their legal obligations, setting off a chain of negative economic consequences that pervade an entire financial system (M. J. Trebilcock, National Securities Regulator Report (2010))...By definition, such risks can be evasive of provincial boundaries and usual methods of control..."[18] This is similar (though more general) to the definition of systemic risk used in the PCSA where it is defined as "the risk that the inability of a participant to meet its obligations in a clearing and settlement system as they become due or a disruption to a clearing and settlement system could, through the transmittal of financial problems through the system, cause (a) other participants in the clearing and settlement system to be unable to meet their obligations as they become due, (b) financial institutions in other parts of the Canadian financial system to be unable to meet their obligations as they become due, or (c) the clearing and settlement system's clearing house or the clearing house of another clearing and settlement system within the Canadian financial system to be unable to meet its obligations as they become due." Both definitions incorporate the concept of participant defaults and a domino effect.

Pursuant to the CMSA, "systemic risk related to capital markets means a threat to the stability or integrity of Canada's financial system that originates in, is transmitted through or impairs capital markets and that has the potential to have an adverse effect on the Canadian economy."[19] This definition is much broader than the Supreme Court's and does not require risk of failure of any entity. The threshold of threat, impairment and potential adverse effect under the CMSA is much lower and the scope of the CMSA is therefore much broader than the Supreme Court's with respect to the role for federal regulation in the area of systemic risk. The definition is also broader than that set out under the PCSA which may result in a clearing house being found to potentially create systemic risk under the CMSA, but not under PCSA which would likely be a confusing and unintended outcome.

TMX Group submits that the definition of systemic risk should be amended to be more consistent with either the definition used by the Supreme Court.

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[16] *Ibid.*, para. 128.
[17] *Ibid.*, para. 105.
[18] *Ibid.*, para 103.
[19] CMSA, s. 3(1).

b. General Scope of the Act

The powers of the Authority to designate the contemplated wide range of entities, products and practices as potentially systemically important under the CMSA appear broader than necessary. The Supreme Court decision does not contemplate that systemic risk could potentially be generated by such a wide range of entities. The US system similarly engages a narrower range of entities. Under the CMSA, the Authority has the power to declare the following to be systemically important:

- Trading facilities (which appears to be intended to capture exchanges);
- Clearing houses;
- Credit rating organizations;
- Benchmarks;
- Capital market intermediaries (including dealers, issuers whose primary purpose is to invest money from its security holders, pension funds, investment managers and prescribed capital market intermediaries);
- A class of securities or derivatives; and
- "a practice" (not defined).

Once an entity is designated, the Authority has extremely broad powers to supervise key aspects of its business and it is unclear to what extent designations may be rescinded or appealed. Section 100 of the CMSA empowers the Authority and Chief Regulator to revoke or vary any of their decisions if they consider that doing so would not be contrary to the Act, but little detail is provided regarding how and when this power is intended to be used. TMX Group submits that the ability to rescind and appeal decisions when systemic risk does not exist should be more clearly provided in the CMSA.

In the US, for example, pursuant to a section titled "Rescission of Designation" in the Dodd-Frank Act, FSOC "shall rescind a designation of systemic importance for a designated financial market utility [includes clearing houses] or designated activity if the Council determines that the utility or activity no longer meets the standards for systemic importance...Upon rescission, the financial market utility or financial institutions conducting the activity will no longer be subject to the provisions of this title or any rules or orders prescribed under this title."[20] Also, before making any determination regarding designation or rescission, FSOC must provide the entity being evaluated with advance notice to allow the entity to request a hearing to demonstrate that the proposed designation or rescission is not supported by substantial evidence should the entity disagree with the FSOC's determination.[21]

Exchanges

The common view is that exchanges do not cause systemic risk. The Authority should not therefore be empowered to find them systemically important. The failure of an exchange is unlikely to create systemic risk as it does not take title in securities/derivatives transactions *i.e.*, the risk lies at the clearing agency level. This

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[20] Dodd-Frank Act, s.804(b).

