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The Secretary
Ontario Securities Commission
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Re: OSC Staff Notice 11-784 *Burden Reduction*

We commend the OSC for its increased focus on reducing the regulatory burden where possible. It is important that the burden is commensurate with the regulatory objective sought to be achieved and we appreciate this opportunity, which comes in addition to the initiatives already commenced by the Canadian Securities Administrators ("CSA"), to provide further input on measures that could further reduce regulatory burden.

Before providing our comments, we would like to raise some general considerations about the approach to regulation, which we urge the OSC to take into consideration when reviewing the various comments provided by industry stakeholders both within the frame of this initiative and in respect of the other ongoing initiatives. We are proponents of a strong regulatory framework, as it is critical to the credibility of our industry domestically and internationally, but we believe there are multiple ways to achieve that objective.

1. This is an opportunity to revisit the principles behind the securities regulatory framework and ensure that the requirements have not become too prescriptive[1];
2. While prescriptive rules provide for certainty, they come with high compliance costs while making it increasingly difficult to compete and innovate;
3. Overly prescriptive regulation causes a non-virtuous cycle:
    a. Rules are applied more and more mechanically, losing sight of the regulatory objective and leading to a failure to properly address new scenarios, which may be contrary to that objective but not contemplated by the rules;
    b. The emphasis shifts to finding loop-holes, which results in more activities that are technically onside but contrary to the regulatory objective;

[1] For further certainty, we wish to clarify that all of these considerations also apply to the Investment Industry Regulatory Organization of Canada ("IIROC").

    c. More rules are put in place, to address new scenarios and loop-holes;

4. In light of this, we urge the OSC, as part of all regulatory burden reduction initiatives it is a party to as well as within the scope of any new regulatory initiatives, to reconsider the benefits of detailed rules versus well-defined principles;
5. We do believe, however, that more principles-based regulation needs coordinated, strong enforcement and prosecution by the CSA and IIROC;
6. More principles-based regulation would probably also allow the plethora[2] of developments with respect to market structure, and issues relating to access to and cost of market data, and disclosure and improper application of rules that affect the fairness and efficiency of our markets, to be addressed more rapidly; and
7. In addition to these considerations with respect to the approach to rule making, we also believe the OSC, and other CSA members, should revisit requiring that a thorough cost-benefit analysis be performed for any new rule.

Our comments are divided into two general categories:

- Issues specific to Neo Exchange Inc. ("NEO") (and its peers) within the OSC's jurisdiction; and
- Issues that are relevant to the initiatives to which the OSC is party within the frame of the CSA, based on our observations having now operated for more than three years as a recognized exchange.

I. <u>OSC – Orders, Policies and Practices with respect to a Recognized Exchange</u>

1. Recognition Order ("RO")

Some of the concerns and suggestions expressed are also applicable to other recognized entities, i.e. self-regulatory organizations and clearing agencies.[3]

Concerns and suggestions:

- Terms and conditions imposed on shareholders of a recognized exchange should be limited to those shareholders in a real or perceived position of influence. That is, "significant shareholders" should have ownership interests or access to information that would indicate such influence. We understand the concern that shareholders may be in a position to direct an exchange in a manner that is not consistent with the public interest, but we note that the traditional conflict of interest was centered on dealer-shareholders, a risk that has been much reduced since the creation of IIROC. Although it would still be possible for an exchange to create functionality that benefits certain parties over others, with current levels of scrutiny it would be very difficult to use this leverage. We suggest that a simple threshold test such as 20%, board membership, or a combination of the two would be more appropriate and more

[2] See recent market structure comments by TD Securities and Scotia Capital Markets, the Bridgemark case in British Colombia, the recently annouced class-action suit against a venture listed security, etc.

[3] We thank OSC staff for the work already done to remove some burdensome elements through the RO restatement that was published on February 21 (along with those of the other exchanges).

effective in managing conflicts of interest. This would reduce work effort for the exchanges, and reduce significant work efforts for exchange shareholders that are without any real or perceived position of influence, and reduce barriers to exchange ownership.

