Osler, Hoskin & Harcourt LLP
Box 50, 1 First Canadian Place
Toronto, Ontario, Canada M5X 1B8
416.362.2111 MAIN
416.862.6666 FACSIMILE

OSLER

Toronto

Montréal

Calgary

Ottawa

New York

July 19, 2011

Mark DesLauriers
Direct Dial: 416.862.6709
mdeslauriers@osler.com

Sent By Electronic Mail

Canadian Securities Administrators

c/o John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario M5H 3S8
Email: jstevenson@osc.gov.on.ca

and

Me Anne-Marie Beaudoin, Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal, Québec H4Z 1G3
Email: consultation-en-cours@lautorite.qc.ca

Dear Sirs/Mesdames:

Request for Comments - Proposed National Instrument 23-103 *Electronic Trading and Direct Electronic Access to Marketplaces* (the "Proposed Rule")

The comments in this letter are my personal comments (and are not those of the firm or the firm's clients).

I am writing to provide feedback on subsection 6(2) of the Proposed Rule which states that DEA may only be provided to a registrant that is a participant dealer or portfolio manager. According to the Request For Comments, this provision is intended to preclude exempt market dealers from being able to act as DEA clients. The CSA's stated rationale is that a dealer that wants DEA should not be able to "opt out" of the application of the Universal Market Integrity Rules ("UMIR") and should be an IIROC member. It is stated that this exclusion would prevent regulatory arbitrage. The Request for Comments indicates that the CSA is seeking specific feedback on this issue.

In my view, the proposal to preclude exempt market dealers from having DEA (the "EMD Restriction") gives rise to a number of significant concerns and potential unintended consequences for foreign broker-dealers providing brokerage services to Canadian institutional investors. For the reasons discussed below, I believe that the costs

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of adopting the EMD Restriction would significantly outweigh the perceived benefit of preventing regulatory arbitrage.

Reduced Access to Global Electronic Trading Platforms

There are a number of U.S. and other foreign broker-dealers that have registered in Canada as exempt market dealers in order to offer certain types of securities brokerage services directly to institutions and other sophisticated investors in Canada. For the most part, these foreign broker-dealers have obtained the exempt market dealer registration to permit them to trade securities of Canadian issuers listed on U.S. and other foreign securities exchanges with their Canadian customers. The demand from Canadian institutional investors for one-stop global electronic trading services has led the foreign broker-dealers to make arrangements to offer their customers DEA to Canadian marketplaces as well.

Absent registration as an exempt market dealer, U.S. and other foreign broker-dealers are significantly restricted in providing Canadian institutional investors with electronic access to trade securities in U.S. and other foreign marketplaces. This is the case because the International Dealer Exemption does not allow a foreign broker-dealer to trade securities of Canadian issuers with Canadian institutional investors, even though the securities are cross-listed and/or principally traded on a U.S. or other foreign marketplace. In other words, the restriction on trading securities of Canadian issuers turns solely on the domicile of the issuer without regard to the marketplace in which the issuer's securities are traded. This anomaly was the subject of extensive comment when the National Registration Rule was being introduced. The CSA has generally responded to these comments by pointing out that the exempt market dealer registration is available to those foreign broker-dealers that wish to trade in securities of Canadian domiciled issuers with Canadian institutions.

The proposal to preclude exempt market dealers from having DEA to Canadian marketplaces would, if implemented, have the effect, intended or otherwise, of restricting these foreign broker-dealers from providing Canadian institutional investors with direct access to their global electronic trading platforms and brokerage services.

Options and Implications for Foreign Broker-Dealers

The Companion Policy to the Proposed Rule states that, "if a registered dealer wishes to have direct access to marketplaces, then the registered dealer should be an IIROC member and therefore be directly subject to IIROC rules including the Universal Market Integrity Rules (UMIR) if accessing equity marketplaces." Unfortunately, becoming an IIROC member is not an option for a foreign broker-dealer such as a U.S. broker-dealer registered with the SEC and regulated by FINRA. The IIROC rules do not permit a foreign broker-dealer to become an IIROC dealer member. Therefore, the only option for a U.S. or foreign broker-dealer is to form a Canadian subsidiary or affiliate to obtain registration as an investment dealer as well as the IIROC membership required by such registration.

Many U.S. broker-dealers already have affiliated Canadian investment dealers. However, the resources required to replicate the U.S. broker-dealer's electronic trading services in the Canadian investment dealer where it will be subject to IIROC's dealer member rules (which differ in many respects from U.S. broker-dealer regulations) are very significant and for many firms the costs would significantly outweigh the benefits. As well, this model would not serve Canadian institutional investors well as they would no longer have the option of dealing directly with the U.S. broker-dealer's electronic trading "hub" but rather would be subject to the operational inefficiencies of having all of their trade flow routed through the Canadian affiliate, thereby subjecting it to a separate redundant set of controls and filters, with added latency and cost. It would also be impractical for the Canadian institutional investor to route part of its trade flow indirectly through the Canadian affiliate and part of its trade flow directly to the foreign broker-dealer as many Canadian securities are cross-listed on foreign marketplaces and certain trading strategies, such as trades in global equity baskets, require that single trades be executed across global markets. For example, it would be impractical to break up a global equity basket and trade the Canadian names in the basket through the Canadian affiliate and the international names in the basket through the foreign broker-dealer.

