May 1, 2006

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
New Brunswick Securities Commission
Office of the Attorney General, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Legal Registries Division, Nunavut
Registrar of Securities, Yukon Territory

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Dear Mr. Stevenson / Madame Beaudoin:

Re: Proposed National Instrument 24-101 and Proposed Companion Policy 24-101CP on Institutional Trade Matching and Settlement

We are writing to provide the views of the Investment Dealers Association (the Association) in relation to the questions posed in the notice and request for comment on Proposed National Instrument 24-101 and Companion Policy 24-101CP (collectively the Proposed Rules) and on the Proposed Rules themselves. We hope that our views will contribute to the development of regulatory policy in this area, at both the CSA and SRO levels.

Question 1: Should the definition of "institutional investor" be broader or narrower?

When DP 24-401 was published in April 2004, it indicated that the purpose of the Proposed Rules was to "provide a framework in provincial securities legislation for ensuring more efficient post-trade processing of trades in publicly traded securities" by requiring "dealers and their institutional clients to complete the process of trade comparison and matching as quickly as practicable." The presumption of this stated purpose is that trades involving institutional clients generate the most settlement risk to the Canadian securities industry.

While we agree with this presumption, there has been little or no discussion to date of whether the settlement risk for all trade types involving institutional investors and for all categories of institutional investors is material enough to warrant risk mitigation rulemaking for each and every category. Without this discussion, it is difficult to determine whether the current proposed definition of "institutional investor" is too narrow or too broad.

An additional consideration is that trades involving dealers and their institutional investors (both domestic and foreign) take place through multiple dealer systems and account types which may or may not involve settlement with a third party custodian and may involve meeting different settlement requirements (i.e., different foreign settlement requirements). As a result, there are practical considerations in determining the most appropriate definition of "institutional investor" for the purposes of this Instrument.

In summary, the scope of application of this Instrument (which is in part based on the definition of "institutional investor") should reflect the categories of institutional clients and trade types that currently generate the greatest trade settlement risk.

Question 2: Does the definition of "trade-matching party" capture all the relevant entities involved in the institutional trade matching process?

Yes.

Question 3: The scope of the matching requirements of the Instrument is limited to DAP or RAP trades. Should the requirements be expanded to include other trades executed on behalf of an institutional investor? Should the requirements capture trades executed with or on behalf of an institutional investor settled without the involvement of a custodian?

It is our understanding that under the Proposed Rules, DAP and RAP trades involve either a security delivery or receipt by the dealer to or from the institutional client's appointed non-dealer security custodian. As a result, we do not believe that prime brokerage account trades (where the Prime dealer acts as the institutional client's appointed security custodian) would be subject to the proposed matching requirements of the Instrument. We believe prime brokerage account trades should be subject to the proposed matching requirements.

We believe there are also important implications for the Instrument recommendation that matching requirements are to apply to DAP and RAP trades rather than to DAP and RAP

accounts. Specifically, DAP and RAP trades may take place from time to time in a cash account creating a situation where certain account trades would be subject to the matching requirements and others would not. We believe because of the potentially significant operational compliance implications that the scope of the matching requirements should be determined on an account basis rather than on a trade basis.

An alternative would be to amend the Instrument so that it would apply to all DAP and RAP accounts, including those that involve a dealer security custodian. This alternative would not only capture the DAP and RAP account trades currently captured but would also capture prime brokerage account trades where the dealer executing the trade is different from the prime broker custodian. It would also eliminate the need for an "institutional investor" definition, as relatively few retail investors use a third party custodian. The only prime brokerage trading that would not be captured by this revised account scope definition would be trades executed by the prime broker. Under this trading circumstance, there would be no real benefit to the dealer and the custodian matching trade details, since they would be the same organization.

Question 4: Are each of these methods (compliance agreement and signed written statement) equally effective to ensure that the trade-matching parties will match their trades by the end of T? Should trade-matching parties be given a choice of which method to use?

Determining whether both methods are equally effective is largely based on whether both methods are equally enforceable from a compliance standpoint. Provided both methods are equally enforceable, the trade-matching parties should be given a choice.

More important than the issue of equal effectiveness is the structure of both approaches to the contractual method. Both approaches propose for a trade involving a dealer, an institutional client and the institutional client's appointed custodian, that the dealer only must police compliance with the matching requirements. We believe that the proposed Instrument should consider the policing role that should be played by the institutional client's appointed custodian. As a result, we do not believe that the application of either approach to the contractual method should be limited to the dealer / client relationship when it could also be used effectively in governing the client / settlement agent relationship. We therefore recommend that to the extent the custodians are regulated, they should be policing their client relationships in the same manner as proposed for IDA Member firms. This could be achieved by developing a separate client / settlement agent trade matching compliance agreement or amending the Instrument compliance agreement and signed written statement to include custodians.

