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Dear Mr. Stevenson and Mme. Beaudoin:

Re: Canadian Securities Administrators (CSA) Notice and Request for Comment on Proposed Amendments to National Instruments 21-101 – *Marketplace Operation* and 21-103 – Trading Rules

On behalf of the Investment Industry Association of Canada's (IIAC's) Marketplace Operations Working Group, we are pleased to provide comments on the CSA Notice and Request for Comment: Proposed Amendments to National Instrument (NI) 21-101 – Marketplace Operation and National Instrument 23-101 – Trading Rules (the "Proposed Amendments"), released on April 24, 2014. The Marketplace Operations Working Group was formed recently to review the Proposed Amendments and, as you know, the IIAC represents 160 investment dealers regulated by the Investment Industry Regulatory Organization of Canada (IIROC) that work to ensure a smooth and efficient savings-to-investment process to support the Canadian economy. The IIAC's main concern is ensuring strong and efficient markets through effective investor protection and capital formation processes. We know that the CSA and IIROC appreciate the fine balance between the needs of investors, issuers/users of capital, the intermediaries between them and markets in which they operate. Below are our comments on the impact of certain of the Proposed Amendments, with recommendations on how to achieve what our members believe is a better equilibrium.

1. Section 5.10: Confidential Treatment of Trading Information

Section 5.10 of NI 21-101 currently prohibits a marketplace from disclosing a marketplace participant's order and trade information to researchers without the marketplace participant's

consent. We appreciate the CSA's efforts to keep pace with market developments, awareness of the breadth of new dealer and market regulatory requirements, and growing focus on impact analyses before introducing new policy. Our members understand the importance of transparency, and last month, the CSA re-designated CanPX, which the IIAC supports, as an information processor for corporate debt securities under NI 21-101. As the CSA is aware, CanPX's objective is to establish an optimal level of transparency for the Canadian marketplace that balances investors' need for price discovery that can lead to lower prices, while preserving client trade anonymity and dealer market-making capabilities without reducing trading activity and liquidity – also a desirable feature for investors.

As there is a thin line between too little and too much disclosure, there is a possibility that market participants entering orders onto marketplaces, and their clients as originators of the data in question, will experience additional risks while the rewards accrue to third parties despite contractual limitations. Specifically, subsection 4.6(4) of NI 23-103, with Rules 6.1(7), 6.1(9)(a)(ii) and 7.13(2)(c) of IIROC's Universal Market Integrity Rules (UMIR), require the order and trade information to include the market participant's identifier and this would be provided to capital market researchers, allowing the identification of proprietary trading strategies.

We appreciate that the Proposed Amendments recognize that what is being discussed for research is marketplace participants' trading information. Providing to third parties order and trading information is akin to a third party in the IT industry getting access to proprietary code, and efforts to protect information in such cases are well-understood. A market participants' intellectual property is a commercial right with value that is protected through extensive investments in technology, information security and contracts. We believe this concern as it regards market participants has been explained well in the Canadian Securities Traders Association (CSTA) submission on the Proposed Amendments. Briefly, there is no way to correct for the inadvertent or intended misuse of data, which may lead to a curtailment in market participation.

While we cannot quantify the impact of reverse-engineering, similarly the explanatory text accompanying the Proposed Amendments does not provide quantification of the potential benefits. The CSA's reference to the fact that Canadian markets are significantly smaller than those in Europe and experience in the U.S. – and caution exhibited by market regulators of markets significantly deeper than ours that are struggling with the right balance – suggest erring on the side of caution while further analysis and discussion are undertaken.

Recommendations:

- **Process:** We respect the need for and support credible capital markets research. ***The most straightforward solution to concerns of the various stakeholders would be, we believe, to have requests for such research channeled to IIROC, which regulates both marketplaces and dealer participants, and which is in a neutral position to adjudicate between these parties and investor interest*.** IIROC staff have the knowledge and experience to assess the reasonableness

of requests and credibility of researchers (an example of this is IIROC staff's involvement with researchers as part of the self-regulatory organization's Study of High Frequency Trading – Phase III (see MER 13-0125). IIROC staff can review and negotiate agreements signed with third parties receiving confidential information and request term changes as necessary in consultation with the industry. For example, terms should include appropriate standards of care and the opportunity to request senior officers to attest to the destruction of information in the rare situation particularly sensitive data is provided (industry members have extensive expertise and have shared best practices in regard to information security with a number of regulators in the past, promoting higher standards). This would provide consistency and security of approach and, potentially, better manage multiple requests for data. Also, IIROC would be in a position to and should advise dealer participants if information originated through them is being used. Moreover, we believe that it is reasonable for IIROC to charge for the review of appropriate capital markets research and verification requests.