[21] Dodd-Frank Act, s. 804(c)(2).

means that if an exchange failed, contracts between parties on either side of a transaction would remain in effect and outstanding contracts would be honoured. Further, the exchange business carries lower risk than the activities of other capital market participants. An exchange cannot engage in the types of activities carried out by a clearing agency, dealer or bank. It cannot guarantee transactions or engage in the types of activities where the imposition of minimum capital requirements may improve its safety and soundness. Exchanges do not own the underlying products or securities nor are they involved in payment and settlement. The primary function of the exchange is to provide a platform to foster liquidity by bringing sellers' and buyers' orders together and providing transparency on market prices. It is a key infrastructure in the capital markets, but does not itself create systemic risk. Exchanges are also already stringently regulated at the provincial level to ensure financial viability.

In the United States, the FSOC is empowered to designate "financial market utilities" as systemically important. This term includes clearing agencies, but exchanges are specifically excluded from FSOC jurisdiction[22] as they do not give rise to systemic risk.

Other Categories

TMX Group submits that further consideration should be given to whether every category under the CMSA has the potential to create systemic risk. We submit that in general, the scope of entities, products and practices captured is broader than necessary leading to unnecessary regulation, duplication and inefficiency without corresponding benefit.

In the United States, rather than systemic risk regulation of all "practices", oversight regulation by the FSOC relates to particular practices by particular types of entities. With respect to regulation of clearing houses, it is confined to "payment, clearing and settlement activities".[23] The FSOC does not have the authority to designate credit rating organizations, benchmarks or classes of securities or derivatives as systemically important. In Europe, pursuant to systemic risk legislation, the definition of systemic risk notes that while certain entities may be systemically important, there is no reference to products or practices.

III. Level Playing Field Concerns

TMX Group is concerned that certain of its entities and products may be designated as systemically important under the CMSA, while those of domestic and foreign competitors in the same business may not.

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[22] Dodd-Frank Act, s.803(5)(B) and (6)(B). "The term 'financial market utility' does not include— (i) designated contract markets, registered futures associations, swap data repositories, and swap execution facilities registered under the Commodity Exchange Act (7 U.S.C. 1 et seq.), or national securities exchanges, national securities associations, alternative trading systems, security-based swap data repositories, and swap execution facilities registered under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), solely by reason of their providing facilities for comparison of data respecting the terms of settlement of securities or futures transactions effected on such exchange or by means of any electronic system operated or controlled by such entities, provided that the exclusions in this clause apply only with respect to the activities that require the entity to be so registered;"

[23] Dodd-Frank Act, s.804.

Provincial securities regulators have historically tended to rely upon home country regulation of foreign clearing agencies, SEFs and exchanges in granting orders to exempt such entities from recognition requirements. As the proposed CMSA applies to a wider range of entities and products and imposes a greater reporting burden upon capital market participants than comparable foreign systemic risk regulation, this would subject TMX Group to a higher regulatory and compliance burden than its peers and impede its ability to compete on a level playing field. Further, this may result in a shift in financial activity to entities/products/practices that are not deemed (or not yet deemed) systemically important or risky as this may be less costly and result in a lower regulatory burden upon participants. Creating a regulatory regime where market activity may shift to avoid dealing with systemic risk regulation is neither optimal for capital market efficiency nor for domestic competitiveness. The approach taken should be designed to promote, not derogate from, the existing Canadian capital markets.

TMX Group submits that in applying the CMSA:

(i) foreign regulation should not be relied upon with respect to foreign entities and products which are not subject to systemic risk regulation in their home jurisdiction, and to the extent that such entities/products could pose systemic risk, they should be regulated in Canada in the same manner as domestically regulated entities/products which are deemed to pose systemic risk; and

(ii) differences between regulations imposed upon systemically important entities and others should be minimal and differences should exist only where thorough analysis concludes such differences are essential to the stability of capital markets so as not to inappropriately distort market activity.

IV. Impact Upon International Equivalence

The imposition of an entirely new capital markets regulatory system in Canada may negatively impact clearing agency business with European bank participants. Canadian existing and proposed clearing and market infrastructure regulations are currently under review by European regulators to determine their equivalence. European regulators began this process over a year ago and are nearing completion of their analysis in order to meet certain deadlines to ensure that European bank participants of third country central counterparties will not be subject to higher capital requirements and other additional regulatory requirements.