The time provided to dealers to execute the compliance agreements or the signed written statements (the compliance documentation) is an issue. It is our understanding that under the Proposed Rules dealers will have until July 1, 2006 to obtain the compliance documentation from their institutional clients. We do not believe this provides dealers adequate time and suggest that dealers be given until January 1, 2007, the date under the Proposed Rules when the first matching compliance percentage benchmark must be met, to obtain the compliance documentation.

There also may be opportunities for efficiencies in executing the necessary compliance agreements / signed written statements. We have identified two as follows: (1) the development of a standard industry compliance agreement, and (2) the use of a bare trustee approach whereby the IDA would execute the standard industry compliance agreement on behalf of all of its dealer Member firms with each institutional client.

The use of a standard industry agreement would reduce both the compliance burden for dealers and the agreement review burden for regulators.

The use of a bare trustee approach would eliminate the need for each dealer that trades with a particular institutional client to obtain a separate agreement from that client. Rather, the IDA would execute one agreement on behalf of all of its dealer Member firms with each institutional client. This approach is currently being used by the IDA in executing custodial agreements on behalf of all of its dealer member firms with a custodian that holds client assets. To implement this opportunity, the IDA would need to hire additional staff to manage the obtaining of these bare trustee agreements.

Question 5: Will exception reports enable practical compliance monitoring and assessment of the trade matching requirements?

The Instrument proposes exception reporting for registrants, regulated clearing agencies and matching service utilities. The distinct purpose of each of these intended reporting requirements is unclear. For example, if a registrant chooses to exclusively use a trade matching utility to meet its matching requirement obligations and all trades settle through the same regulated clearing agency, all three reporting requirements will result in the submission of the substantially similar trade matching information by three parties. To extend this example further, if the registrant is an introducing broker, the similar trade matching information would be submitted by four parties.

We believe that a more practical approach would be to receive exception reporting from the recognized clearing agency for the trades that they match and from the matching service utility for the trades that they match that are in turn settled by the recognized clearing agency [and from the registrant for the trades that are not settled by a recognized clearing agency]. Based on analysis of this reporting information and in order to target material non-compliance, additional information could be requested from registrants with the highest non-compliance percentages / values.

Question 6: Is it necessary to require custodians to do exception reporting in order to properly monitor compliance with this Instrument?

Further to our response to Question 4, from a fairness standpoint, the dealer should not be held exclusively responsible for policing compliance with the matching requirements, particularly the compliance of the regulated custodians. It is therefore necessary to require that custodians participate in any exception reporting regime.

Question 7: Is it feasible for trade-matching parties to achieve a *7:30 p.m. on T* matching rate of *98 percent* by July 1, 2008, even without the use of a matching service utility in the Canadian capital markets?

Only a study of the current state of industry trade matching preparedness and an assessment of remaining steps to be taken (along with timelines to achieve them) can answer this question.

Other important questions are:

(i) Is matching by 7:30 p.m. on T the right objective now?

(ii) Is the proposed matching compliance rate a fair benchmark?

(iii) What is the likelihood that the industry will achieve this matching compliance rate?

With respect to the question of whether matching by 7:30 p.m. on T is the right objective now, we believe that other matching cut-off times should be examined to determine the most appropriate matching cut-off time objective that achieves the best compliance cost versus settlement risk reduction balance.

With respect to the question of fairness, there are two aspects to the Proposed Rules which involve IDA Member firms: (i) trade reporting; and (ii) customer compliance monitoring and resolution. The timing of dealer trade reporting is completely under the dealer's control and therefore we believe it is appropriate that the dealer should be held immediately accountable for untimely trade reporting.

The timing of institutional client / custodian trade reporting is not under exclusive dealer control. While the dealer can influence institutional client / custodian trade reporting timeliness by monitoring adherence with the client compliance agreement and by resolving client non-compliance situations, this is ultimately an industry issue, not an individual firm issue. Specifically, where institutional client non-compliance is an issue that affects a dealer's matching compliance rate it will likely be an issue at all dealers that execute trades for the particular client. We would therefore recommend more of an industry solution in such instances rather than holding individual dealers accountable for failing to adequately police the trade reporting timeliness of an individual institutional client.

With respect to the question of compliance likelihood, we believe we are now in an environment where the likelihood of a move to T+1 trade settlement in other countries is less likely in the near to mid term. Because there is now less of a near to mid term settlement competitive threat, industry willingness to take the necessary steps to implement more timely trade matching is waning. Therefore, while a 98 percent matching compliance rate may be feasible, it is not likely achievable without an acceleration in the international move to T+1 trade settlement. Passage and implementation of this Instrument, while extremely important, may not be enough to change this assessment given the significant expenditures that will be required in making the necessary changes to achieve this compliance rate.