- **Order and trade information:** We believe that the Proposed Amendments represent a change from what our members understood would be the case prior to issuance of the October 3, 2013 OSC Order (the "Order"), namely, industry members believe they were assured that the order and trade information disclosed would be provided in aggregate form, without client-specific identifiers. ***For this reason, we believe that the Proposed Amendments should be modified to exclude trader IDs and potentially other fields***. Also to be excluded, in all but select cases, should be significant shareholder and insider trade markers, which can be used in combination with public shareholder disclosures to identify activities of large institutional investors.

- **Definition of "capital markets research" and "verification":** Proposed NI 21-101 paragraph 5.10(1.3)(a) would permit the release to a publication of order and trade information for verification purposes. The proposed changes to section 5.10 of NI 21-101 do not reflect the language of the Order, which includes a "bona fide" qualifier immediately before "capital markets research"; as well, the terms of "capital markets research" and "verification" are currently undefined. ***Provided that the process of having IIROC review requests is adopted as recommended, such definitions can evolve through procedures and guidance developed by IIROC.*** If this recommended process is not adopted, we strongly believe that the terms must be carefully defined and that further consultation on this point is warranted.

- **Data security:** It is widely accepted that for every improvement in information technology security there is a comparable effort to "break" that security. The investment industry, due to its clients and the nature of its business that rely more than most others on confidence and confidentiality, has invested heavily in information security measures, which leads us to make two points:

    - ***Assuming adoption of our recommendation regarding involvement of IIROC in the "capital markets research" definition process, we believe that IIROC staff should satisfy themselves that those parties seeking to use the information for capital markets research, and those***

wishing to verify that research, have comparably strong information security protocols, meet other suitable requirements, and enter into appropriate agreements addressing all of the below:

(i) prevent breaches;
(ii) monitor for the protection of confidentiality;
(iii) provide for the notification of appropriate parties in the case of actual or possible breaches of confidentiality (that is, not only marketplaces and regulators under NI 21-101 subparagraph 5.10(1.1)(a)(vi) and paragraph 5.10(1.2)(a), but also marketplace participants);
(iv) permit the identification and tracing of those who breached confidentiality obligations, especially when confidential information obtained by researchers is disclosed to further third parties under subparagraph 5.10(1.1)(a)(i);
(v) assign responsibility for assessment and collection of damages stemming from the breach; and
(vi) specify unambiguously when and how confidential information is to be returned to the data originator or destroyed, including definition of what constitutes a "reasonable amount of time" after completion of the research and publication process under NI 21-101 subparagraph 5.10(1.1)(a)(iv).

- Absent adoption of the previously noted proposed role for IIROC, we recommend that the CSA consider whether sufficient attention has been directed to the potential for more serious cyber-security attacks and, and at the margin, systemic risk and impact on confidence in Canadian capital markets from the potential derivation of confidential data from information ostensibly used for capital markets research under the Proposed Amendments as currently drafted.

2. Information transparency for government debt securities

The IIAC supports the CSA's proposal to delay imposing requirements that would mandate transparency in government debt and extend the exemption from transparency for government debt securities until January 1, 2018. We believe that there have been significant advances in debt market transparency delivered by the marketplace since the original government debt transparency exemption was put in place in 2003. Additionally, the prevalence of electronic trading in government debt securities in Canada today has also contributed favourably to price discovery. We also note that CanPX, the designated information processor for Canadian corporate debt markets, continues to voluntarily provide transparency on government debt transactions. These market developments have been in response to investor interest and competition in this space, and have resulted in Canadian investors having much improved access to pre- and post-trade information on government debt securities. The CSA, with the industry, should continue to monitor developments in other jurisdictions and their impacts on local markets.

3. Section 12: Marketplace systems and business continuity planning

We agree that the high degree of connectivity among marketplaces and marketplace participants required for not only electronic equity trading, but also trading, clearing and settlement generally, means that the impact of marketplace systems failures can have wide-reaching and unintended consequences. We hope to work with other interested parties on these matters, including greater transparency regarding marketplace testing environments, the use of industry-wide test symbols in marketplace production environments and for marketplace requirements related to business continuity planning to be equivalent to those of marketplace participants, consistency in dealing with security breaches, and other marketplace technology-related matters.

4. Other

While beyond the immediate scope of this request for comments, we recommend that the CSA consider the broader impact of cumulative regulatory changes on investors directly and through competitors – those that are regulated extensively, lightly and at times not at all. Greater transparency and other investor protection measures benefit investors until that point that prices have risen and/or services have become more limited and less accessible to those that need them.

Conclusion

We appreciate the opportunity to comment on the Proposed Amendments and would be pleased to answer any questions that you may have. We may have further comments to make and look forward to meeting with CSA representatives to discuss our concerns and assist in the rule development process.

Yours truly,

Cc:
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