

13.3.2 CDS Notice and Request for Comments – Material Amendments to CDS Rules – Termination of Euroclear UK Direct Service

CDS CLEARING AND DEPOSITORY SERVICES INC. (“CDS[®]”)

MATERIAL AMENDMENTS TO CDS RULES

TERMINATION OF EUROCLEAR UK DIRECT SERVICE

REQUEST FOR COMMENTS

A. DESCRIPTION OF THE PROPOSED CDS RULE AMENDMENTS

CDS Clearing and Depository Services Inc. is proposing amendments to its Rules to redact all references to the Euroclear UK Direct Service (the “Euroclear Service”). The Board of Directors¹ of The Canadian Depository for Securities Limited approved the termination of the Euroclear Service at its meeting in January 20, 2010, pending regulatory approval of consequential changes to CDS’s Participant Rules.

The Euroclear Service was set up as a means to facilitate the settlement of transactions in CREST between CDS participants and CREST members. CREST is the settlement service operated by Euroclear UK and Ireland Limited. Since the launch of the service there has been limited interest in the Euroclear Service by participants. The credit crisis reduced interest in the market; the lack of a facility for the two-way transfer of securities positions between the Canadian and UK markets limited the utility of the link. At the present time, no participants use the Euroclear Service. CDS incurs cost to maintain the link, even when not used by participants, related to maintaining a SWIFT connection and payment of the annual CREST fees. In September 2009, CDS was advised that changes in legislation would remove its previous exemption from compliance with anti-money laundering legislation in the United Kingdom. As a result, if CDS continued to offer the Euroclear Service, CDS would be required to create an anti-money laundering compliance program that would expose CDS to costs and to increased reputational risk. In light of the lack of utilization of the Euroclear Service and the increased costs and risks associated with an anti-money laundering compliance program, the Board approved the termination of the Euroclear Service.

B. NATURE AND PURPOSE OF THE PROPOSED CDS RULE AMENDMENTS

The proposed amendments remove references to the Euroclear Service from the CDS Participant Rules. The deleted sections include the definitions of terms used in describing the Euroclear Service, and all of Rule 14, which governs the Euroclear Service.

C. IMPACT OF THE PROPOSED CDS RULE AMENDMENTS

CDS does not foresee any impact or effect, resulting from the proposed amendments, on CDS Participants, other market participants, or the securities markets in general. There are currently no CDS Participants subscribed to, or using, the Euroclear Service. Termination of the Euroclear Service will allow CDS to reduce current operating costs and avoid the projected costs of an anti-money laundering compliance program.

C.1 Competition

The Rule amendments are expected to have no impact on competition.

C.2 Risks and Compliance Costs

The termination of the Euroclear Service eliminates the significant risk and compliance costs which would have been incurred by continuing to offer the service.

C.3 Comparison to International Standards – (a) Committee on Payment and Settlement Systems of the Bank for International Settlements, (b) Technical Committee of the International Organization of Securities Commissions, and (c) the Group of Thirty

International standards for clearing agencies are not relevant to the termination of the Euroclear Service.

¹ Pursuant to a unanimous shareholder agreement between The Canadian Depository for Securities Limited (“CDS Ltd.”) and CDS, effective as of November 01, 2006, CDS Ltd., which acts under the supervision of its Board of Directors, assumed all rights, powers, and duties of the CDS Board of Directors.

D. DESCRIPTION OF THE RULE DRAFTING PROCESS

D.1 Development Context

In September 2009, CDS was advised of the changes in anti-money laundering legislation in the United Kingdom, and of new CREST Rules which would have imposed impose new anti-money laundering requirements on CDS. This lead to a review of the need for the Euroclear Service.

D.2 Rule Drafting Process

Each amendment to the CDS Participant Rules is reviewed by CDS's Legal Drafting Group ("LDG"). The LDG is a committee that includes members of Participants' legal and business groups. The LDG's mandate is to advise CDS management and its Board of Directors on rule amendments and other legal matters relating to centralized securities depository and clearing services in order to ensure that they meet the needs of CDS, its Participants and the securities industry. The proposed amendments were reviewed by the LDG on March 18, 2010; the LDG had no comments on the proposal to terminate the Euroclear Service.

These amendments were reviewed and approved by the Board of Directors of CDS Ltd. on April 21, 2010.

D.3 Issues Considered

CDS weighed the benefits of the Euroclear Service against the current and potential costs of maintaining an under-used service, and determined that it was in the best interest of CDS, and of its participants and stakeholders, to terminate the Service.

D.4 Consultation

No participants have been, or are currently, actively using the Euroclear UK Direct Service.

D.5 Alternatives Considered

CDS considered the two available options. As UK law had been amended, the *status quo* (wherein CDS would act as sponsor to its Participants if they chose to use the Service, but would not be required to perform AML checks on those Participants, as would other 'Sponsoring Members' of EUI, by virtue of CDS's status as a CSD) was not an available alternative.

CDS considered the current costs, and the potential future costs of implementing an AML compliance program solely for purposes of the Service, and weighed those costs as against the costs of Termination.

D.6 Implementation Plan

CDS is recognized as a clearing agency by the Ontario Securities Commission pursuant to section 21.2 of the Ontario *Securities Act*. The Autorité des marchés financiers has authorized CDS to carry on clearing activities in Québec pursuant to sections 169 and 170 of the Québec *Securities Act*. In addition CDS is deemed to be the clearing house for CDSX[®], a clearing and settlement system designated by the Bank of Canada pursuant to section 4 of the *Payment Clearing and Settlement Act*. The Ontario Securities Commission, the Autorité des marchés financiers and the Bank of Canada will hereafter be collectively referred to as the "Recognizing Regulators".

