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

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President & Chief Executive Officer

December 19, 2007

Ms. Adrianne Marskell
Senior Compliance Counsel, Corporate Finance
British Columbia Securities Commission
PO Box 10142, Pacific Centre
701 West Georgia Street
Vancouver, BC, V7Y 1L2

Dear Ms. Marskell:

Re: Proposed BC Instrument 51-509 Issuers Quoted in the US Over-the Counter Markets and Proposed Conditions of Registration for Investment Dealers that Trade in the US Over-the-Counter Markets

The Investment Industry Association of Canada (IIAC) appreciates the opportunity to comment on the above noted Proposed Instrument and Conditions of Registration. IIAC supports the efforts of the BCSC to improve issuer disclosure on over-the-counter (OTC) issuers and discourage the manufacture and sale in British Columbia of US OTC quoted shell companies that can be used for abusive purposes.

We agree that the manufacture and sale of shells of OTC issuers appears to be a problem, particularly in respect of their profile in British Columbia. While the damaging effect of this business is difficult to quantify, the reputational issues relating to the integrity of the British Columbia capital markets are of concern to legitimate issuers and other market participants.

The IIAC and its members were pleased to provide the BCSC with feedback on the proposal prior to its publication. However, while the Instrument and the proposed Conditions of Registration reflect much of the input provided by our members, we have a few remaining concerns with both the Instrument and the Conditions of Registration.

On a general level, although it appears that the problem, or perception of the problem is largely in British Columbia, we are concerned about the implementation of regulation on a regional rather than national basis. This non-level playing field and differentiation of regulation creates complexities and works against the continuing move to harmonization of provincial regulation.

Our specific comments on the Instrument and the Conditions of Registration are as follows.

BC Instrument 51-509 Issuers Quoted in the US Over-the-Counter Markets

In general, we believe the provisions in the Instrument applicable to the OTC Issuers are appropriate. The few questions and issues that remain are outlined below.

An important matter that requires clarification is the commission's expectation of investment dealers with respect to what due diligence will be required to ensure that the issuers and the securities that they are trading are in full compliance with the Instrument. It should be noted that a good deal of the information required to make such an assessment may not be readily available. As such, it may not be clear if the Instrument applies to the issuer, and if so, whether the issuer is in compliance. We are concerned that dealers may be held responsible in respect of matters for which they do not have proper access to information and that are not covered under the proposed Conditions of Registration.

Definitions / Application

In general, the application of the Instrument and the exemptions are appropriate, however, we note that American Depository Receipts (ADRs) which represent significant and reputable international issuers and are increasingly being traded OTC, may be caught under the current definitions of OTC quoted securities. Since these are not the types of securities that are of concern, we suggest that they be exempted from the definition of OTC quoted securities.

In order to assist market participants, including investors and intermediaries dealing with OTC issuers, it would be helpful if the BCSC could publicly identify the issuers to which the Instrument applies on its website. This information would be available to the BCSC via the continuous disclosure requirements applicable under the Instrument.

In respect of the specific provisions under this heading, we have the following comments:

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Section 1.4 (1)

(a) The term "administered in or from British Columbia" is not clear. Guidance or examples should be provided to assist issuers and intermediaries in determining whether the Instrument is applicable. The activities that would be captured under this section should be clarified.

Section 1.4(2)

(a) In respect of the exemption based on being a public issuer for more than one year, it should be recognized that there are corporate events such as reverse take-overs and other reorganizations that would constitute the effective creation of a new company. These types of events may change the risk profile of the issuer so that it may not be appropriate to provide such an exemption in those situations. In addition, the Instrument should apply to pink sheet issuers, regardless of how long they have been listed, as they remain high risk despite their tenure in the public markets.

Proposed Conditions of Registration

We agree that British Columbia investment dealers have a role in protecting the reputation of the capital markets in the province. All dealers should take a serious interest in reducing the risk of inappropriate trading activity occurring within their firm.

We support certain of the targeted measures in the Conditions of Registration, such as the provisions focusing on physical deliveries of OTC securities. It has been the experience of many of our members that persons who deliver physical OTC securities are often closely connected with the issuer and sometimes present a higher risk in terms of the potential for inappropriate activity.

In respect of the other provisions in the Conditions of Registration, we have the following comments.

Application

As noted above, although we acknowledge the perception that this is a problem generally affecting British Columbia markets, we are concerned about the implementation of regulation on a regional rather than national basis. The existence of a non-level playing field may shift, rather than address the problem, and introduce further compexities into the multi-jurisdictional system.

