



INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

Ian C. W. Russell, FCSI
President and CEO

May 20, 2011

Mr. Jacques Tanguay
Vice-President, Regulatory Division
Bourse de Montréal Inc. (the Bourse)
Tour de la Bourse, P.O. Box 61
800 Victoria Square I
Montreal, Quebec H4Z 1A9

Dear Mr. Tanguay:

Re: IIAC Member Comments on LOPR Circular 074-2011 and Other Matters

We are writing on behalf of members of the Investment Industry Association of Canada (IIAC) to follow up on meetings with you and Bourse staff regarding implementation of Large Open Position Reporting (LOPR), scheduled to be launched on July 25, 2011. Also, thank you for meeting with us on information technology security matters on May 3, 2011 and with us and Ogilvy Renault on privacy matters on May 5, 2011.

We believe that we are conceptually in agreement on the issues surrounding privacy of personal information and information security. These matters are proceeding on a parallel track towards an approved Rule change and a signed confidentiality agreement subject to concerted efforts on both the Bourse's and Approved Participants' side. Completion of these two steps is critical before July 25.

Our members also have analyzed the new information in Circular 074-2011 against the particulars of earlier requirements and need answers to some questions before firms developing internally, and those using service providers, can complete development (see Attachment 1). Once these questions are answered, we would like the complete business requirements (the original specifications plus amendments from Circular 074-2011 and other sources) to ensure all parties have complete correct information. As the members listed in Attachment 2 remain concerned by their ability to meet implementation deadlines on the basis of still incomplete requirements, I will call to discuss next steps.

Yours truly,

Cc : Anthony Tamvakologos; François Gilbert

Attachment 1

Large Open Position Reporting

The points below are in the order of the sections in Circular 074-2011: "Large Derivative Instruments Open Positions Reporting Tool Project (LOPR Project) – Requirements changes and clarifications". The comments are mainly from the options side, however, a number of topics, notably the beneficial owner roll-up, are major issues for both futures and options.

I. CHANGES

1.a Requirement to Provide Clients' SIN

We appreciated the meeting with the Bourse and Ogilvy Renault on Thursday, May 5, 2011. We were pleased that the Bourse's counsel agreed that: (i) even just four digits of the SIN is "information about an identifiable individual", (ii) the exemptions of Subsection 7(3) of the Personal Information Protection and Electronic Documents Act (PIPEDA) do *not* apply in and of themselves, (iii) the principle of proportionality *does* apply (in other words, that if requirements can reasonably be met in a less privacy-intrusive way, they should be), and (iv) a Bourse Rule change is required.

We understand that the Bourse will not be joining our representatives in a meeting to be scheduled with the Office of the Privacy Commissioner of Canada (it now appears this may be on June 21). We will reflect any relevant outcomes from that meeting in the IIAC's response to requests for comments from the Regulatory Division of the Bourse and the Autorité des marchés financiers (AMF) regarding elimination of Rule 6654 and amendment to Rule 14102 to allow required reporting formats to be prescribed.

Removing required information from a rule and putting it into a prescribed form leaves APs exposed to form/format/delivery changes in the future that may not be workable without the formality of mandatory discussion. In terms of the proposed Rule changes to be issued for comment, please note, as discussed, that some clients have specified that their SIN can only be used for tax reporting purposes.

Would the Bourse please include in Rule 14102 a requirement to consult effectively with the APs regarding future form/format changes and, in background material accompanying the proposed Rule change (for example, the final version of the prescribed format/accompanying instructions/circular), wording along the lines of 'if, and only if, [the SIN is] unavailable or cannot be provided' [emphasis ours].

1.b Confidentiality of information transmitted

Thank you also for the Tuesday, May 3, 2011 teleconference between the Bourse's and IIAC members' information and systems security experts. As mentioned, most if not all Approved Participants (APs) will be unable to provide Personal Information as defined in PIPEDA until the new Rule and a signed Confidentiality Agreement are in place (a number question whether there is a workable alternative for the requirement). As a minimum, it is important for our members: (i) that there be a rule or equivalent, (ii) that the process leading to the new requirements be public and transparent, (iii) that the final rule and form/format be widely obtainable through the Bourse's website, and (iv) that the Bourse sign a confidentiality agreement with each AP.

We have a draft confidentiality agreement that has been circulated for review and we are receiving input; we expect to provide a draft for your review next week.