- Exchange Holding Companies (HoldCos) should only be included under ROs where control/direction and/or key functions are housed in them – if any exchange operator were to use a HoldCo to try to avoid oversight of regulatory or public interest functions, the Commission has the power to require recognition at that point. This would reduce the work effort of exchanges under both the RO and Form 21-101F1 (see further information on the Form below).

- Obligations related to conflicts of interest ("COI") are found in multiple places, often overlapping. Streamlining these obligations would substantially reduce the work effort of exchanges:
    - NEO's current RO has requirements for the Regulatory Oversight Committee (the "ROC") to: 1) generally consider COI; 2) oversee COI mechanisms including COI policies required under the RO (a requirement already covered off by the condition that these COI policies be considered to be rules and the ROC's obligation to approve rules); 3) monitor the mechanisms, 4) review COI policies regularly and no less than annually; and 5) annually prepare a report examining the avoidance and management of COI;
    - Most of these requirements are duplicated in a requirement placed on the exchange to have COI management and avoidance policies and procedures; and
    - Therefore, to assist in avoiding time consuming, interrelated documentation, we suggest that the requirements be simplified to RO provisions that require ROC oversight, documentation of mechanisms in policies and procedures and reviews by management and the ROC, at least annually, of their effectiveness.

- All terms and conditions that have already been met should be revised or removed, such as those in sections 13(b), 22(a), 39(a) and 46(a) of NEO's RO.

- Please see the note below in respect of filing of annual audited financial statements in the section discussing NI 21-101.

- The obligation in the ad hoc reporting to provide prompt notification of any suspension or delisting of a NEO listed issuer should be reconsidered – this is a normal course activity for an exchange and will require a public notice; there does not appear to be any utility in a separate RO reporting requirement.

- The requirement to have COI polices re: listed competitors should also be reconsidered. The need for these policies originated at a time when exchanges were monopolies and as this is no longer the case, the concerns over unfair treatment of competitors have been diminished to the point where, arguably, they are moot. Quarterly reporting about any such listings and the ability for an issuer to raise concerns with the applicable regulator should be sufficient constraints.

- It would be helpful, given all of the restrictions in the RO, if clarification could be added about what significant shareholders *can* do – including supporting the exchange so long as the support is not simply based on ownership. The current restrictive provisions can cause some shareholders to hesitate to take any action that could be perceived as "favouring" the exchange.

- Simplification in Schedule 5 of the long list of required items for notices of rule and fee amendments and other changes would assist in making the notices more readable – for example it should be presumed that anything suggested by a marketplace will be in compliance with laws and will not materially increase systemic risk. If there are issues that cause Commission staff to have any sense that this is not the case, prior to publication this can be discussed and a question can be added for comment.

2. Staff Notices

We urge that caution be exercised in use of staff notices. Providing guidance, expectations and clarification is very helpful, but we believe there have been occasions where staff notices have altered the nature of a requirement. An example of this is the interpretation in OSC Staff Notice 21-706 of the material system change requirements in section 12.3 of NI 21-101.[4] The national instrument has some flexibility built into it and, while it is not unreasonable to expect entities to wait for final approval of a change before starting the clock on the 90 day period during which technical information must be available prior to making the change (and the associated 60 day period relating to availability of testing facilities), there may be considerations that would make it reasonable to provide specifications and testing facilities prior to approval. There are cases where a limited group of industry participants would be impacted and/or adopting the change is not mandatory, and flexibility in when the 90 days begins in some cases would allowing more certainty around launch dates.

3. Tracking of Additional Requirements and Requests

There does not appear to be a centralized mechanism available to oversight staff for ensuring that requirements that are not specified in ROs are tracked. For example, certain reporting will stem from an RO requirement, as further defined by staff, but will be developed in association with the regulated entity. Staff overseeing an entity can change over time and it can be difficult for them to be aware of the origins of such reporting. A robust centralized mechanism would also reduce the need for some of the duplicative filing requirements under the Forms, as discussed in the next section.