We are also concerned about the breadth of the application of the Conditions of Registration. The Conditions will effectively apply to all dealers, even if they do not engage in the type of business that is of concern to the Commission. In many cases,

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dealers that do not undertake OTC business as a matter of policy may process an occasional trade for a client that may have one or a two OTC stocks in their portfolio. These trades are not in furtherance of the shell manufacturing or abusive trading practices targeted by the Commission. It is not appropriate to place all of the conditions of registration on these dealers where their connection with OTC business is infrequent and only occasionally incidental to their core business. Recognizing that it will be necessary to track OTC business regardless of the applicability of the Conditions of Registration, a diminimus test based on dollar amounts or trades would be useful and appropriate to determine whether the Conditions of Registration should apply.

Risk Management

The provision requiring dealers to specifically manage the risks of trading OTC issuers should enumerate these risks, particularly if they differ from those covered under IDA rules and regulations relating to supervision and monitoring. In order to design appropriate systems and processes to manage such risks, dealers must be clear what the Commission perceives such risks to be.

Monitoring, recordkeeping and reporting

While we agree that the requirement to track OTC trades is appropriate, these provisions will, in many cases, require system developments from dealers and third party providers. As such, the requirement should be phased in to allow providers the time to establish systems to track and record such transactions. We also assume the responsibility for monitoring OTC trading volume is the responsibility of the carrying broker in relationships between Introducers and carrying brokers. This should be made clear in Conditions of Registration.

Our specific comments on the provisions of section 2 are as follows.

Section 2

(a) We understand that only "BC" OTC commissions generated by the investment dealer are intended to be captured. If commissions generated by offices or salespersons outside of BC are not intended to be captured by this requirement, it would be helpful if the wording would clearly state that.

(c) It is unclear whether the word "deposits" is intended to cover electronic (book-based) delivery, or physical delivery, or both. Since section 5 refers to physical delivery, we assume that section 2(c) means both electronic and physical delivery. The provision should state clearly what it is intended to cover. Given that the inappropriate activity targeted by the proposed Instrument and Conditions of Registration is generally undertaken by those closely connected to the issuer, and are in relation to transactions involving the delivery of physical certificates, we suggest that the term "deposits" be narrowed accordingly.

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Also, 2(c) contains the term "founder", without providing a definition. It is unclear whether this term mirrors the one in NI 45-106, or if a different standard applies. The Conditions of Registration should be clear on this point. It should be noted that the information required to determine if an individual is a founder may not be easily obtained in filings made to the SEC, so it may be difficult for the dealer to ascertain this status. It would be helpful if the standard of inquiry expected of dealers was clearly defined.

This section also uses the phrase "a person that is "involved" with investor relations activities". It would be helpful if the parameters of "involved" could be more clearly defined.

(e) Given the limitations noted above, reporting may be approximate initially and may not be an accurate reflection of percentage of earnings for the dealer or its salespeople. Also note that the manual processes in tracking and recording OTC trades may also introduce some element of inaccuracy.

Establishing beneficial ownership

General Concerns with Establishing Beneficial Ownership

A number of our members have expressed concern about this section. In particular, the concern relates to the dealers' relationships with large institutional clients that transact on behalf of other parties. In these relationships dealers may not be able to obtain details about the identity of the beneficial owner due to confidentiality and privacy laws of the jurisdiction in which the intermediary operates. It should be noted that Canadian privacy laws would preclude dealers from divulging the name or identify of the Canadian clients that purchase securities from issuers that are located in jurisdictions outside of North America. The net effect may be to discourage international investment due to the more stringent and inconsistent disclosure requirements. It should be noted that this requirement is also inconsistent with the general direction taken by clearing/settlement and exchanges in establishing the ability for intermediaries and foreign dealers Direct Market Access to a marketplace through a Participating Organization, in that the dealer is never aware of the identity of the client for whom the intermediary acts.

Certain members are concerned that the provision will effectively block market participants out of the British Columbian, and, by extension, the Canadian markets, which could have a negative impact on Canadian investment.

Rather than requiring the disclosure of the names of the beneficial owners, the Commission may wish to consider the following alternatives which may address the concerns underlying the proposed regulation, while mitigating the possible negative effects on the dealers and the markets.

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For instance, dealers can prevent or deter inappropriate trading behaviors by building in policies and procedures that would require their salespersons to question intermediaries about the nature of and source of the orders, without violating privacy laws in the various jurisdictions. Assuming the Conditions of Registration will only apply to the delivery of physical certificates, a list of mandatory questions could be developed to ascertain whether the beneficial owner is an insider, promoter, control person, investor relations person, or whether they have a contract with the issuer. This would help ascertain the risk without violating privacy concerns. In addition, questions about the residence of the beneficial owner, how they acquired the securities and any other affiliation with the issuer could form part of a mandatory questionnaire.