While the deadlines are extremely tight given the target rule amendment schedule the Bourse shared (May 31 – delivery of proposal by the Bourse to the Special Committee of the Regulatory Division; mid-June – delivery to the Bourse's Rules and Policy Committee; no later than June 24 – release of the proposed Rule changes with additional information for comment by the AMF and the Bourse for 30-day comment), we believe the Confidentiality Agreement and Rule Amendment at present appear achievable by July 25 (recognizing that some APs may not subscribe to an AP-wide confidentiality agreement).

As you will recall, there were other information security matters discussed when we teleconferenced on May 3, 2011 and we have summarized them, with two new issues (1. and 6.), below:

1. We encourage the Bourse to include an identifier of the AP for whom a file is being reported *within* the actual file layout. Currently, the Bourse is relying on the user id and password used to establish the connection as the only identification of the AP, which we believe is prone to error.
2. User ids and passwords are to be used both as sign-on credentials for individual users at the members' offices and as server-to-server connections for systems connectivity, which is problematic. User credentials for accessing the GUI should be completely separate from credentials used to assure proper connectivity of systems, and separate again from identifying the AP for which the data is reported.
3. The Bourse agreed to look at the possibility of a 60-day password expiry for the user ID for the GUI channel.

4. The Bourse will consider what can be done to: (1) securely destroy member clients' personal data (e.g., 7xOverwrite for electronic file destruction) and (2) confirm data destruction after seven years (we suggest an annual standard letter).
5. The Bourse agreed to consider an upgrade from its MD5 algorithm for data security purposes. This is an important issue in our view in light of MD5's known encryption weaknesses. Additionally, we know that a switch to SFT is not being considered at this time, however, we strongly suggest that the Bourse enter into discussions with the APs or others to map out a move to this form of file transfer. This form of file transfer is both secure and more widely used, and therefore easier and more economical for development than the proprietary SAIL protocol standards.
6. We would like to confirm that all activity sessions that create or access AP data are logged and that the logs are maintained in a secure manner.
7. The Bourse was going to consider sharing its SAS 70/CICA 5970 equivalent, in confidence, with at least some APs.

Would the Bourse be able to provide an update on these matters or confirmation where required as soon as possible?

2. Position and Account Submissions Time Extension

The extension of the required reporting time to 8:00 a.m. ET on T+1 is appreciated, but is still problematic for the majority if not all of our members, large and small, clearing and introducing brokers, particularly those with the greatest options volumes and in time zones west of Ontario (see Attachment 3). For those using the GUI facility for reporting (which most of the members plan to do, at least initially), it will be necessary to bring staff in before the start of the normal working day to check the date of and submit the file. For those members reporting on behalf of multiple APs, and for those members out West, this is even more onerous.

Our strong preference remains reporting reconciled data of transactions from transaction date (T) by end of business day on T+1 if not on T+2 as had been requested.

Providing data in unreconciled form (with 'unreconciled' meaning cancels and corrects of incorrect amounts and accounts will not have been completed) would allow earlier delivery (although not by 8:00 a.m. in some cases), however, if unreconciled data is provided in any form:

- a. the Confidentiality Agreement will have to be signed and in place;

- b. the Confidentiality Agreement will have to provide that the disclosing AP assumes no responsibility for information provided or actions taken by the Bourse on the basis of unchecked-as-to-the-correct-file and unreconciled data;
 - c. a reasonable process that provides APs with certainty regarding what corrections to unreconciled data to report and how must be discussed and agreed to; and
 - d. there should be discussion of processes/exceptions for peak periods, such as the third Friday of every month when a preponderance of options expire.
- i. While we are working to complete (a), would you confirm the acceptability of (b) and advise when you will be providing clarity re (c) and (d) or let us know if you would prefer a teleconference on these latter two points to expedite matters?*

For July 25, 2011, and on a best-efforts basis, we believe that non-clearing members may be able to file by 8:00 a.m. daily information that is:

- Unreconciled
- At the current level of aggregation
- At a best-efforts level of completeness.

Clearing and west-coast members will *not* be able to meet the 8:00 a.m. timeline without bringing in personnel far outside normal business hours.

Reconciled data could be provided by both non-clearing and clearing brokers by the close of business on T+1 on a best-efforts basis, with the exception of times when there are significant option expiries.

