



March 8, 2023

**VIA ELECTRONIC SUBMISSION**

British Columbia Securities Commission  
Alberta Securities Commission  
Financial and Consumer Affairs Authority of Saskatchewan  
Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
New Brunswick Financial and Consumer Services Commission  
Prince Edward Island Office of the Superintendent of Securities  
Nova Scotia Securities Commission  
Newfoundland and Labrador Office of the Superintendent of Securities  
Northwest Territories Office of the Superintendent of Securities  
Office of the Yukon Superintendent of Securities  
Nunavut Office of the Superintendent of Securities

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**Re: Joint CSA and IIROC Staff Notice 23-329 - *Short Selling in Canada***

Cboe Global Markets, Inc., Neo Exchange Inc. (“NEO”), and MATCHNow (collectively, “Cboe”) appreciate the opportunity to respond to the Joint Canadian Securities Administrators’ (“CSA” or “CSA Staff”) and Investment Industry Regulatory Organization of Canada (“IIROC” or “IIROC Staff”) Staff Notice 23-329 – *Short-Selling in Canada* (“Staff Notice”).<sup>1</sup> Cboe commends the CSA

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<sup>1</sup> Cboe Global Markets, Inc. is a provider of trusted market infrastructure and tradable products. Cboe delivers trading, clearing and investment solutions to market participants around the world and across multiple asset classes including equities, derivatives, FX and digital assets. Both NEO and MATCHNow are Cboe Global Markets, Inc. companies.

and IIROC for undertaking this review as a consequence of the numerous comments provided in response to the CSA Consultation Paper 25-403 – *Activist Short-Selling*, which raised concerns about short selling activities other than those related to activist short selling.

For the avoidance of any doubts, our responses to this review do not include any considerations with respect to activist short selling. NEO provided a response to the CSA Consultation Paper 25-403 – *Activist Short-Selling* on March 3, 2021.

### **General Considerations**

As a global markets' operator, familiar with regulatory regimes across multiple jurisdictions and informed by NEO's specific experience as one of Canada's recognized stock exchanges, we believe improvements to the Canadian short selling regulatory framework can be achieved to reduce systemic risk and predatory short selling activities.

As an initial matter, we note that Cboe concurs with the following views expressed in the Staff Notice and corroborated by numerous academic and regulators' studies:

- Short selling plays an important role in the financial markets by contributing to liquidity and facilitating price discovery.
- The uptick rule, as it was in place in the US until July 2007 and in Canada until March 2012, did not prove to be an effective tool to restrict significant and rapid systemic price declines and could have had a negative impact on liquidity and price discovery. Cboe does however recommend that regulators consider the "Circuit Breaker Rule" implemented by the SEC in February 2010, by amending Rule 201 of Regulation SHO<sup>2</sup>. This rule should only be considered within the frame of issuers listed on a non-venture exchange, considering the high degree of volatility of companies listed on venture exchanges.

The central observations Cboe wants to bring to CSA and IIROC Staff's attention can be summarized as follows:

- The absence of a pre-borrow or locate requirement for short selling and the lack of mandatory buy-in or close-out for short sale driven settlement failures leads to two consequences:
  - It exposes the Canadian financial markets to systemic risk<sup>3</sup>.
  - It facilitates predatory short selling when informed market participants short sell stocks ahead of the public announcement of a bought deal under a prospectus offering or as part of a private placement, harming issuers, their shareholders, and the investors trading against the short sellers.
- The current data reported to and, where applicable, made available by IIROC is not sufficient to provide timely information to the market or market regulators to be able to

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<sup>2</sup> See US Code of Federal Regulation, Title 17, Chapter II, Part 242, *Regulation SHO - Regulation of Short Sales - eCFR :: 17 CFR Part 242 - Regulation SHO - Regulation of Short Sales*.

