

March 30, 2015

**BY EMAIL**

Dear Sirs/Mesdames:

Alberta Securities Commission  
Autorité des marchés financiers  
British Columbia Securities Commission  
Manitoba Securities Commission  
Financial and Consumer Services Commission (New Brunswick)  
Nova Scotia Securities Commission  
Ontario Securities Commission

Josée Turcotte, Secretary  
Ontario Securities Commission  
20 Queen Street West Suite 1900, Box 55  
Toronto, Ontario M5H 3S8  
E-mail: [comments@osc.gov.on.ca](mailto:comments@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  
E-mail: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)

**Re: CSA CONSULTATION PAPER 92-401 *Derivatives Trading Facilities* (the  
“Proposed Amendments”)**

The Canadian Advocacy Council<sup>1</sup> for Canadian CFA Institute<sup>2</sup> Societies (the CAC) appreciates the opportunity to comment on and wishes to provide comments on the following specific questions posed with respect to the Proposed Amendments.

---

<sup>1</sup>The CAC represents the 14,000 Canadian members of CFA Institute and its 12 Member Societies across Canada. The CAC membership includes portfolio managers, analysts and other investment professionals in Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. See the CAC's website at <http://www.cfasociety.org/cac>. Our Code of Ethics and Standards of Professional Conduct can be found at <http://www.cfainstitute.org/ethics/codes/ethics/Pages/index.aspx>.

<sup>2</sup> CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors' interests come first, markets function at their best, and economies grow. CFA Institute has more than 119,000 members in 147 countries and territories, including 112,000 CFA charterholders, and 143 member societies. For more information, visit [www.cfainstitute.org](http://www.cfainstitute.org).

### **Defining “Derivatives Trading Facility”**

1. *Is the DTF category appropriately defined? If not, what changes are needed and why?*

Yes, the DTF category is appropriately defined.

2. *Is it appropriate to permit a DTF operator a degree of discretion over the execution of transactions? Why or why not? If discretion is permitted, should it be permitted only for trading in products that have not been mandated to trade on a DTF?*

It is appropriate to permit a DTF operator a degree of discretion over the execution of transactions because it provides additional flexibility for clients. Discretion should be permitted for trading in some products that are mandated to trade on a DTF, such as semi-standard swaps (e.g. CDS, IRS).

### **Permitted Execution Methods**

3. *Is the description of permitted execution methods for a DTF suitable for facilities that currently offer or plan to offer trading in OTC derivatives?*

We are of the view that the description of permitted execution methods is exhaustive and thus suitable for facilities that offer or plan to offer trading in OTC derivatives.

4. *Please comment on required modes of execution. Should any particular minimum trading functionality be prescribed for DTFs generally?*

Given the broad scope of the Proposed Amendments, an order book or an RFQ should be the minimum trading functionality prescribed.

### **Regulatory Authorization of DTFs**

5. *Is the proposed regulatory framework for DTFs appropriate?*

We agree that the proposed regulatory framework is appropriate.

6. *Is it appropriate to impose dealer requirements on a DTF where the operator of the DTF exercises discretion in the execution of transactions? (Please explain.) If so, should such a DTF be required to register as a dealer, or should only certain dealer requirements be imposed on the DTF? (Which ones?)*

We do not believe that it would be appropriate to impose all of the dealer requirements on a DTF in these circumstances. We believe that the dealer requirements currently applicable to exempt market dealers that address conflict of interest matters and financial solvency would be relevant to a DTF where the operator exercises discretion. We note that while it will be important that the operator of the DTF be subject to regulatory oversight and scrutiny, the functions of an operator exercising discretion in matching orders is different

from an entity that is in the business of trading. If the operators were required to register as a dealer subject to all of a dealer's obligations, it could increase their operating costs which could be passed on to the end users.

*7. To address conflicts of interest, should a DTF that exercises discretion in the execution of transactions be required to exercise this functionality in a separate affiliated entity? Why or why not?*

We do not believe it would be necessary for a DTF to exercise discretion in a separate affiliated entity. The DTF would likely lose some operational and regulatory efficiencies if they were required to operate two entities, and clients could be subject to additional administration and costs if they were forced to deal with two entities. It would be more efficient for clients, and potentially for collateral management, if only one entity was required. As noted above, we do not believe that full dealer registration should be required in these circumstances but that a level of regulation and oversight may be desirable depending on the model of the DTF. From a registration and surveillance perspective, a single entity could be easier to monitor, and would have fewer related party conflicts to manage.