The amendments to Participant Rules may become effective upon approval/disapproval of the amendments by the Recognizing Regulators, following public notice and comment. The target date for implementation is July 26, 2010.

E. TECHNOLOGICAL SYSTEMS CHANGES

E.1 CDS

The required technological changes within CDS include the termination of the link with the SWIFT Euroclear UK server and the removal of the CREST GUI from CDS user workstations.

E.2 CDS Participants

No technological systems changes will be required, as no CDS participants currently subscribe to the Service.

E.3 Other Market Participants

CDS foresees no technological systems changes required of other market participants.

F. COMPARISON TO OTHER CLEARING AGENCIES

There is no direct comparison with clearing agencies in other jurisdictions.

G. PUBLIC INTEREST ASSESSMENT

CDS has determined that the proposed amendments are not contrary to the public interest.

H. COMMENTS

Comments on the proposed amendments should be in writing and submitted within 30 calendar days following the date of publication of this notice in the Ontario Securities Commission Bulletin to:

Legal Department
CDS Clearing and Depository Services Inc.
85 Richmond Street West
Toronto, Ontario M5H 2C9

Fax: 416-365-1984
e-mail: attention@cds.ca

Copies should also be provided to the Autorité des marchés financiers and the Ontario Securities Commission by forwarding a copy to each of the following individuals:

M^e Anne-Marie Beaudoin
Secrétaire del'Autorité
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal (Québec) H4Z 1G3

Manager, Market Regulation
Market Regulation Branch
Ontario Securities Commission
Suite 1903, Box 55,
20 Queen Street West
Toronto, Ontario, M5H 3S8

Télécopieur: (514) 864-6381
Courrier électronique: consultation-en-cours@lautorite.qc.ca

Fax: 416-595-8940
e-mail: marketregulation@osc.gov.on.ca

CDS will make available to the public, upon request, all comments received during the comment period.

I. PROPOSED CDS RULE AMENDMENTS

Appendix "A" contains text of current CDS Participant Rules marked to reflect proposed amendments as well as text of these rules reflecting the adoption of the proposed amendments.

APPENDIX "A"
PROPOSED CDS RULE AMENDMENTS

Text of amended CDS Participant Rules marked to reflect proposed revision	Text of amended CDS Participant Rules reflecting the adoption of proposed revisions
<p>additions are <u>underlined</u> deletions are struck-out</p> <p>1.1.1 Application The Rules adopted by CDS by which each Participant has agreed to be bound pursuant to the Participant Agreement are: Rule 1 - Documentation Rule 2 - Participation Rule 3 - Operations Rule 4 - Liability and Indemnity Rule 5 - Risk Management Rule 6 - Depository Service Rule 7 - Settlement Service Rule 8 - Payment Exchange for CDSX Rule 9 - Default Rule 10 - Cross-Border Services Rule 11 – TA Participants Rule 12 – ATON Rule 13 – Delivery Services Rule 14 – Euroclear UK Direct Service</p> <p>1.2.1 Definitions For the purposes of the Legal Documents, unless otherwise specified: ... "Credit Ring" means either a Category Credit Ring or a Fund Credit Ring. "CREST" means the system operated by Euroclear UK & Ireland for the settlement of trades in securities "Euroclear UK Direct Charges" has the meaning set out in Rule 14.1.10. "Euroclear UK Direct Participant" means a Participant who uses the Euroclear UK Direct Service". "Euroclear UK Direct Service" means the Euroclear UK Direct Service made available pursuant to Rule 14. "CREST Software" has the meaning set out in Rule 14.1.6. "Cross-Border Accounts" means the CDS DTC Account, the CDS NSCC Clearing Account and the Link Accounts. ... "Entitlements Processor" means a Participant who performs the activities of an Entitlements Processor set out in Rule 2.5.5. "Euroclear UK & Ireland" means Euroclear UK & Ireland Limited, the central securities depository for the UK market and Irish equities and a part of the Euroclear group, or any Person who succeeds to the rights and obligations of Euroclear UK & Ireland with respect to CREST. "Exchange" means the Montreal Exchange, the Toronto Stock Exchange, the TSX Venture Exchange or any other regulated securities exchange. ... Rule 14 – Euroclear UK Direct Service is deleted in its entirety.</p>	<p>1.1.1 Application The Rules adopted by CDS by which each Participant has agreed to be bound pursuant to the Participant Agreement are: Rule 1 - Documentation Rule 2 - Participation Rule 3 - Operations Rule 4 - Liability and Indemnity Rule 5 - Risk Management Rule 6 - Depository Service Rule 7 - Settlement Service Rule 8 - Payment Exchange for CDSX Rule 9 - Default Rule 10 - Cross-Border Services Rule 11 – TA Participants Rule 12 – ATON Rule 13 – Delivery Services</p> <p>1.2.1 Definitions For the purposes of the Legal Documents, unless otherwise specified: ... "Credit Ring" means either a Category Credit Ring or a Fund Credit Ring. "Cross-Border Accounts" means the CDS DTC Account, the CDS NSCC Clearing Account and the Link Accounts. ... "Entitlements Processor" means a Participant who performs the activities of an Entitlements Processor set out in Rule 2.5.5. "Exchange" means the Montreal Exchange, the Toronto Stock Exchange, the TSX Venture Exchange or any other regulated securities exchange. ...</p>