

BY EMAIL

September 21, 2018

Ontario Securities Commission
20 Queen Street West
Toronto, Ontario M5H 3S8
Email: comments@osc.gov.on.ca

Attention: The Secretary of the Commission

Re: Application to vary the Recognition Order for the Canadian Depository for Securities Limited and CDS Clearing and Depository Services Inc. (together, "CDS")

CDS is seeking to vary its recognition order to remove the requirement that one of the members of its board of directors ("Board") be a representative of a non-TMX marketplace ("Unaffiliated Marketplace Director"). As noted in the Request For Comment, this requirement was put in place as part of the Maple transaction, to deal with the conflicts of interest that would result from TMX owning 100% of CDS. In its place, CDS proposes an advisory committee requirement (including all non-TMX marketplaces), to provide advice, comments and recommendations to CDS management and the Board. We appreciate the opportunity to comment on this important pros

In our view, if the Unaffiliated Marketplace Director requirement truly cannot be managed without undue difficulty, the proposal is not an unreasonable alternative – subject to the suggested changes below - but we believe further attention should first be paid to whether the CDS concerns that led to the proposal can be addressed.

Background

We summarize CDS' stated concerns as follows:

1. Difficulty in obtaining the required skill mix, experience and knowledge of the entity ("Skill Mix") for the Board, due to the technical nature of CDS, as the Unaffiliated Marketplace Director requirement "...narrows the pool of potential directors for one of the CDS Board seats".
2. The conflicts of interest inherent in the Unaffiliated Marketplace Director's attendance at a meeting, given the challenges "...for an individual to effectively separate his interests as a marketplace operator from his fiduciary responsibility as a clearing house director."
3. That the Unaffiliated Marketplace Director requirement is a "...disproportionate response to competition law concerns raised in the Maple transaction context".

These are significant issues and we understand CDS' desire to resolve them. However, we submit that the following additional information should be included in the considerations:

1. Skill Mix. We sympathize with the difficulties inherent in meeting the variety of requirements and objectives as a regulated entity. We note that this has likely been exacerbated by the fact that, subsequent to the first Board after the Maple transaction, CDS does not appear to have followed its original process that included obtaining nominations from all of the non-TMX marketplaces. It is possible that requests for nominations from all marketplaces would have provided deeper pools of candidates. More importantly, by having two TMX Group representatives (in addition to the President of CDS and CDCC), individuals who are likely to have similar skill sets to senior executives at unaffiliated marketplaces in relation to the clearing function, CDS has reduced that pool even further.
2. Dealing with the Unaffiliated Marketplace Director's Conflicts of Interest. That there have been and will be conflicts to deal with in relation to an unaffiliated director is unavoidable and fundamental to the purpose behind the requirement to have him or her in place. We submit that the challenge in managing this particular conflict should be no different among all marketplace representatives – including those from TMX – and therefore the logic for arguing that they be removed from the Board is identical. To our knowledge, all of these directors were asked on several occasions to recuse themselves from entire discussions on issues that impacted marketplaces instead of recusing themselves from the decision itself, which meant that the value of having marketplace directors to inform the discussion and the intended checks and balances were absent.
3. Need for the Requirement due to Competitive Concerns. We respectfully disagree with the statements made by CDS on this topic. Post-Maple, the CDS Board has, in fact, supported anti-competitive changes, such as:
 - Following the announcement by Nasdaq of its plan to transform its ATS registration into an exchange recognition, CDS proposed to charge a fee of \$80,000 to set up an exchange without listings (plus a fee of \$150,000 for an exchange with listings and \$80,000 for an ATS).¹ This was ultimately not approved. One of the reasons was likely that the list of required work cited was not accurate (see the Nasdaq response²), and a robust discussion at the Board would have been of assistance. A non-TMX marketplace representative could have provided insights into how CDS sets up all marketplaces for clearing similarly, regardless of whether they are exchanges (with or without listings) or ATSs.
 - It is our understanding that, after the TSX/TSX Venture boards of directors determined that they could not list or allow to remain listed any issuers with US cannabis operations or assets, the CDS Board initially supported a proposal to cease clearing such issuers, despite the fact that the other listing exchanges in Canada relying on CDS continued to list them. This was ultimately resolved in a different way, but the CDS Board should have had access to as broad a range of information on this topic as possible.

Suggestions

We agree that the Unaffiliated Marketplace Director requirement has not led to the desired checks and balances but believe that this was impacted to some degree by the approach taken, as noted above. We provide some considerations for how this could be improved and, in the alternative, if CDS' proposal is

¹ http://www.osc.gov.on.ca/documents/en/Marketplaces/cds_20160707_sn-rfc-rules-cds-fee-schedule-revised.pdf

² http://www.osc.gov.on.ca/documents/en/Marketplaces/com_20160806_nasdaq.pdf

approved, how to ensure the advisory committee is positioned to succeed in achieving the desired outcome:

- Follow the previous process for obtaining candidates for the nomination from all marketplaces.
- Explicitly set out the expectation that the Unaffiliated Marketplace Director consult with other marketplaces on an ongoing basis, unless confidentiality is requested.
- All of the marketplace directors should be allowed to remain for at least part of the discussion on issues impacting marketplaces – and then recuse themselves so that the CDS Board has as much information as possible on which to make the decision.
- To help resolve both the conflict of interest and Skill Set issues -
 - If the CDS proposal is not approved, we suggest that there should be only one TMX Group director in addition to the CEO of CDS and CDCC, plus one Unaffiliated Marketplace Director. CDS is not like other subsidiaries and standard corporate governance principles supporting membership on the Board by representatives of the parent should not be applied.
 - If the CDS proposal is approved it should be subject to the requirement that there be no TMX Group representatives, other than the CEO of CDS and CDCC, on the CDS Board. They should instead be participants in the advisory committee.
- Should CDS' proposal be accepted, we also suggest that information would need to be provided in advance so that there is an opportunity to provide timely input. We are not sure how a committee could receive sufficient information to provide advice that an individual director could not, but agree that the advisory committee could allow for the broader input that has been lacking to date.

Summary

We feel that there are options for addressing CDS' valid concerns that should be explored prior to removing the Unaffiliated Marketplace Director requirement. If CDS' proposal is approved it should be adjusted to ensure that the Board is able to focus on clearing issues, free of all marketplace conflicts of interest and that the advisory committee is in a position to provide to provide meaningful input. Significant controls have been put in place to deal with the risks of the clearing agency being used by the parent exchange in an anti-competitive way and if one is to be removed, then a meaningful, workable replacement is required.

Thank you for your attention to this matter.

Yours truly,

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