- ii. Given the concerns with unreconciled data and issues of clearing and west-coast brokers, can the data submission deadline be changed to reconciled at close of business on T+1 (or later) or to address the issues of west-of-Eastern-Time APs and clearing brokers?*

In order to deal with the remaining issues regarding aggregation and completeness of data, we believe that it would be prudent to have a transition or “extended test” period with live data that would respect the July 25, 2011 launch date, while recognizing the challenges of the beneficial ownership roll-up and certain other requirements, as well as late changes and as-yet incomplete requirements. During this period, we would like to work together with the Bourse and service providers to map the Bourse-desired new fields to fields commonly already available within major industry vendors’/service providers’ systems, ideally identifying more straightforward and therefore possibly quicker ways to meet the Bourse’s remaining requirements. It would be an opportunity for further discussions regarding aggregation requirements – both systems-wise and in terms of data-gathering – that are much more extensive than were apparent until earlier this year. This phased bring-on strategy is frequently used by infrastructure providers to reduce implementation risk and better manage the roll-out of new requirements,

particularly where there are no indications that there is a problem of unfair practices.

We believe that such an approach would alleviate some of the challenges that the APs face and should be pursued in light of:

- a. Our reading of Section 21 of the Quebec Derivatives Act, namely that, “In establishing its rules, the entity must consider the costs to its members and to market participants that may result from their application.” – our members and the service providers of those using such entities are looking at what practical steps will most cost-efficiently achieve Bourse requirements, however, require the answers to most of the questions in this letter to complete their efforts;
- b. Manual AP work required to complete fields that currently do not exist and to develop or have service providers develop systems logic to match beneficial owners, link registered companies, replace a business or incorporation number or other identifier with the last four SIN digits for sole proprietorships and build other relationships – note that while on average 28 positions a day per AP may be being reported, tens of thousands of accounts will have to be identified and searched for available additional information that may exist in different parts of the AP if at all, for thousands of reportable positions;
- c. The sensitivity of the Personal Information; and
- d. The partly manual approach the Bourse will itself use for reconciliation in the first phase.

iii. As we believe that this represents a reasonable approach, would the Bourse confirm that staged implementation, with filing and aggregation discussions following a formal mapping of Bourse and service provider fields, is acceptable? The Bourse can monitor the time files are provided and question those APs that are reporting outliers.

II. CLARIFICATIONS

1. Account Ownership

Account ownership is limited to, according to Circular 074-2011, 24 characters in one place and 25 in another. We have learned from consultation with APs that the name fields for the majority of accounts in our members’ systems can accommodate up to two 32-character lines (i.e., 64-characters) to capture accounts in trust for multiple people, people with particularly long names, etc. “Renaming” accounts, when account names are used for many important purposes, is not workable.

Will the Bourse increase the maximum name character limit to 64 digits? In the alternative, names will be truncated and the Bourse can follow up with the AP where the Bourse determines there is a need to “look through.”

2. Account Ownership ID

The Circular states that the reporting applies to beneficial owners, whether persons or entities, with more than a 50% ownership share. Our members rarely if ever maintain ownership percentages for joint accounts for retail clients, while for investment clubs, the data is not on member systems. Under Investment Industry Regulatory Organization of Canada (IIROC) Rule 1300.1 (Bulletin 3294), IIROC members are only required to collect ownership information when an owner holds more than 10%, however, name and address only must be and are collected directly or through layers of entity ownership – not social insurance numbers (SINs), not other taxpayer numbers, and not incorporation numbers.

To manage the reporting process, unless otherwise advised by the Bourse, we believe that a review of all retail joint accounts can be excluded, *unless ownership is otherwise known*, on the basis that spouses typically split assets 50/50 and would not exceed a 50% share (note that if an AP's systems do not have a joint account flag, the AP will aggregate using the primary joint account identifier with accounts with the same identifier). Also, joint accounts with family members, friends for shared rental purposes, and investment clubs, etc. with more than two owners would typically have equal shares and, unless ownership is otherwise known, would have shares of 50% or less and thus would not be LOPR-reportable.

i. Should an investment club, joint account or equivalent appear to be materially and frequently exceeding the minimum reportable thresholds, could the Bourse request an AP to obtain and report additional information?

The requirements and guidelines regarding the number or identifier field have mostly been around the retail customer (i.e., SIN, SSN). For corporations, Circular 074-2011 mentioned using an incorporation number. With respect to institutional clients, a business number (BN) or, outside of Canada, corporate tax number may be more commonly used or accessible than incorporation number and should likely replace the requirement for incorporation number, while still leaving the other options. We would like to suggest that, as an additional – non-mandatory – alternative, one other identifier be added, that is, an 'in concert number'. Foreign APs operating in the U.S. and Canada with U.S. or global institutional clients are required by U.S. regulators – for similar reporting purposes – to use a common 'in concert number' for all accounts that should be aggregated for option position limit purposes (this aggregation is required by control or order placer and not beneficial owner) and this should help aggregation of out-of-Canada client data across APs.