II. CSA – National Instruments

1. National Instrument 21-101 *Marketplace Operation* (NI 21-101) and Forms 21-101F1 and 21-101F3

(a) NI 21-101

This rule, although created to provide a framework for multiple marketplaces, was initially developed in a monopoly exchange environment. The provisions relating to governance, financial viability and systems all reflect the risks in that environment and explain many of the differences (which have been reduced through the years) between the requirements for exchanges versus alternative trading systems (ATSs). In our view, it is time to review some of these assumptions[5]:

- Section 4.2 – Filing of Annual Audited Financial Statements. In section (1), a recognized exchange must file annual audited financial statements within 90 days after the end of its

[4] (1) A marketplace shall make publicly available all technology requirements regarding interfacing with or accessing the marketplace in their final form... (b) if operations have begun, for at least three months before implementing a material change to its technology requirements. (2) After complying with subsection (1), a marketplace shall make available testing facilities for interfacing with or accessing the marketplace… (b) if operations have begun, for at least two months before implementing a material change to its technology requirements.

[5] We do believe however that exchanges should continue to have a higher standard relating to risks unique to them (listings, formal market making and, if applicable, market regulation).

financial year and in section (2) an ATS must file annual audited financial statements. For exchanges that are not reporting issuers constrained by other securities law requirements, there should be the option to provide financial statements within 120 days instead of 90. Given that, under recognition orders, exchanges are required to provide quarterly financials and calculate financial viability ratios, staff would still be in the position to know when to ask for further information. The 90 day obligation is a source of additional work effort as it requires additional board and board committee meetings to achieve that deadline.

- Section 12.2 – System Review. The current multiple marketplace environment has provided evidence to support the argument that costly audits should not be required on an annual basis. Marketplaces may choose to have assurance audits carried out for their own purposes and it may be that the requirement should be included for critical entities (based on volumes, risks to listed issuers or another metric), but the benefits of this requirement have not been proven in practice. The original purpose was to ensure the exchange had an independent third party view relating to the integrity, security, etc. of key systems but it has now become a resource heavy exercise that appears to be more of a check-the-box exercise. It would be more impactful to clarify that dealers can consider the robustness of a marketplace, even a "protected" one, as part of reasonable order protection rule procedures so that the market can determine for itself whether sufficient steps are taken to address system issues. It could also be a requirement imposed by regulators where concerns have surfaced and a review is warranted. At a minimum, there should be clearer expectations set out in NI 21-101.

(b) Form 21-101F1 ("F1")

This form provides a single location for all information about an applicant for exchange recognition, which has proven to be a good approach to gathering such extensive information. The issue is that, once operational, minor changes to the information are generally not relevant for oversight purposes and yet must be tracked and filed. We suggest that there are ways to ensure all pertinent information remains available without resources wasted in tracking and reporting immaterial items.

- Exhibit B – Ownership. Exchanges should in the normal course be maintaining details about their significant shareholders to meet fit and proper requirements under ROs, which can be confirmed as part of the oversight process. Since there are also share ownership restrictions under ROs, we therefore suggest that the required information in the F1 for non-publicly listed exchanges should be limited to the list of shareholders, whether they hold over 5% and any changes to the list or to holdings with respect to that threshold. To provide some perspective: one of the most common reasons for filing changes to NEO's Exhibit B to date has been to report minor changes to the number of employee-held options.
- Exhibit C – Organization. We request that consideration be given to whether the detailed information required about directors is needed in the F1. A requirement to post information regarding officers and directors on the exchange's website would likely be of more benefit and, as exchanges do so already, would remove duplicative effort.
- Exhibit E – Operations of the Marketplace. A number of items in this exhibit are needed at the time of the initial application, but afterwards they form part of publicly available materials, such as rules, guides and information found on exchange websites. It would substantially reduce the effort required to keep this exhibit current if after launch only the non-public information was updated.

- Exhibit J – Access to Services and Exhibit L – Fees. Initial rules and fees are appropriately filed as part of the initial F1 but since all changes must be filed in accordance with the protocols attached to ROs, it should only be necessary for an exchange to post revised versions on their websites. Having to update exhibits to reflect rule and fee changes that have been filed and approved is duplicative.