Question 8: Are the transitional percentages outlined in Part 10 of the Instrument practical? Please provide reasons for your answer.

Refer to response to Question 7.

The remainder of this letter details our drafting comments on proposed National Instrument 24-101 and Proposed Companion Policy 24-101CP.

Part 1.1 - Definitions

DAP or RAP trade

The definition of "DAP or RAP trade" does not specify whether or not a custodian other than a dealer is involved in the settlement of the trade. In line with our previous comments, we suggest that the wording of the definition of "DAP or RAP trade" be clarified to include situations where the third party custodian is a dealer.

Institutional investor

The definition of "institutional investor" ("institutional client" in the previous draft of the Instrument) has been amended in this draft to include non individuals with net investment assets in excess of $10 million. The commentary in the notice for the proposed Instrument indicates that this change was made to ensure "that the scope of the Instrument includes those institutional investors that do not necessarily use custodians". However, when this defined term is considered in conjunction with the trade matching requirements set out in Part 3 of the proposed Instrument, we do not believe the current draft of the Instrument would apply to institutional investors that do not use a non-dealer custodian. This result is therefore not consistent with the commentary in the notice for the proposed Instrument.

Part 2.1 - Application

It is our understanding that the previous draft limited the scope of the Instrument to institutional trades in depository eligible securities. It is unclear whether this is still the case with the current draft. The removal of interpretive language and the reference in 2.1(d) to the exclusion of only those options and futures contract trades that clear through a clearing house would suggest that the scope in the current draft has been broadened beyond depository eligible securities. Given that there is a certain lack of clarity as to what actually is considered to be a security, it would be helpful if the scope of the securities subject to the Instrument were made specific.

Part 3.1 - Matching deadlines for registered dealer

It is our understanding that there is no intent in the proposed Instrument to mandate the use of either a regulated clearing agency or a matching service utility to perform trade matching. It

therefore seems inconsistent that the 7:30 p.m. trade processing cut-off time used by the Canadian Depository for Securities Limited (CDS) would be proposed as the Instrument's end of trade date, if market participants are not obligated to perform their matching at CDS or anywhere else.

While there are significant merits to establishing a close of business definition, we suggest that any definition established should be determined through discussions with the key trade settlement infrastructure providers and industry participants rather than by selecting the existing trade processing cut-off time used by CDS.

Part 4 and Form 24-101F1 - Reporting Requirement for Registrants

It is highly likely that even if non-compliance with the trade matching timelines is isolated to a relative few number of institutions, that virtually all registrants will be required to report under 4.1(a). This is because the reporting requirement will be triggered when a specified percentage registrant's trades are determined to be non-compliant, whether or not they are responsible for the non-compliant classification. As we are unclear as to what additional information would be provided by these registrant reports (that wouldn't already be available in the regulated clearing agency and matching service utility reports) we would suggest reconsideration of what is likely to be (at least initially) a reporting requirement for all registrants.

Part 5 and Form 24-101F2 - Reporting Requirement for Regulated Clearing Agencies

The reporting requirement for regulated clearing agencies set out in proposed Form 24-101F2 limits the trade entered and trade matched reporting in Tables 1 and 2 of Exhibit A to trades with a T+3 settlement period. This effectively excludes T+1 and T+2 settlement debt trades from any regulated clearing agency reporting even though they are otherwise subject to the requirements of the proposed Instrument. We believe the reporting should be for all trades subject to the matching requirement.

The Exhibit B title "Exceptions" appears to be inaccurate since the information to be reported is matched trade statistics.

Part 6 and Form 24-101F5 - Reporting Requirement for Matching Service Utilities

Two sets of tables: (1) where the institutional client uses an outside custodian and (2) where the dealer acts as custodian, are required in meeting the reporting requirements set out in Exhibit A of Form 24-101F2. A similar requirement should apply in meeting the reporting requirements set out in Exhibit D of Form 24-101F5.

As with Exhibit B of Form 24-101F2, the Exhibit E title "Exceptions" appears to be inaccurate since the information to be reported is matched trade statistics.

Part 10 - Effective Date and Transition

Part 10.1 indicates that the effective date is July 1, 2006 and yet Part 10.2 sets out no minimum matching compliance percentage for the period from July 1, 2006 to December 31, 2006. The implication of this is that a dealer could be offside of the rules on July 1, 2006 by not executing a compliance agreement or signed written statement with each of its institutional customers by that date even though the is no minimum matching compliance percentage to be met. We suggest the Proposed Rules be amended to give dealers until January 1, 2007, the date under the Proposed Rules when the first matching compliance percentage benchmark must be met, to obtain the compliance documentation from their institutional clients.

Thank you for providing us with this opportunity to comment.

Yours truly,

Richard J. Corner
Vice President, Regulatory Policy