<sup>3</sup> By systemic risk, under the discussed scenario, we refer to the settlement failure of one or more dealers that propagates across the industry and causes significant disruption to the Canadian clearing and settlement function causing significant financial losses and undermining investor confidence.

properly identify and address predatory short selling or to mitigate a scenario that could lead to a systemic failure:

- Current periodicity for reporting short sale volumes and positions, and failed trade data per issuer does not provide for the granularity that would allow to identify certain predatory short selling behaviours or to take mitigating actions in case of a settlement failure that could contaminate the Canadian financial system.
- Current short sale data is limited to the data provided by Canadian investment dealers and does not consider short selling information held by both domestic and global custodians or dealers operating outside of Canada, leading to a limited view of reality.
- Current short sale data is at times erroneous, as it appears that under certain circumstances certain dealers open and report a short position in anticipation of an incoming transfer of securities.

Cboe notes that these deficiencies put Canada out of step with short selling regulations in other jurisdictions such as the United States, the European Union and Australia, and believes that Canadian regulations are not consistent with the first two principles of the March 2009 IOSCO Technical Committee report *Regulation of Short Selling*<sup>4</sup>.

To address these deficiencies, Cboe recommends the following amendments in Canada’s current short sale regulatory regime:

- Implement pre-borrow or locate requirements in line with Recommendation 25 of the January 2021 *Capital Markets Modernization Task Force Final Report*<sup>5</sup>.
- Implement close-out provisions in line with Recommendation 25 of the January 2021 *Capital Markets Modernization Task Force Final Report*<sup>6</sup>.
- Require daily publication of short sale volumes and positions, as well as failed trade data.
- Require Canadian market participants, which are currently exempt from short sale reporting, to submit short sale volume and position data daily.
- Pursue an information exchange mechanism with regulators in other jurisdictions where Canadian securities are actively traded, to obtain short sale volume and position data about Canadian issuers.
- Prohibit short selling in connection with prospectus offerings and private placements in line with Recommendation 26 of the January 2021 *Capital Markets Modernization Task Force Final Report*<sup>7</sup>.
- Consider the “Circuit Breaker Rule” implemented by the SEC in February 2010.

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<sup>4</sup> *Regulation of Short Selling*, Consultation Report, March 2009, Section 3, Technical Committee of the International Organization of Securities Commissions - [Regulation of Short Selling \(iosco.org\)](https://www.iosco.org).

<sup>5</sup> Capital Markets Modernization Task Force, Final Report, January 2021, Recommendation 25 - [Capital Markets Modernization Taskforce: Final Report January 2021 | Ontario.ca](https://www.ontario.ca/en/consultations/capital-markets-modernization-taskforce-final-report-january-2021).

<sup>6</sup> Ibid.

<sup>7</sup> Capital Markets Modernization Task Force, Final Report, January 2021, Recommendation 26 - [Capital Markets Modernization Taskforce: Final Report January 2021 | Ontario.ca](https://www.ontario.ca/en/consultations/capital-markets-modernization-taskforce-final-report-january-2021).

<sup>8</sup> See also US Code of Federal Regulation, Title 17, Chapter II, Part 242, Regulation M - Short Selling in Connection with a Public Offering - [eCFR :: 17 CFR 242.105 -- Short selling in connection with a public offering](https://www.ecfr.gov/current/title-17/chapter-II/part-242/subpart-1/section-242.105).

Cboe believes that not addressing the above-mentioned deficiencies in Canada's short selling regulatory framework is detrimental to the integrity and effectiveness of Canada's financial market and could impact investor confidence. Decisive and timely action is required.

In addition, regulators should leverage existing regulatory requirements, currently available to them, to address some of the predatory short selling activities discussed above in line with some of the considerations discussed under Recommendation 26 of the January 2021 *Capital Markets Modernization Task Force* Final Report<sup>9</sup>.

Please find below our answers to the specific questions raised in the Staff Notice.

### **Short Selling and Pre-borrow Requirements**

**Question #1:** *Should the existing regulatory regime around pre-borrowing in certain circumstances be strengthened? What requirements would be appropriate? Specifically, should there be "pre-borrow" requirements similar to those in the U.S., as described above? Please provide supporting rationale and data.*

**Question #2:** *What would be the costs and benefits of implementing such requirements?*

Please see our General Considerations.