- ii. Would the Bourse confirm that institutional clients may use a business number, equivalent tax number or in concert number rather than incorporation number (with an internal identifier remaining an option)?*

3. Account Aggregation

We understand that APs can, when reporting positions of accounts with more than one beneficial owner, report that account either at 100% of the positions or at the percentage ownership rate times the number of open contracts. Also, the Circular provides an example for aggregation purposes, but does not show one with a registered or corporate entity, ones where there is a roll-up of an individual with an account of which they own more than 50%, etc., which would be helpful.

4.a LOPR Exemption

No comment.

4.b LOPR Delegation to Clearing Broker/Other

We strongly encourage a LOPR systems change to allow clearing brokers to file for their introducing brokers and relevant clients for security as well as efficiency reasons under one secured access and in one file. We believe that it is more secure for clearing brokers to file reportable positions through a single file, rather than having multiple user ids and passwords, where passwords are more likely to be written down, posing a security risk.

- i. When will a single sign-on and single-file send option be built for clearing brokers?*
- ii. When will members be receiving the procedures with respect to obtaining, changing and getting forgotten passwords and user IDs? These procedures need to be included, or at least referenced, in the Confidentiality Agreement.*

Also, our members need a more formal process for appointing and confirming the clearing and introducing broker links to the Bourse. We can prepare a short tripartite agreement for your review if one is not already available or contemplated.

- iii. Would you confirm that an appropriately senior Bourse officer will sign such a tri-partite agreement?*

We note also that a number of clearing brokers that deal with omnibus accounts are trying to determine how omnibus accounts will be excluded and what can be done to address challenges in the area.

iv. We hope to provide suggestions regarding omnibus accounts in the near future.

5.0 Hedger versus Speculator

We had asked that an additional option – not available (N/A) – be added to the hedger/speculator alternatives in this field. The Circular says that when an AP cannot differentiate between hedger and speculator at the price of a reasonable effort, speculator should be used.

Our members believe that defaulting to speculator is or would be a concern for not just the APs, but also for clients, other regulators, regulatory examiners and potentially litigators. As the LOPR reports are official, they could cause confusion in the risk management and supervision of accounts, could lead to litigation if an investor that cannot speculate under its investment policy statement is identified as a speculator, and may create confusion when dealing with less experienced examiners or auditors. In terms of examination, for example, retail clients can trade equity options in different accounts, and use multiple trading strategies across these accounts. The sale of calls in an account could be considered a hedging transaction, yet the buying of calls in that same account may be considered a speculative transaction. Most important, defaulting to speculator will divert attention and resources from actual speculator accounts.

- i. Could you confirm that a change will be made to add an N/A category unless an AP has a clear indication otherwise from the client?*
- ii. If not, could you confirm in writing that the Bourse is aware that what is entered in most fields has not been able to be confirmed with clients, could be erroneous and will be used by the Bourse at its own risk?*

6.0 Snapshot of Positions

No comment.

7.0 LOPR May 2, 2011 Deployment

Could the Bourse provide any feedback from testing to date that may assist APs in their development and testing efforts?

8.0 Readiness of Service Providers

We and our members are working with major Canadian service providers and believe that all APs of which we are aware and their service providers are fully engaged in looking for workable solutions. To this end, our members and the

service providers need final answers to questions in this letter and, in particular, confirmed specifications/requirements.

Could you advise when we will be able to obtain consolidated specifications/requirements, including the original specifications plus amendments from Circular 074-2011 and answers provided to some, but not all APs by e-mail and phone that may affect development and procedural changes.

9.0 Virtual Private Network (VPN) Connection Availability

We very much appreciate the Bourse's taking steps to make VPN access available and that it should be ready at the Bourse's end next week.

Following on our May 3 meeting, could you please provide details as soon as possible regarding how the VPN will be managed (if there is to be equipment at the Bourse, how credentials will be provided, tested and regularly refreshed etc.)?

III. Other

- **Country codes:** We are disappointed that the Bourse will not make the requested change to three digits because a cross-reference table can be built by each AP. It seemed to us practical to have one entity change a field than multiple firms having to make the same development and test, however, this additional step is being added to member development requirements.
- **Account owner types:** Given that this information will not be available in a quality format, the Miscellaneous option will be used in most cases.
- **Acceptability of "best-efforts" basis:** Given that APs need clear answers to the questions referenced in 8.0 above to complete business requirements, experience suggests there will be challenges at inception and, while members of our LOPR Committee are actively working to find solutions, we understood from our April 18 meeting that the Bourse will consider what is reasonable under the circumstances.