*8. What factors are relevant in defining the proposed best execution duty?*

With respect to the derivatives contemplated by the Proposed Amendments, it is difficult to quantify the factors in any specific case that would be relevant in defining the proposed best execution duty, resulting from the fact that these derivatives are non-standardized and thus each trade must be examined on a case by case basis. The factors that may be relevant are not just temporal factors; the attributes of the derivative being written or bought will help in the determination. Outside of an RFQ competitive quote situation it will be very difficult to define the duty. The implementation of the best execution duty is complex and ambiguous, as illustrated by the comprehensive CFA Institute Trade Management Guidelines for investment firms which was developed by the CFA Institute Trade Management Task Force, which sets out a framework for firms to make consistently good trade-execution decisions.

### **Organizational and Governance Requirements**

*9. Is it appropriate to allow a DTF to require clearing of all trades on the DTF that are capable of being cleared?*

Our response to questions #9, #10 and #11 depend in part on the number of DTFs operating in Canada. While it is appropriate to allow a DTF to require clearing of all trades that are capable of being cleared, it may not also be appropriate to allow that same DTF to mandate that certain clearing agencies or trade repositories be used, particularly if they are related entities. It should be the choice of the participant as to which facility they wish to use in order to clear their trades. Clients who do not want to be forced to clear trades through a particular clearing agency will deal with DTFs that do not have such a requirement.

10. *Is it appropriate to allow a DTF to require transactions executed on its facility to be cleared through a particular clearing agency and/or reported to a particular trade repository?*

Please see our response to #9 above.

11. *Is it appropriate for a DTF that exercises discretion in trade execution to be permitted to limit access to its facility? If so, on what grounds should it be permissible?*

We do not have a view as to whether or not a DTF that exercises discretion should be permitted to limit access to its facility. In the event DTFs are permitted to limit access, the criteria for determining access should be clear and disclosed to potential participants.

12. *Are the proposed organizational and governance requirements for DTFs appropriate? Are there additional organizational and governance requirements that the Committee should consider?*

Yes, we believe the proposed organizational and governance requirements are robust and appropriate.

13. *Is it appropriate that a DTF that does not exercise execution discretion be permitted to perform its regulatory and surveillance functions itself, or should it be required in all cases to engage a third-party regulation services provider for this purpose? Please explain.*

In order to encourage economic business models we believe that for most cases, it is appropriate that a DTF that exercises discretion be permitted to perform its regulatory and surveillance functions itself, provided that it is subject to regulatory audits. There is a lesser chance of a conflict of interest in the circumstances where the DTF does not exercise execution discretion. DTFs should however have the option of utilizing a third-party regulation service provider for this purpose if they so choose. In addition to being able to engage a third party regulatory service provider should they choose to do so, the regulators could require such an engagement if the unique aspects of a particular DTF's discretion or business model so warrants.

14. *Do you agree with the proposal to prohibit DTF operators from entering into trades on their platforms as principals, on their own accounts? Please explain.*

Such a proposal will help mitigate conflict of interest concerns.

15. *How should the sufficiency of a DTF's financial resources be evaluated? Please comment on the methodology and frequency of the calculation.*

A DTF's financial resources should be evaluated similar to those used for recognized exchanges and clearing agencies to the extent there is an inherent or related clearing business as part of the DTF, or if there is not, similar to the evaluation process of other jurisdictions (such as that used in the United States for SEFs).

### **Pre-trade Transparency**

16. *Should pre-trade transparency requirements apply to OTC derivatives that trade on DTFs but that have not been mandated to be traded on DTFs? If yes, what requirements should apply, and should any exemptions be provided?*

No, we do not believe pre-trade transparency requirements should apply to OTC derivatives that have not been mandated to be traded on DTFs. However, if pre-trade transparency requirements will apply, indicative (non-firm) bids and offers may be appropriate.

### **Post-trade Transparency**

17. *Are the proposed post-trade transparency requirements (involving real-time trade reporting as well as public reporting of certain daily data) appropriate for DTFs?*

Yes the proposed requirements are appropriate.

18. *What is the preferred method for real-time public reporting of transactions executed on a DTF (i.e., directly by a DTF, via trade repositories, or some other method)? What are the advantages and disadvantages of the proposed options?*

We think the most efficient reporting could be done via trade repositories, assuming that reported trades are the sum of all the trades executed in the DTFs reporting to the trade repositories. Such reporting lines should provide a greater potential to preserve confidential information of participants. If a DTF provided real time public reporting directly, there could be a greater opportunity for market participants to identify confidential information.

