DAVIES

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September 10, 2018

BY E-MAIL

Aequitas NEO Exchange Inc.
155 University Avenue, Suite 400
Toronto, ON M4H 3B7
Email: legal@aequin.com

Attention: Cindy Petlock, Chief Legal Officer & Corporate Secretary

Dear Sirs/Mesdames:

We are writing in response to Trading Notice #2018-027 dated August 9, 2018 regarding Aequitas NEO Exchange Request for Comments – Proposed Trading of Foreign-Listed Structured Products (the "**Notice**").

We support initiatives to broaden the range of investment opportunities available to Canadian investors, including retail, and we welcome the opportunity to comment on the Exchange's proposal to initiate the trading of Foreign-Listed Structured Products (the "**Foreign Notes**") set out in the Notice. However, we do have concerns that the trading of Foreign Notes on the Exchange as described in the Notice would compromise investor protections typically afforded retail investors and permit foreign issuers easier access to the Canadian markets than currently permitted for Canadian issuers of similar structured notes.

Our primary concern is that investors in Foreign Notes would not necessarily have access to prospectus level disclosure regarding the Foreign Notes or the issuers of Foreign Notes that is required for Canadian issuers of similar products. Any disclosure provided, even if at a level comparable to a Canadian prospectus, also would not necessarily be in both English and French, as would be required under Canadian prospectus rules and, in fact, may not be in *either* English or French. In addition, Canadian issuers of structured notes are required to provide disclosure regarding material Canadian tax consequences to holders, which is unlikely to be available in respect of the Foreign Notes and, Canadian issuers of structured notes typically ensure that the necessary information is available for Canadian holders to complete their Canadian tax returns. It is not clear that any of these protections or information will be available to Canadian holders of Foreign Notes.

Canadian securities regulators have actively regulated issuers of structured notes and, beyond prospectus-level disclosure, require the pre-clearance of "novel" products, require that marketing materials comply with strict disclosure requirements, prohibit disclosure of hypothetical performance data (in contrast to the regime that has been recommended by IOSCO and adopted by the United States Securities and Exchange Commission) and mandate disclosure regarding suitability, the fair value of the notes on the date of issue, conflicts of interest and fees and expenses.

In addition to the requirement to pre-clear any "novel" securities, structured note issuers under the Canadian securities law regime are prohibited from linking securities to specified underlying interests, including most foreign securities, actively-managed investment funds and proprietary indices, without first pre-clearing such securities. As an added protection to investors, linked note issuers are generally not permitted to link their securities to reference assets or interests for which there is no information in the public domain on the basis that it would be particularly difficult for the linked note issuer to provide full, true and plain disclosure in respect of such references assets or interests.

Issuers of Foreign Notes would not as a result of being traded on the Exchange be subject to the continuous reporting requirements applicable to reporting issuers in Canada, nor would they be subject to the additional disclosure requirements applied by regulators in respect of structured notes qualified under a Canadian prospectus, including the ongoing website disclosure that is mandated pursuant to CSA Staff Notice 44-305 – *2015 Update – Structured Notes Distributed under the Shelf Prospectus System* ("CSA Staff Notice 44-305"). Further, the Foreign Notes would not necessarily be subject to a rigorous vetting process comparable to that which applies to domestic issuances of prospectus-qualified structured notes on the initial clearance of the shelf prospectus establishing a note program and thereafter on novel offerings.

The regulatory regime for Canadian structured notes goes beyond the requirements applicable to reporting issuers and mandates the provision of on-going information regarding the notes. CSA Staff Notice 44-305, for example, contains a lengthy list of the type of information that linked note issuers are expected to include on their websites, including in respect of the composition of the underlying portfolio to which the note is linked, the current and historical daily bid prices for the note, the daily indicative value of the note, the amount of any early trading charges, changes to the underlying portfolio and distributions, coupons or return of capital payments. It is not clear whether the protections afforded to investors by virtue of the continuous disclosure regime, including CSA Staff Notice 44-305, will be available to Canadian holders of Foreign Notes.

We also question the benefit of the limited price transparency afforded to purchasers of the Foreign Notes as a result of their foreign listing. First, the mere listing of a Foreign Note on a foreign exchange, does not guarantee a robust trading market on that exchange. Accordingly, the informational content of the trading price of Foreign Notes may be of only limited value to Canadian investors. Second, structured notes tend to be long-term investments, used in the context of an investor's overall investment portfolio goals, rather than a product that is traded based on price fluctuations. Third, in respect of structured notes, we suggest that the investor needs full transparency regarding the structure of the note itself and the issuer of the note, rather than the trading price. A meaningful proxy for trading price of a structured note is the indicative value of the note at any given time which is required to be posted by issuers of Canadian prospectus-qualified structured notes on a daily basis. However, pricing information alone does not provide the transparency regarding the structure of the note that is required by an investor to make an informed investment decision regarding the Foreign Notes. Finally, the proposed minimum listing or "seasoning" period, for a Foreign Note with an initial term to maturity of five years, would be three months, which would, even with robust trading, yield only limited informational value relevant to the investment goals of a Canadian purchaser, where other information on the Foreign Notes is not necessarily available. The limited length of this "seasoning" period raises the possibility that issuers use the foreign-listed structured notes as an end-run around the Canadian

prospectus rules – and in this regard, we note that the proposed length of the seasoning period is shorter than the restricted period applicable to Canadian reporting issuers with a full disclosure record and strict continuous disclosure obligations who privately place securities in Canada.

Compounding the lack of investor protection discussed above, is that issuers of Foreign Notes are unlikely to be Canadian or Canadian reporting issuers. Accordingly, investors may have difficulty enforcing their contractual rights against them under the Foreign Notes. This contrasts with structured notes issued under a Canadian prospectus, where a foreign issuer would have primary liability on the initial offering prospectus, be required to file a submission to jurisdiction and appoint an agent of service for process in Canada, be subject to the filing requirements applicable to a reporting issuer in Canada and be subject to liability under secondary market disclosure provisions of Canadian securities laws. As a reporting issuer, a foreign issuer of structured notes would have significant continuous disclosure requirements at law whereas an issuer of Foreign Notes may be under no obligation to continue to provide Canadian investors any continuing disclosure about the issuer or the Foreign Notes at all.

Finally, Canada enjoys a robust and competitive market for structured notes in which the Canadian banks constantly innovate and compete for “shelf space” on the basis of pricing and product innovation. The banks have a significant reputational stake in this market which they protect through voluntary rigorous internal compliance and training programs and a concern for the overall customer relationship that transcends any one transaction. To offer a competitive advantage for new entrants not subject to similar constraints and discipline in order to facilitate the offering of a less regulated product that does not offer any material advantage to Canadian investors or the market seems ill-advised.

For the above reasons, we urge the Ontario Securities Commission and the Exchange to ensure that any order permitting the Exchange to trade in Foreign Notes be accompanied by a disclosure regime and restrictions on Foreign Notes that are eligible for such trading and other investor protections akin to those available to investors for structured notes under current Canadian prospectus rules, including CSA Staff Notice 44-304 – *Linked Notes Distributed under Shelf Prospectus System*, CSA Staff Notice 44-305 and the novelty pre-clearance regime and ensure that a robust consultation and comment process is followed prior to the implementation of any such order.

If you have any questions regarding the foregoing, please do not hesitate to contact the undersigned at 416.863.5537.

Yours very truly,

(signed) *Robert Murphy*

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