Impact of Proposed Rule on Other Business Activities

Many foreign broker-dealers have obtained an exempt market dealer registration to provide non-electronic trading and clearing services to Canadian institutional investors. If these firms must give up their exempt market dealer registration to continue to obtain DEA for their global electronic trading platforms, they would be forced to discontinue providing non-electronic trading and clearing services to Canadian institutional investors. For example, Canadian institutional investors are significant users of the prime brokerage platforms of U.S. broker-dealers. It would be very costly and time consuming for a U.S. broker-dealer to replicate its prime brokerage platform in an affiliated Canadian investment dealer. Without an exempt market dealer registration, a U.S. broker-dealer offering prime brokerage services directly would have to exclude trading in securities of Canadian issuers even when the securities are listed and principally traded in U.S. and other foreign marketplaces. In the prime brokerage services business, this kind of restriction is simply not possible to implement from the foreign broker-dealer's perspective and, even if it was possible, the restrictions on trading securities of Canadian issuers would significantly undermine the value of the service offering from the Canadian institutional investor's perspective. In effect, precluding foreign broker-dealers from obtaining exempt market dealer registration will have the unintended consequence of denying Canadian institutional investors access to the prime brokerage platforms of foreign broker-dealers.

There are other types of business activities conducted by foreign broker-dealers in Canada where an exempt market dealer registration is essential to providing the services for the same reasons as arise in the electronic trading and prime brokerage services context. Foreign broker-dealers would have to choose between no longer having DEA to Canadian marketplaces for their home jurisdiction customers or giving up the exempt market dealer registration and thereby restricting their Canadian institutional customers' access to various other types of services that, as a practical matter, can only be offered directly by the foreign broker-dealer.

I would also note that many foreign broker-dealers registered as exempt market dealers are also registered as portfolio managers. A strict reading of subsection 6(2) of the Proposed Rule would indicate that this type of registrant would be entitled to DEA for all of its Canadian business activities, including those conducted under its exempt market dealer registration. This would appear to be a further anomaly arising from this proposed provision.

Goal of Preventing Regulatory Arbitrage Unlikely to be Served

The stated rationale for the EMD Restriction is prevention of regulatory arbitrage. Presumably the concern is focused on Canadian institutional investors who might seek to avoid the application of UMIR to their trades in Canadian listed securities by accessing the Canadian marketplaces through a foreign broker-dealer that is not a Canadian marketplace participant. However, the trading activity of the Canadian institutions taking this approach will still be subject to the policies, procedures and controls implemented by the Canadian marketplace participant providing DEA to the foreign broker-dealer. The Canadian institutions' trading activity will also be subject to the policies, procedures and controls implemented by the foreign broker-dealer under its agreement with the Canadian DEA provider as well as the risk management controls and supervisory procedures required to be implemented under the rules of the foreign broker-dealer's home jurisdiction. In the case of the U.S. broker-dealers (the single largest affected group), SEC Rule 15c3-5 will impose comprehensive risk management controls and supervisory procedures on DEA providers similar to those imposed under the Proposed Rule.

Looking at it from a different perspective, one should ask why the trading activity of Canadian institutions should be viewed differently from the trading activity of non-Canadian investors throughout the world who are accessing Canadian marketplaces through foreign broker-dealers in jurisdictions that are signatories to the IOSCO Multilateral MOU?

Even if a Canadian institutional investor is required to deal with a Canadian participant dealer that is affiliated with a foreign broker-dealer providing electronic trading services, the electronic trade flow in this case will still be directed through a smart order router to the foreign broker-dealer for routing back through the Canadian participant dealer for execution on Canadian marketplaces. In these circumstances, the trade flow of the Canadian institution will be executed on the Canadian marketplace together with trade flow from non-Canadian investors under the unique identifier assigned to the foreign broker-dealer receiving DEA from its affiliated Canadian participant. As such, the trades of the Canadian institutional investors will be indistinguishable from trades of foreign investors coming from the foreign broker-dealer's "hub". In this context, it is not clear what the additional intermediation by the Canadian investment dealer is adding to prevent regulatory arbitrage. In my view, the CSA should not be creating additional burdens for Canadian investors accessing global electronic trading platforms as long as the Canadian investor's trade flow that is routed to Canadian marketplaces passes through the risk management controls and supervisory procedures of a qualifying foreign broker-dealer as well as the procedures and controls that the Canadian participant providing the DEA must implement under the Proposed Rule.

Constraints on International Trade

For the reasons discussed earlier in this letter, the EMD Restriction would operate to significantly restrict the activities of U.S. broker-dealers currently providing brokerage services to Canadian investors. U.S. broker-dealers requiring access to Canadian marketplaces for their customers will no longer be able to obtain the requisite registration to provide a broad range of brokerage services currently provided to institutions and other sophisticated investors in Canada. In effect, the EMD Restriction will obligate foreign broker-dealers to establish a Canadian affiliate to provide brokerage services to qualifying Canadian investors.

This provision may be viewed by U.S. regulators as an attempt to protect Canadian trade in financial services and may adversely impact the opportunity to obtain a mutual recognition arrangement between Canada and the U.S. Apparently, Canadian investment dealers are not subjected to restrictions on trading US securities with US institutions under Rule 15a-6. This would include providing access to electronic trading services that ultimately access U.S, marketplaces through DEA arrangements. These international trade implications of the proposed EMD Restriction would further support reconsideration of this proposed provision.

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Thank you for the opportunity to comment on the Proposed Rule. If you have any questions regarding my submission, please do not hesitate to contact me.

Yours very truly,

Mark DesLauriers

Mark DesLauriers
Partner
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