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By email:

Ontario Securities Commission

Re: OSC Staff Notice 33-753 - *OSC Consultation on Tied Selling and other Anti-Competitive Practices in the Capital Markets* (SN 33-753)

Dear Staff:

We are writing in response to your request for comment dated November 29, 2021 regarding the matters set out in SN 33-753. These comments are provided by the lawyers of Torys LLP who are signatories below, in their personal capacities, and not on behalf of the firm or any of its clients.

We understand that the Minister of Finance has asked the OSC to undertake an analysis of concerns identified in the *Final Report of the Ontario Capital Markets Modernization Taskforce* (Taskforce) that certain commercial lenders may be engaging in improper practices that may impede competition. Among other things, SN 33-753 seeks feedback on the Taskforce's recommendation that restrictions on tying commercial lending services and capital markets activities be enhanced in order to facilitate the growth of independent dealers and ensure issuer choice. In particular, the Taskforce recommended that securities legislation or rules be amended to:

1. prohibit registrants, as a consequence of an exclusivity arrangement, from providing capital markets services in certain circumstances;
2. require a senior officer of a registrant to attest that no such prohibited conduct occurred each time the registrant provided such capital markets services to a reporting issuer with whom the affiliated commercial lender has a banking relationship;
3. require an independent underwriter in prospectus offerings where the issuer would be considered to be a "connected issuer" to one or more of the underwriters involved in the offering by virtue of any commercial lending relationship between an affiliate of the underwriter and the issuer; and
4. ban certain restrictive clauses in underwriting agreements where a commercial lending or capital markets relationship exists.

The OSC has a mandate to foster fair, efficient and competitive capital markets, and we support additional resources, supervisory mechanisms and enforcement to identify and expose market-harming anti-competitive behaviour. As we discuss below, however, we believe that robust laws and mechanisms already exist and that securities laws do not need to be expanded or added to further address tied selling.

The options proposed by the Taskforce also raise questions about the potential unintended consequences of interfering with issuer choice (including by directing transaction flow to independent underwriters where the benefits to the issuer or the underwriting process are not apparent) and creating duplicative requirements and overlapping jurisdiction of the responsible regulatory authorities, any of which could lead to increased transaction costs (including increased costs of capital for issuers) and potentially compromise the competitiveness of market participants that focus on servicing Canadian issuers relative to foreign finance providers.

Exclusivity Arrangements

Tied selling is already restricted under the *Competition Act*, the *Bank Act* and National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (NI 31-103). The Companion Policy to NI 31-103 (the CP) states that the tied selling restrictions prohibit an individual or firm from engaging in "abusive sales practices". The CP provides examples of abusive sales and potentially anti-competitive practices such as selling a security on the condition that the client must purchase another product or service from the registrant or one of its affiliates, or a financial institution agreeing to lend money to a client only if the client also acquired securities of mutual funds sponsored by the financial institution. The CP goes on to say that the tied selling restrictions are not intended to prohibit relationship pricing or other beneficial selling arrangements similar to relationship pricing.

Effective legislation, enforcement tools and regulatory expertise in competition matters already exist at the federal level to address anti-competitive behaviour. Therefore, if improper tied selling that impedes competition is occurring in Ontario's capital markets, we believe it would be more effective and efficient for the OSC to work with the Competition Bureau and the Office of the Superintendent of Financial Institutions (OSFI) to best enforce existing laws, and draw upon the Competition Bureau's and OSFI's deep expertise in competition matters and bank conduct, respectively, to address the matter, instead of creating a duplicative and potentially inconsistent regulatory framework.

Independent Underwriter

Currently, the Companion Policy to National Instrument 33-105 – *Underwriting Conflicts* (NI 33-105) states that the mere existence of a debtor/creditor relationship between the issuer and the specified firm registrant does not necessarily give rise to a connected issuer relationship. In practice, many issuers routinely include connected issuer disclosure in their prospectuses when they have lenders that are affiliated with underwriters of their offering, particularly when the proceeds from the offering may be used to repay indebtedness. Therefore, an amendment to NI 33-105 that deems an issuer to be a connected issuer of an affiliate of its lenders would be unlikely to result in any meaningful change in an issuer's prospectus disclosure.

We also note that under the current rules, the existence of a connected issuer relationship does not give rise to an independent underwriter requirement. An independent underwriter is only required under Section 2.1(3) of NI 33-105 if the issuer or selling securityholder is a related issuer of the underwriter. The distinction made in NI 33-105 between a "connected issuer" and a "related issuer" is a meaningful one. A related issuer relationship is based on having a 20%+ voting or equity interest, or being a control person, of an issuer, which understandably gives rise to heightened concerns about independence. By contrast, a connected issuer relationship may exist in any circumstance where a reasonable prospective purchaser may question the independence of the underwriter and the issuer, but where the independence of the underwriter may not necessarily be compromised.

Given that many issuers in Canada have lending relationships with affiliates of one or more of their underwriters, requiring the participation of an independent underwriter in every offering where the issuer receives commercial lending services from an affiliate of an underwriter, mandating a specific percentage of all underwritings be comprised of non-bank owned investment dealers and/or requiring that an independent underwriter act as the lead or co-lead manager or bookrunner would be a significant departure from market practice and could adversely affect capital markets.

Issuers benefit from Canada's highly competitive financial services market. Independent investment dealers play, and can continue to play, an important role in servicing issuers in the Canadian capital markets, including early-stage companies with more limited access to capital as well as more seasoned issuers. In our experience, issuers make decisions about which dealers to retain for an offering based on the issuer's assessment of the structure, cost, service, capabilities, and client service relationships that they find most beneficial. A dealer that is affiliated with a member of the issuer's lending syndicate may be well-positioned to offer the issuer an integrated package of advice and financing options that is based on a holistic view of the issuer's capital structure and funding capacity.

Requiring an issuer to include an independent underwriter in the syndicate, where the issuer has not otherwise identified a commercial need for that dealer's advice or underwriting commitment has the potential to itself create market-distorting effects and inefficiencies, resulting in increased costs and administrative burdens without meaningfully advancing the issuer's interests.

Such requirements could also disadvantage Canadian financial institutions that focus on the Canadian marketplace and provide a wide range of financing services to domestic issuers through their dealers and other affiliates, relative to foreign financing providers, which would be less likely to service Canadian clients with both lending and capital markets relationships and could recommend that Canadian issuers pursue offshore offerings that would not be subject to the proposed rules.

Restrictive Clauses

In our experience, there are valid commercial and even pro-competitive reasons for registered firms to include certain types of time-limited restrictive clauses in engagement agreements for capital markets services. For example, a registered firm that is engaged to help an issuer get ready for an initial public offering (IPO) typically receives all, or almost all, of its compensation through the underwriting fee that it earns only upon the successful completion of the IPO. It would not be unusual, therefore, for the engagement agreement to grant the firm a time-limited right to act or right of first refusal in connection with an IPO that might be commenced following termination of the engagement. Without these clauses, certain issuers might not benefit from the same options or access to firms because of the barriers created by the need for upfront fee payments.

Although we do not think it is necessary or appropriate for securities laws to regulate restrictive clauses in engagement or underwriting agreements, if rules in this area are introduced, we believe that they should apply to all registered firms that provide capital markets services to issuers, not just firms that have an affiliated commercial lender.

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We appreciate the opportunity to comment on SN 33-753 and would be happy to discuss any of our comments set out above with you by phone or by email.

Yours truly,

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