Would you confirm that the Bourse will instruct its examiners to apply a reasonableness standard?

Steps in the event of excessive holdings: There is a question regarding what steps the Bourse may initiate if a roll-up across APs suggests excessive or otherwise unacceptable activity, e.g., whether the Bourse would unwind or otherwise negate existing positions and, if so, how. While this likely would not be the first regulatory response, it is important to understand all possible eventualities from a client disclosure and AP perspective.

Could you advise what steps the Bourse would take in the case of evidence of a client's inappropriate/unacceptable activity across APs, including whether the Bourse would ever require an unwind or offset of positions and how that would work?

IV. Project Management

- ***Timelines/deliverables:*** We think there may be value, even at this stage, in developing an AP Bring-On project plan, with timelines, deliverables (such as updated specifications/requirements), communications plan (at present, answers to some common questions are only being sent to the person asking the question, but would in some cases be of interest to all APs and prevent inadvertent misunderstandings and wasted development), testing specifications, regular meetings to ensure that the next stages move forward, etc.

Could you confirm that the Bourse will put in place a process for future communications of refinements in the reporting requirements and status that will be more structured for LOPR from now until July 25th and beyond?

- ***Post mortem:*** Following implementation, we would like to discuss with the Regulatory Division of the Bourse and Bourse more generally a way to involve APs in planning of new requirements to achieve straightforward, cost-effective and minimally disruptive implementation of changes in the best interests of the derivatives markets in Canada, and in terms of cost-efficiency for the Bourse and its APs.

Attachment 2

IIAC Members Requesting to Be Identified to Date as Having Concerns that Need to Be Addressed

Note that a number of the following APs act for other APs and that some APs not listed here are inactive.

BMO Nesbitt Burns Inc.

CIBC World Markets Inc.

Desjardins Securities Inc.

Friedberg Mercantile Group Ltd

Fraser Mackenzie Limited*

GMP Securities L.P.

MacDougall, MacDougall & McTier Inc.

National Bank Financial Inc.

NBCN

Raymond James Ltd.

RBC Dominion Securities Inc

Scotia Capital Inc.

TD Securities Inc.

TD Waterhouse Canada Inc.

** Not a member, however, concerned with privacy of clients*

Attachment 3

Elaboration on Large and Small AP Challenges

What may not be appreciated is the amount of work already done manually to obtain the data for LOPR reporting, that will be multiplied 10 times until the new specifications are final, any possible programming can be done, and data can be obtained that is not used for any purpose in the ordinary course of business.

Using as an example a AP with average reportable positions of 28, as mentioned by the Bourse on April 18, clients with such positions often have multiple accounts with reportable positions in multiple different options. To get to the reportable positions:

- queries must be generated against a service providers' system to obtain a listing of all open options positions, which, depending on server traffic and the number of positions involved, can take up to 10 minutes (considerably longer for larger volumes);
- query output is exported to an Excel spreadsheet with thousands of rows, which is then sorted by underlying security and client name;
- subtotals must be created to identify positions exceeding defined contract thresholds; and
- on a best-efforts basis, accounts are linked to the same beneficial owner, but this is not tracked to the level of beneficial owners of corporate entities, nor is it possible for a number of entities to link non-corporate accounts.

In summary, the aggregating process is manual, time-consuming, and subject to human error, taking about an hour by this firm in the current environment. Proportionally more resources would be required for a daily report, with considerably more fields, some of which need to be "replaced" with a SIN. While some automation is possible, it is uncertain how easy this will be. In the interim, to go from one hour a week to, say, 10 hours a week due to five days of required reporting and more data required to be added and matched daily, does not seem reasonable where we have been presented with no evidence of wrongdoing to date.

Although large-volume firms will eventually have the technology to meet most of the requirements, additional manual work for the foreseeable future will be onerous due to the sheer volumes involved. Although the Bourse reports average reportable positions as 28, large-volume firms are dealing with thousands of positions and tens of thousands of accounts approved to trade options. While the perception may be that large-volume firms already have the technology that would automate the work, the files currently received from service providers are stripped into reportable and not-reportable accounts, with additional fields added from other sources, which now would have to be done daily and much earlier. The manual effort includes additional aggregation, individual introducing broker reporting by clearing brokers and, for some, could include reporting the breakdown of positions in omnibus accounts.