19. *When should deferred publication of trade information be permitted? Are there circumstances other than block trades?*

Deferred publication of trade information should be permitted in the event of illiquidity (i.e. below a certain volume/trade count threshold). There should be a mechanism to prevent disclosure where the situation warrants delayed disclosure.

20. *Assuming that deferred publication of trade information should be permitted for block trades, what criteria should be considered when determining the minimum block trade threshold size to permit deferred trade disclosure?*

Criteria to be considered should include the instrument type, currency of the instrument, historical liquidity of the instrument (total notional amount and trade count), as well as settlement risk. The criteria should be reviewed at regular intervals (e.g. every six months) to determine if they are still relevant.

21. *What market information should a DTF be required to provide to the general public without charge, and on what schedule? Please be as specific as possible as to data elements, granularity, and schedule (compare with the US CFTC rules in 17 CFR 16.01).*

A DTF should be required to provide information on the total notional volume, market value and percentage of block trade volume per instrument type (e.g. IRS, OIS, CDS – single name, CDS Index). The information should be published daily within one business day of the trade.

22. *In addition to reporting trade information to a trade repository, should a DTF be required to disseminate trade information directly to all its participants, or only to the counterparties to the trade? Should there be a minimum amount of post-trade information that is disseminated to all participants, containing less detail than the information provided to the counterparties? Please specify.*

A DTF should only be required to report to the counterparties to the trade. We do not believe there would be a benefit to providing post-trade information to all participants.

### **Trading Mandate**

23. *Are the proposed criteria for determining whether a derivative will be subject to a DTF-trading mandate appropriate? Should other criteria be considered?*

Yes the proposed criteria are appropriate.

24. *Are there existing OTC derivatives that should be considered suitable for mandatory trading on a DTF? Are there classes of OTC derivatives for which a mandatory trading obligation would be detrimental to market participants?*

To ensure the greatest amount of harmonization possible with the United States and other jurisdictions such as the EU, we would encourage the types of OTC derivatives suitable for mandatory trading on a DTF in the first instance be the same as those already designated in other jurisdictions (e.g. interest and credit swaps). We strongly support the “wait-and-see” approach discussed in the Notice, as there may be some products where there is insufficient liquidity in Canada to mandate clearing even though the market ecosystem in other jurisdictions is more developed. If package trades and total return swaps were subject to a mandatory trading obligation, it could be detrimental to market participants.

25. *Are there any situations in which a product that has been mandated to trade exclusively on a DTF should be permitted to trade other than on a DTF? Should any category of market participants be exempt from a trading mandate?*

Package trades should be permitted to trade other than on a DTF, since they are used by commercial enterprises to hedge specific commercial risks. They may trade infrequently, and it could be more of a burden for such products to trade on a DTF than bilaterally (or through other means). Non-financial users of derivatives in certain instances should be

eligible for non-DTF trading. Exemptive relief should be available for such trades, potentially through an expedited process.

*26. Should there be a formal role for DTFs in initiating the process to specify that a class of OTC derivatives is mandated to trade exclusively on a DTF, comparable to the role of SEFs in the MAT process described on page 813?*

Yes there should be a formal role for DTFs, but they should not be permitted to arbitrate the process for commercial reasons.

*27. What pre-trade transparency requirements are appropriate for OTC derivatives that have been mandated to be traded on a DTF? In particular, what precise pre-trade information should a DTF be required to publish for OTC derivatives that are subject to a DTF-trading mandate? Please be specific in terms of the execution method (e.g., order book, RFQ, etc.).*

An order book model price and size would be appropriate, and for an RFQ model indicative size and a price would initially be appropriate.

*28. For the purpose of exempting large orders and quotes from pre-trade transparency requirements or permitting modified disclosure, how should an appropriate size threshold be determined?*

The size threshold should be discretionary, and there should be a pre-trade process for exemption and/or standing criteria, regularly evaluated and updated by the regulator and/or the DTF in consultation with the regulator and industry, by which a trade is automatically exempted from the reporting requirements.

### **Concluding Remarks**

We thank you for the opportunity to provide these comments. We would be happy to address any questions you may have and appreciate the time you are taking to consider our points of view. Please feel free to contact us at [chair@cfaadvocacy.ca](mailto:chair@cfaadvocacy.ca) on this or any other issue in future.

(Signed) *Cecilia Wong*

**Cecilia Wong, CFA**  
**Chair, Canadian Advocacy Council**