Putting in place an entirely new regulatory regime that will either replace or add to existing and proposed regulations may delay the equivalency process as reviews may need to be conducted again to incorporate the new capital markets regulatory system. This may result in less foreign investment into Canada due to the higher capital costs that will be imposed upon foreign bank counterparties in the interim, ultimately result in a rejection of equivalency and, as a result, lead to a further rethinking of Canadian systemic risk regulation.

We understand the objective of the CCMR system is to support Canada's capital markets, including the ability of domestic corporations, including financial market infrastructures/clearing agencies, to grow internationally and attract foreign customers to Canada.

If Canadian clearing regulations are not deemed equivalent by the upcoming deadline, or if they are deemed equivalent, but the decision is later reversed following major changes to the way in which securities, derivatives, clearing agencies and systemic risk generally is regulated in Canada, Canadian clearing agencies' European bank participants will be subject to higher capital requirements. As a result, likely this European business will be lost to other foreign clearing agencies or to less costly bilateral transactions. Once Canadian clearing agencies have lost this business and European participants have found other alternatives, it will likely be difficult to regain this business. Some of these foreign clearing agencies may also enter the Canadian marketplace exempted from most requirements where they will continue to grow. An inability to service international participants in a major economy together with higher regulatory standards domestically will make it difficult for Canadian clearing agencies to compete in an international industry both domestically and abroad.

It is important that these proposed very substantial regulatory changes be managed in a way that minimizes disruption to business in the Canadian economy so that this European business is not lost.

In conducting its review to date, European regulators reviewed Canada's extensive existing and proposed systemic risk regulation including:

(i) the recently proposed reforms developed by the OTC Working Group (securities regulators from Quebec, Ontario, Alberta and British Columbia as well as the Office of the Superintendent of Financial Institutions ("OSFI") and the Bank of Canada) regarding:
- mandatory clearing of certain derivatives (CSA Staff Notice 91-303 *Proposed Model Provincial Rule on Mandatory Central Counterparty Clearing of Derivatives*)
- segregation and portability (CSA Staff Notice 91-304 *Model Provincial Rule – Derivatives: Customer Clearing and Protection of Customer Collateral and Positions*) and
- derivatives data reporting (OSC Rule 91-507 *Trade Repositories and Derivatives Data Reporting* and similar rules in Quebec and Manitoba and proposed by the CSA);

(ii) proposed provincial rules regarding PFMI implementation in Canada;

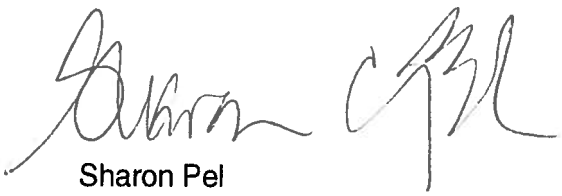
(iii) PFMI and other compliance requirements in clearing agency recognition orders from provincial securities regulators; and

(iv) Bank of Canada designation and oversight of systemically important clearing houses pursuant to the *Payment Clearing and Settlement Act*.

TMX Group submits that this risk to Canadian business should be factored into any decision to implement, and the timing of, the proposed CCMR system. Before enacting new systemic risk legislation and regulations, we strongly encourage discussion and coordination with the Bank of Canada, relevant provincial securities regulators and European securities regulators to consider the impact this new model of systemic risk and capital markets regulation would have upon the equivalency determination and timing so that the consequences and potential solutions to mitigate any damage to capital markets are fully understood.

TMX Group supports any efforts to make Canada's capital markets more efficient and welcomes the opportunity to engage with you and share TMX Group's unique perspective and long experience as a leader in Canada's markets. TMX Group appreciates the opportunity to provide comments with respect to the proposed CCMR system and related legislation and looks forward to further dialogue on this issue. We appreciate your consideration of our concerns, suggestions and requests for clarity and we would be happy to discuss these at greater length with the appropriate representatives. Please do not hesitate to contact me if you have any questions regarding our comments.

Respectfully submitted,



Sharon Pel

Appendix/Questions

TMX Group seeks clarity on many issues that are detailed below. We may have further comments regarding the CCMR system and related legislation depending upon responses to these questions.