Further, Canadian regulators have historically taken the position that the unique characteristics of the Canadian market justify a more lenient short sale regulatory regime than in other jurisdictions:

- Studies showing that short selling is not a factor in failed trades<sup>10</sup>.
- The size of Canada's financial market requiring more flexibility to facilitate capital raises through bought deals.

Cboe is not in agreement with this view for the following reasons:

- The Failed Trade Study conducted by IIROC in 2022 indicated a meaningful correlation between CNS failure and short positions reported to IIROC<sup>11</sup>.
- Numerous foreign investors are reluctant to participate in Canadian bought deals as a consequence of the predatory short selling activities that accompany many of these deals, preventing Canadian issuers from having access to substantial capital pools available outside of Canada.
- None of these reasons, even if they were to be correct, justify the risk of exposing Canada to a higher degree of systemic risk than other jurisdictions, nor does they justify the adverse consequences on investors and issuers.

With respect to costs, Cboe acknowledges that implementing pre-borrowing will increase costs, but these costs will be passed through to the short seller. This will, like in other jurisdictions,

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<sup>9</sup> Ibid.

<sup>10</sup> See IIROC 2007 Failed Trade Study.

<sup>11</sup> See IIROC 2022 Failed Trade Study, Section 4.D. - [IIROC Failed Trade Study | IIROC](#).

contribute to more discipline by the short sellers.

### **IIROC's Extended Failed Trades Requirements**

**Question #3: *Does the current definition of a “failed trade”, as described in Part 1, above, appropriately describe a failed trade?***

Cboe believes the definition is appropriate.

**Question #4: *Should a timeline shorter than ten days following the expected settlement date be considered? What would be an appropriate timeline? Please provide rationale and supporting data.***

Please see our General Considerations and, more specifically, Recommendation 25 of the January 2021 Capital Markets Modernization Task Force Final Report<sup>12</sup>.

### **Transparency of Short Selling Positions**

**Question #5: *Should additional public transparency requirements of short selling activities or short positions be considered? Please indicate what such requirements should be and the frequency of any disclosure. Please also provide a rationale and empirical data to support your suggestions or to support why changes are not needed.***

**Question #6: *Should additional reporting requirements regarding short selling activities be considered by the securities regulatory authorities? Please indicate what such requirements should be and the frequency of any disclosure. Please also provide a rationale and empirical data to support your suggestions or to support why changes are not needed.***

Please see our General Considerations.

In addition, within the frame of its gatekeeper role, NEO has provided regulators with various examples of what it deemed to be predatory short selling within the frame of bought deals. These examples demonstrated the need for access to additional information beyond what is provided by the Canadian investment dealers.

**Question #7: *As noted above, IIROC's study of failed trades showed that correlations between short sales and settlement issues in junior securities were more significant, and that junior securities experience more settlement issues compared to other securities. Should specific reporting, transparency or other requirements be considered for junior issuers? Please provide additional relevant details to support your response.***

Cboe believes that the same requirements should apply to all types of issuers when it comes to transparency.

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<sup>12</sup> Capital Markets Modernization Task Force, Final Report, January 2021, Recommendation 25 - [Capital Markets Modernization Taskforce: Final Report January 2021 | Ontario.ca](#).

**Buy-in and Close-out Requirements**

**Question #8: *Would mandatory close-out or buy-in requirements similar to those in the U.S. and the European Union be beneficial for the Canadian capital markets? Please provide rationale and data substantiating the costs and benefits of such requirements on market participants.***

Please see our General Considerations and, more specifically, Recommendation 25 of the January 2021 Capital Markets Modernization Task Force Final Report<sup>13</sup>.

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We commend the CSA's and IIROC's efforts to address the short sale issues in the Canadian marketplace and welcome the opportunity to further discuss our views. Please do not hesitate to contact us if you have any additional questions or comments.

Sincerely,



Jos Schmitt  
President & CEO  
Neo Exchange Inc.



Dmitri Smidovich  
Head of Regulatory & Legal  
Neo Exchange Inc.

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<sup>13</sup> Ibid.