

CDS Clearing and Depository Services Inc. (CDS®)

**Proposed Amendments to CDS Fee Schedule re
New Fees for Linkage Service with Shanghai Clearing House (SHCH Link)**

NOTICE AND REQUEST FOR COMMENT

DESCRIPTION OF THE SERVICE AND PROPOSED AMENDMENTS TO FEE SCHEDULE

A. DESCRIPTION OF THE PROPOSED NEW SERVICE

Background

On October 18, 2018, CDS published a Notice and Request for Comments in respect of proposed amendments to CDS Participant Rules and the implementation of a linkage with the Shanghai Clearing House (SHCH) (http://www.osc.gov.on.ca/documents/en/Marketplaces/cds_20181018_introduction-china-bond-link-service.pdf). Concomitant with the proposed rule amendments, and subject to regulatory approval for the proposed Rules, CDS intends to add fees for the SHCH Link to the CDS Fee Schedule. As a recognized clearing agency under the Ontario Securities Act and the British Columbia Securities Act, and a recognized clearing house under the Quebec Securities Act, CDS is providing this Notice and Request for Comment in accordance with the recognition requirements of each of these jurisdictions.

The present Notice and Request for Comment, including SHCH Link fees listed in Appendix A, is provided pursuant to Sections 7.6 and 7.8 of Schedule B – Terms and Conditions of the Ontario Securities Commission (“OSC”) Recognition Order, pursuant to Articles 26.6 and 26.9 of Recognition Decision 2012-PDG-0142 of the Autorité des marchés financiers du Québec (“AMF”), and pursuant to Section 9 of the British Columbia Securities Commission (“BCSC”) Recognition Order, each as amended.

To further the efforts towards enhancing the efficiency and cost-effectiveness of the clearing and settling of eligible securities for market participants CDS serves, CDS has, and maintains, unilateral and bilateral links with central securities depositories (“CSDs”), including links with CSDs in the United States (bilateral), and France and Sweden (unilateral). These links are intended to provide control, ease of access, and market efficiency, for CDS participants transacting in those markets and for foreign market participants seeking to access Canada’s capital markets.

As described in more detail in the abovementioned Notice and Request for Comments respecting proposed amendments to CDS Participant Rules, CDS has been developing a unilateral fixed income clearing and settlement link with Shanghai Clearing House (“SHCH”). SHCH’s principal business lines include the registration, custody, clearing, settlement, and delivery of fixed income securities, and margin and collateral management for direct and indirect *Renminbi* (RMB) and foreign currency transactions and derivatives transactions.

Proposed New Service: SHCH Link

The proposed SHCH Link is a service providing North American Foreign Institutional Investors (“FIIs”, a term commonly used by Chinese capital markets participants to refer to investors who are domiciled outside of mainland China) who are CDS Participants, and their clients, efficient access to the Chinese Interbank Bond Market (CIBM). The Service will eliminate the need for CDS participants and their clients to become direct members of a CSD and clearing agency in China in order to transact in the CIBM, and is intended to reduce or eliminate the direct costs of market access and technical infrastructure set-up.

This service will be operated outside of, and apart from, CDSX, and will use a new, web-based, Graphical User Interface (GUI) application.

Approved CDS Participants, and their clients (who must also be FIIs; CDS will facilitate FII registration with the People’s Bank of China as a direct member of SHCH) who trade SHCH Link eligible bonds

settling in RMB in North American time zones may clear and settle these trades at SHCH using the SHCH Link interface.

CDS will open an aggregate, omnibus account at SHCH on behalf of all CDS participants. SHCH will not open or maintain separate accounts for CDS clients; rather, CDS will act as a nominee and maintain a record that will segregate the securities held, pro-rata, by our Participants, in discrete accounts for its clients (the “SHCH Link Accounts”).

CDS’s SHCH Nominee Holding Account at SHCH will be used to:

1. Deposit aggregate Chinese bond positions held by FIIs using SHCH Link
2. Act as bond settlement account at SHCH for transactions submitted by FIIs for settlement via SHCH Link. SHCH will debit and credit this account consistent with SHCH agreements with CDS.