In addition to the above, dealers could also build appropriate escalation policies to deal with suspicious trading. A reporting mechanism could be established to provide the information to the Commission for follow-up either with the SEC or FINRA in the US.

There should be appropriate exemptions from this requirement in relation to accounts to which Canadian regulators already have access to beneficial ownership information (eg: accounts for Canadian dealers and institutions or accounts for institutions in countries that already have MOUs)

If the Commission does not believe that the alternative steps above will achieve its objectives, and requires dealers to ascertain the beneficial ownership, it should provide clarification of the phrase "you must form a reasonable belief" in respect of the identity of the beneficial owner. We query whether representations from the account holder would be sufficient to satisfy this requirement and, if not, what alternative steps would be considered sufficient. The provision should provide clarity as to what steps would be sufficient to establish having acted reasonably.

Specific Concerns

Section 3

In respect of the other elements of section 3, we are concerned with the provision that states "you must not accept an order to trade OTC issuer securities deposited in an account". The word "trade" connotes both purchasing and selling securities and "deposits" only relate to sales of securities. As such, the word "trade" should be changed to the word "sell".

Section 3 is also unclear in relation to its application to the different ways that securities can be deposited into a firm account. It should be noted that securities can be deposited in several ways, other than physical form. Securities that are directed to a specified dealer and account via DTC cannot be identified prior to receipt. The only way that a firm could identify source of shares prior to the delivery of the shares is to refuse the incoming delivery, also known in the industry as a "DK". The Commission should

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consider the increased liability that may result for a dealer if this were to occur. Liabilities can be as significant as market exposure resulting from a delayed delivery and/or market exposure from a delayed sale into the market that occurred when the dealer queried the deposit or refused delivery via DTC.

Although most dealers that operate in the US OTC markets query incoming physical certificates to determine how the shares were obtained, fewer dealers query electronic deposits of securities via the DTC system. Dealers could take a cautionary approach and review electronic deposits in the same manner as physical securities, however, for practical reasons this would need to occur after receipt and deposit.

Section 4

This section uses the phrase "you must determine". It is unclear why section 3 permits a dealer to form a "reasonable belief" but section 4 requires a mandatory "determination". The inquiries in both sections are similar and they would typically be made at the same time. As such, the same standard of inquiry should apply. It is our view that the proper standard of inquiry ought to be one of reasonableness, provided that the steps that are sufficient to establish having acted reasonably are clarified. Guidance as to what is suspicious or what might be an inappropriate transaction should be provided, along with instructions on how to report such transactions.

Responsibility of UDP

We have some concerns as to the practicalities in this part of the Conditions of Registration.

Section 5

In respect of specific approval of the deposit of share certificates it should be recognized that in certain cases, the UDP is not an individual that is available for such deposit approval on a day to day basis. This individual may not be the most effective person to grant such approval and guidelines for such approval or denial. Some members are concerned that this requirement may delay sending legitimate trades to market and may result in the client not receiving the best fill.

In addition, the approval process could take a significant amount of time to complete in some cases, during which the share certificate would need to be deposited in order to comply with IDA Policy 3 and FIB requirements. Rather than prohibit the deposit of the securities it would perhaps be more meaningful to require dealers to have an approval process prior to trading in any security that was deposited in a physical form, or explicitly allow for deposit processes using dummy CUSIPs that can be removed only after the approval process has taken place. These processes are consistent with a number of current dealer practices.

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Section 6

Given differing structures of most dealers, we agree that it would be appropriate for a designate to be able to provide approval for deposits. However, in our opinion it would be the dealer that would be most capable of determining the person(s) that would be most appropriate to approve the deposits and we believe that rather than require this to be either the UDP or a director or senior officer in BC, which may not be the best choice in all cases, that the dealer should identify the position / person(s) most appropriate to perform this function.

Section 7

This section requires the UDP to "confirm that those policies and procedures will ensure compliance". We are concerned that this type of language creates an unrealistically high standard, particularly where many processes requiring human intervention are involved. We are of the view that it is not possible for any system to "ensure" compliance with the proposed Conditions of Registration. As such, we recommend that the provision be changed to read that the "policies and procedures are reasonably designed to achieve compliance with these conditions".

Further to that point, we question why it would be necessary to require the UDP to sign-off on procedures adopted to comply with the Conditions of Registration when all investment dealers must have a Corporate Governance structure that requires an approval and review process under IDA By-law 38. The UDP would be part of a committee that would review policies and provide approval. We therefore request that this requirement specifically placing this burden on the UDP be amended to have the policies and procedures signed off in accordance with the existing governance structure of the firm.

Thank you for providing us with the opportunity to comment on this proposal. If you have any questions or comments on our submission, please do not hesitate to call.

Yours sincerely,

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