Purpose of this Notice

Staff (staff or we) of the Canadian Securities Administrators (the CSA) have issued this notice (the Notice)

- to highlight the CSA’s consideration of concerns raised by Canadian institutional investors over reduced access to international dealers to trade foreign-currency-denominated fixed income securities issued by Canadian issuers;
- to clarify the scope of the international dealer exemption in National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations (NI 31-103) in relation to trades in foreign-currency-denominated fixed income securities of Canadian issuers; and
- to outline the circumstances in which staff would be prepared to recommend exemptive relief to facilitate greater access to global fixed income markets by Canadian issuers and Canadian institutional investors.

The CSA are aware of reports by some market participants of a perceived decline in liquidity in the Canadian fixed income markets, and understand that some market participants have suggested that recent changes in the securities regulatory regime in Canada may have contributed to this perceived decline. Accordingly, we are publishing this guidance to clarify the scope of the international dealer exemption in NI 31-103 and to confirm staff’s willingness to support exemptive relief, if required, to facilitate access to global fixed income markets by Canadian issuers and Canadian institutional investors.

Background

The CSA, in consultation with the Bank of Canada, the Investment Industry Regulatory Organization of Canada (IIROC) and other stakeholders, have been monitoring a number of potential financial system vulnerabilities in Canada, including reports of a perception by some market participants of a decline in liquidity in the Canadian fixed income markets.1

In addition, the CSA are participating in work being conducted by the International Organization of Securities Commissions (IOSCO) with a view to examining the state of liquidity in global fixed income markets. Specifically, as reported in the IOSCO report entitled Examination of Liquidity of the Secondary Corporate Bond Markets, IOSCO did not find substantial evidence showing that liquidity in these markets has deteriorated markedly from historic norms for non-crisis periods. Its conclusions were based on a detailed analysis of liquidity metrics, survey results from industry and regulators, roundtables with industry, and a review of academic, government and other research articles.2

The CSA have also been consulting with a number of stakeholders, including representatives from the Canadian Bond Investors’ Association (the CBIA), over concerns that recent actions taken by certain foreign dealers in relation to their participation in fixed income markets may have affected the ability of Canadian institutional investors to trade foreign-currency-denominated debt securities of Canadian issuers in global fixed income markets.3

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2 The 2016 Liquidity Report was published on August 5, 2016 and is available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD537.pdf.
3 We understand that stakeholders have also expressed a concern regarding reports of exempt distribution required under National Instrument 45-106 Prospectus Exemptions. These concerns are being considered separately by the CSA.
We are sensitive to the concerns that a reduction in market liquidity can increase the costs and risks to Canadian asset managers and other institutional investors in terms of complying with their mandates, and to corporate and other debt issuers in obtaining necessary financing.

We are publishing this guidance to address any misperceptions that may exist in relation to the scope of the international dealer exemption in NI 31-103 and to confirm our willingness to support exemptive relief to facilitate access to global fixed income markets by Canadian issuers and Canadian institutional investors.

**Recent changes in market practice**

We understand that a number of international dealers have recently advised their Canadian institutional clients that they are unable to trade debt securities of Canadian issuers with Canadian clients due to recent changes in the securities regulatory regime in Canada. While in some cases the Canadian investment dealer affiliates of these firms are able to conduct this trading with the Canadian institutional clients, in other cases, the investment dealer affiliates may be unable to offer a comparable level of access to global fixed income markets.

As a result of these developments, a number of stakeholders have expressed concern that Canadian institutional investors, including Canadian pension funds, investment funds, and other asset managers, are facing difficulties in being able to invest in certain debt offerings of Canadian issuers, such as U.S.-dollar-denominated debt offerings that are offered primarily outside of Canada, and are therefore placed at a competitive disadvantage to their international peers.

**Clarification of the scope of the international dealer exemption**

Subsection 8.18(2)(b) of NI 31-103 provides that, subject to certain conditions, the dealer registration requirement does not apply in respect of “a trade in a debt security with a permitted client during the security’s distribution, if the debt security is offered primarily in a foreign jurisdiction and a prospectus has not been filed with a Canadian securities regulatory authority for the distribution”.

Accordingly, an international dealer that meets the relevant conditions may trade debt securities of any issuers, including foreign-currency-denominated fixed income securities offered by Canadian corporate and governmental issuers, with Canadian institutional investors at the time of the offering of the securities if the offering is made primarily outside of Canada and the issuer has not filed a prospectus in Canada in connection with the offering.

We acknowledge that the international dealer exemption does not explicitly address the question of the resale of or secondary trading in such securities by Canadian institutional investors, whether to another institutional investor in Canada or to a person or company outside of Canada.

Staff do not believe there is a policy reason to limit the exemption in subsection 8.18(2)(b) to trades that occur during the initial period of the securities’ distribution or to conclude that an international dealer should be permitted to sell a debt security to a Canadian institutional investor but not be permitted to act for the institutional investor in connection with the resale of the security. However, we acknowledge that concerns over the current drafting may be affecting the willingness of international dealers to participate in Canadian fixed income offerings denominated in a foreign currency on behalf of Canadian institutional clients.

Accordingly, staff are publishing this guidance to confirm that staff are prepared to recommend exemptive relief to permit international dealers to deal with institutional investors to facilitate resales of such debt securities, whether to another institutional investor in Canada or to a person or company outside of Canada, provided such debt securities are not listed, quoted or traded on a marketplace in Canada, subject to conditions the CSA consider appropriate.

We also acknowledge that there may be circumstances where, at the time of a resale of a debt security, it is difficult to determine whether the debt security was originally offered as part of an offering that was made primarily in a foreign jurisdiction and whether a prospectus was filed in Canada in connection with such offering. We are in discussions with stakeholders with a view to confirming the extent to which this issue exists and will consider recommending exemptive relief to address this concern if necessary.

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4 These conditions generally require the international dealer to have its head office or principal place of business in a foreign jurisdiction, to be registered as a dealer in the foreign jurisdiction, to trade only with issuers of securities or permitted clients, to make a submission to jurisdiction and appointment of agent filing, and to provide certain risk disclosures to the permitted client relating to its status as an international dealer.

5 The term “permitted client” is defined in section 1.1 of NI 31-103 and generally refers to various types of institutional investors.
Staff may recommend an amendment to the international dealer exemption to address these concerns in the context of pending amendments to NI 31-103. Pending such amendment, staff in certain jurisdictions may also recommend that these concerns be addressed through a blanket order. If you have any comments, please direct them to the staff listed below.

Questions
If you have questions regarding this Notice, please refer them to any of the following:

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