Market Places / Trading Facilities / Securities – Issues

TMX Group seeks greater clarity regarding the following issues:

1. What additional entities is the broadened definition of market place under the PCMA intended to capture? (The proposed term would explicitly include exchanges as well as "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…")

2. What entities is the term "trading facility" under the CMSA intended to capture and how is this different from what is captured under "market place" under the PCMA?

3. Why was the concept of an ATS removed from the PCMA and how will these entities be regulated going forward?

4. Regarding market places, (i) why there will now be "recognized", "designated" and "other" marketplaces; (ii) what entities are intended to be captured under each; and (iii) how each category will be treated differently, including with respect to regulation and oversight?

5. Why does part (d) of the definition of "trade" include only "any participation as a trader in any transaction in a security through the facilities of *an exchange [italics added]*"? Why would the term exchange in this section not be replaced with "market place" given that the use of "trade", "traded" or "trading" throughout the PCMA where (d) would be applicable should equally apply with respect to any such trade occurring through the facilities of a market place?

6. The definition of "security" is much broader under the CMSA ("any contract, instrument or unit commonly known as a security") than under the PCMA (which lists specific types of securities). TMX Group seeks clarity regarding:

    a. the reasons for this difference;
    b. what products are intended to be captured under one act, but not the other;
    c. why certain securities deemed to be systemically important may require regulation under the CMSA but not under the PCMA;
    d. how would new forms of products be captured under the CMSA as they might fall under the PCMA, but not be commonly considered a security?
    e. how would products captured by securities legislation in foreign countries, but not the PCMA be treated under the CMSA?

We would further suggest that it should be possible to narrow the types of securities that could be captured under the CMSA as it is unlikely that all security products have the potential to create systemic risk.

Further Questions Regarding the *Capital Markets Stability Act*

1. Will there be a list maintained by the Authority of systemically important entities and made available to the market? Will this create a two tier market for the entities that are not systemically important?

2. How will Bank of Canada oversight of systemic risk change following implementation of the CMSA?

3. For clearing agencies recognized by the Authority under the PCMA and found to be systemically important under the CMSA, would they be subject to two recognition orders from the same regulator?

4. The definition of "capital markets intermediary" and "clearing house" do not appear to be mutually exclusive – that is, it appears that an organization can be both a clearing house and a capital markets intermediary. Could a clearing house also be a capital markets intermediary under the CMSA? If so, what are the designation requirements are for each, if they overlap?

5. What is the purpose of enabling a trade repository applying to become a designated trade repository (s.11)?

Further Issues Regarding the *Provincial Capital Markets Act*

1. *Carrying on Business* - Under the PCMA, to carry on business, an exchange must be recognized (s. 8) and thus be subject to the Chief Regulator's oversight. There is no territorial scope to the definition of carrying on business. TMX Group seeks further clarity regarding limitations on scope.

2. *Amendments to rules regarding reviews of decisions of recognized entities by the Tribunal (PCMA, s.13)* – There is no indication of the level of deference that will be given to the decision of a recognized entity under the proposed PCMA provision.

3. *Appeals* - There should be a clear limitation period on the review of decisions of exchanges. The PCMA now proposes a broad ability for extension which will create uncertainty with respect to the finality of decisions.

4. *Prospectus requirements (s.27)* – Currently the proposed provision does not account for the prospectus-exempt distributions set out under National Instrument 45-106. Although the regulations may address this, we believe reference should be made to the exemptions in the PCMA itself.

5. *Cease trading orders (PCMA, s. 86)* – This is a new power that did not previously exist under the *Securities Act* (Ontario). TMX Group seeks further clarity as to:

    a. why such broad powers were deemed necessary;
    b. why a cease trade order would only be applied to recognized exchanges and not other market places as extraordinary circumstances may also occur on other market places and impact capital markets; and
    c. how such powers may coordinate with IIROC's market-wide circuit breakers.

    We would suggest that there be a more specific and high threshold for a disturbance before such a drastic measure be taken.

6. *Commodity Futures Act* – TMX Group seeks clarity as to whether this will be rescinded as the related references do not appear in the PCMA.

7. *TMX Group Shareholding Restrictions* – TMX Group seeks clarity with respect to whether the shareholding restrictions set out in section 21.11 of the *Securities Act* (Ontario) will be set out in the PCMA regulations as they do not currently appear in the PCMA itself.