B. NATURE, PURPOSE AND IMPACT OF THE PROPOSED AMENDMENTS

CDS proposes to amend its Fee Schedule to establish fees for the use of the Service by CDS Participants. Use of the Service is entirely optional and ancillary to CDS’ existing clearing, settlement, and depository services. CDS proposes to add two specific fees to the Fee Schedule; they are:

- A Maintenance Fee for the opening and maintenance of FII registrations and the record of the CDS Participant’s of securities held by CDS, as nominee, at SHCH. The fee will be calculated based on the number of Foreign Institutional Investors (FIIs) registered as such and wishing to use the SHCH Link, either directly (as a CDS Participant) or indirectly (*through* a CDS Participant). The fee will only apply to Participants who have expressly on-boarded FIIs who wish to take advantage of the SHCH Link service. By way of example, if a CDS Participant is, itself, an FII, and intends to settle transactions on behalf of ten (10) of that Participant’s FII clients, the Maintenance Fee would be 11 times the fee table amount per month.
- A Custody Fee based on the monthly average nominal value of Chinese securities recorded in CDS’s systems as being held in SHCH by CDS for the CDS Participant. This fee will only apply to CDS Participants who have both registered FIIs to use the SHCH Link service, and have a positive balance in their SHCH Link account during the month.

C. THE FEE SETTING PROCESS

Pricing Philosophy

In developing the proposed fees, CDS considered the following principles:

1. Fees should be commensurate with the commercial value that the Service provides to its users (CDS Participants)
2. Fees should encourage the use of the Service
3. Fees should be straightforward for users and should not create undue administrative effort or costs
4. Fees should support the allocation of costs to clients of CDS Participants and should use a set of objective, easy-to-measure, fee drivers.
5. Fees should cover costs for initial and continuous development, operations, risk management, as well as incentives for competition and innovation

Consultation

In preparing the recommendation for SHCH Link fees, CDS consulted with a broad array of stakeholders. Included in the discussion and formation of the recommendation were CDS’ Board of Directors, the CDS Fee Committee, as well as individual discussions with various Participants and investors who may use the

Service. While CDS was not in a position to disclose specific pricing details and methodology in the course of our initial discussions with prospective Participant users of the SHCH Link, we did provide order-of-magnitude estimates with respect to the fees which would attach to the Service in order to gauge market interest.

Comparisons to Alternatives

The Service provides access to the CIBM in a way that is most comparable with the “CIBM Direct” access model, through which Foreign Institutional Investors (FIIs) open accounts, directly, with SHCH, and set up operations in Asian time zones to facilitate post-trade processing.

In particular, the Service eliminates the following CIBM Direct access costs and expenses:

- SHCH fees:
 - Account maintenance fee
 - Per transaction DVP settlement fee
- Correspondent banking fees:
 - In Canada, for on-shoring of funds
 - Account maintenance fee
 - Per-wire transaction fees (incoming and outgoing)
 - in China, for settlements¹
 - Account maintenance fee
 - Per-wire transaction fees (incoming and outgoing)

In addition, the SHCH Link minimizes the following ancillary expenses:

- Operational expenses:
 - Asian time zone staffing costs
 - Translations (between Simplified Chinese and English)
- Legal costs
 - Establishment of SHCH account
 - Establishment of onshore RMB banking relationship(s)
 - Registration of Asian time zone subsidiary or agency relationship (if not already available)

Accessing the CIBM via the CIBM Direct model requires a fixed-cost investment that may be cost-prohibitive for some Participants, or their clients, who may instead require only incremental exposure to Chinese markets and assets. The proposed SHCH Link fees provide a viable alternative that relates service costs directly to level of usage.

Comparisons to Fee Model of Other Services

Conceptually, account maintenance fees and custody fees are commonly charged in custodial products. In developing the fee model for SHCH Link, we considered that these costs align well to the core value proposition of the Service, and determined them to be appropriate fee items for the Service.

D. PUBLIC INTEREST

CDS submits that the proposed charge for SHCH Link, as developed and described in this Notice, are not contrary to the public interest.

¹ A China onshore bank account is not required in the Service’s operating model to effect cash settlement. However, the CIBM Direct access model would require such an account.

E. 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 or the Autorité des marchés financiers' Bulletin to:

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

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Comments received by CDS during the comment period will be made available to the public.

Appendix A: Proposed SHCH Link Fee

New Fee Description	Fee Description	Proposed Fee
SHCH Link Account Maintenance Fee	<p>Fee to cover the maintenance of active Foreign Institutional Investors (“FIIs, in the perspective of mainland China) utilizing SHCH Link, as registered by CDS Participant.</p> <p>This fee is charged at FII level, and full fee applies even if the FII is subscribed to the Service for any part of the month, or has no other billable items for the month.</p>	CAD 100 per FII per month
SHCH Link Custody Fee	Fee to cover volume-driven service costs of the SHCH Link service, calculated based on the Participant’s monthly average nominal custody value converted from CNY to CAD based on average monthly CFETS ² CNY Central Parity Rate for the month.	CAD 0.0002 x monthly average nominal custody value

² CFETS: China Foreign Exchange Trade System