(c) Form 21-101F3 ("F3")

- This quarterly filing requires extensive statistics, the vast majority of which is in IIROC's possession. The ability to search and run reports on IIROC's data would provide information in a much more efficient way as it could then be more easily compared among marketplaces.
- More importantly, even if the quantitative information in the F3 cannot be easily obtained from IIROC, we ask that the descriptive information required in sections A. 4, 5, 6 and 7 be reconsidered. Marketplaces should not be asked to provide status updates relating to filings with regulators except as to whether approved changes have been implemented. It is currently prescribed that exchanges must report in the F3 that a change under review by staff of their lead regulator is outstanding because it is still under review by said staff. Further, systems incidents must be reported at the time of the incident, and requiring the marketplace to gather the information again for a quarterly report is time consuming and of questionable oversight value.

2. Streamlining/Improvements re: Investment Funds

Although we are aware and appreciative of the ongoing initiatives to streamline requirements for ETF issuers, we wanted to take this opportunity to provide a few additional observations, as we have gained some insights into the difficulties ETF issuers face while processing their listing applications.

- Streamlining of Personal Information Forms (PIFs). Considerable efforts have been made by exchanges to reduce the burden associated with completing PIFs. Individual exchanges can only go so far, however. We believe that a centralized database, accessible to CSA members and exchanges, would be the ultimate solution. If an insider could complete and update the information online, and have control over which entities are permissioned to review it, the process would be greatly improved. We acknowledge that this would require a secure system, which would in turn require funding and maintenance, but we ask that it be given serious consideration. The reduction in work effort and cost for multiple industry stakeholders would be substantially reduced and the CSA should be able to leverage some of its existing infrastructure already in place to manage similar types of information.
- We suggest that an equivalent to the shelf prospectus concept be considered for investment fund issuers. A base prospectus could be filed and if key elements are not changing, such as the trustee and fund manager. Only an ETF Facts type document would be necessary to qualify new funds and it would be the document that is renewed annually instead of the prospectus. It would reduce substantially the review time, work effort and cost without a material impact on disclosure.
- With the keen interest shown by many parties in crypto-assets, it is important that CSA members come to a conclusion on custodians. We are sensitive to the multiple priorities facing staff who are working on these issues, but a clear view on this would be an important foundational step.

- An element of the process for both ETF and mutual fund issuances that can impact timing but which is not well-understood (and which also applies for non-investment fund issuers) is how securities become CDS-eligible. We are not in any way questioning the competency of the clearing agency but suggest that it would be helpful to issuers if the regulators of CDS were to review this process.

3. Streamlining/Improvements re: Non-investment Fund Issuers

Again, we appreciate the ongoing initiatives in this area, and would like to raise some further issues for consideration relating to the current rule framework for non-investment fund issuers:

- Please see the notes above with respect to PIFs.
- There are certain requirements in Form 41-101F1 *Information Required in a Prospectus* where three years of information is required for non-venture issuers versus two years for venture issuers. We have noticed that for many growth focused companies, the three years requirement for non-venture issuers is representing a substantial cost, while not being of any benefit to the investors, and suggest that the requirement be streamlined across the board for both venture and non-venture issuers to two years.

4. Oversight of IIROC

IIROC plays an important role in our securities markets. Anything that can be done to streamline its obligations to better serve its members would be of benefit. We do not presume to know all of the constraints they are under, but suggest that their oversight model be revisited to ensure that rule changes they seek to make can be done more efficiently and rapidly than today. We also believe that IIROC should initiate a similar regulatory burden reduction initiative as those undertaken by the OSC and the CSA.

Thank you for your consideration. We again commend the OSC for establishing this initiative and for seeking to hold the March 27 roundtable to further discuss these issues. It is likely that the discussion will lead to the identification of further streamlining opportunities. Please note that we are interested in participating.

Yours truly,

"*Cindy Petlock*"

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