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Re: Large Open Position Reporting (“LOPR”) Required Certification - as per Circular 124-17 issued on September 1, 2017 – and other LOPR Related Issues.

The Investment Industry Association of Canada (the "IIAC") and its members would like to take this opportunity to express their views on the LOPR certification required by Bourse de Montreal Inc. (“the Bourse”) in its Circular 124-17 issued on September 1, 2017, as well as on other LOPR related items.

The LOPR special examination introduced by the Bourse's Regulatory Division has resulted in concerns and questions from many industry members. We wish to inform you in order to find acceptable solutions for all parties.

The IIAC is the national association representing the position of 131 IIROC-regulated Dealer Member firms on securities regulation, public policy and industry issues. We work to foster a vibrant, prosperous investment industry driven by strong and efficient capital markets.

Mission of the Regulatory Division

The IIAC strongly supports the Mission of the Regulatory Division and its importance for market quality as well as market participants.

Circular 023-17 issued by the Bourse on February 17, 2017, in regards to the Bourse's Regulatory Division mission states that the Division:

*"is responsible for market regulation for the Bourse de Montréal Inc. The Division's mission is to promote the integrity of exchange-traded derivatives markets at the Bourse or in Canada through the development and **consistent application of clear, fair rules and policies that are effectively adapted to market needs**". [Emphasis added]*

The IIAC recognizes that clear and fair rules that can be applied by market participants and adapted to market needs enhance the quality of markets and support the industry.

Unfortunately, with the issuance of Circular 124-17, many of our members have had to spend significant time and effort to understand and try to adapt to the new LOPR certification requirement. Many industry members feel that the impact on firms was not well assessed by the Regulatory Division prior to issuing the Circular. We bring this concern to your attention to ensure that the Regulatory Division of the Bourse and industry participants continue to have a cooperative and productive relationship.

Certification Requirement

Circular 124-17 issued on September 1, 2017, states:

"To this end, the Division will perform a special inspection on LOPR during which participants will be required to: (i) verify, validate and confirm to the Division the accuracy and completeness of their LOPR reports, and (ii) confirm to the Division that reasonably designed surveillance and compliance mechanisms have been implemented in order to ensure the regulatory compliance of their LOPR reports submitted to the Division."

Article 4003 of the Rules of the Bourse

Circular 124-17 also states that the LOPR special examination by the Regulatory Division is ordered by the Division's Vice President under Article 4003 of the Rules of the Bourse.

Article 4003 certainly stipulates that the Regulatory Division can ask for all and any information regarding a participant's activity in TMX derivatives. However, some members believe that demanding certification seems to go beyond what Article 4003 contemplates. Furthermore, there is no contemplation of anything other than immaculate perfection in compliance with Articles 14102 and 3011.

Industry Concerns and Questions

Industry members understand the need for complete and accurate regulatory reporting.

However, some active industry members are finding it difficult to meet the new LOPR certification requirement. The Regulatory Division may have overlooked certain important operational facts and negative impacts. Industry concerns and questions are summarized below.

The IIAC hopes that the Regulatory Division can find solutions to these industry issues. We would like to take the opportunity to reiterate that the IIAC and its members are available for further discussion and wish for increased collaboration and dialogue.

Among the issues expressed by members:

- An introducing broker/carrying broker agreement (IIROC Rule 35) may prevent or limit introducing brokers to certify the accuracy and proper management of the order books and records. These order books and records are held, managed and controlled by the carrying broker as per the IIROC rules and regulations. This may also apply where settlements are cleared by different clearing brokers.
- Members using Independent Software Vendors ("ISV") may only have access to the vendor's CSV files. The member must trust that the information contained in the vendor's file is complete and accurate and does not have a different database to reconcile the vendor's data. It was mentioned by the Regulatory Division that the CSV file could be compared to SOLA or CDCC reports. These reports do not allow our members to perform the reconciliation requested by the Regulatory Division and to properly assess accuracy and completeness. CDCC reports do not provide a granular view of the positions held by each client. CDCC MP01 (Options open positions) and MP51 (Futures open positions) reports aggregate all positions held at the clearing member. These reports are insufficient to ensure the accuracy of the LOPR reports since only positions exceeding LOPR thresholds are reportable to the Regulatory Division.

- If there was a reliable alternative methodology and data available to reconcile the ISV LOPR output, the development of an automated system (necessary for speed of processing and accuracy) would likely take months of development. Firms typically plan initiatives of this scale during the annual budgeting process. Business Planning Initiatives (BPI's) are submitted for budget approval and must compete for limited time and resources available. BPI's are typically managed by the Project Management Office, which again involves the allocation of limited resources.
- The testing which must be performed should be further detailed. For example, members would need to know what the Regulatory Division considers as a proper testing period, sample size, and what results are required for certification (once the sample has been extrapolated). What error percentage would the Regulatory Division consider acceptable for certifying that a firm has implemented a system "*that is reasonably designed to achieve compliance*"?
- Legal Counsel has indicated, at least to certain of our members, that they will not permit signature of the LOPR certification in its current form since the wording of the TMX Certification Form is absolute. If legal departments confirmed that a certification could be submitted, the certification would need to be approved by executive management and the wording of the certification would need to be revised to reflect the reality of each firm's business practice. There are also questions regarding the legal weight of such certification.
- The Regulatory Division should be aware that the LOPR special examination implemented recently is adding a lot of pressure on the compliance departments of approved participants who submit LOPR reports on behalf of other entities. The Regulatory Division has originally implemented the LOPR tool without taking into account the needs of the firms who delegate their LOPR submissions. The Regulatory Division was aware that not all firms were receiving copies of their LOPR reports submitted by their delegates. Now, the compliance departments of the LOPR delegates must answer numerous questions from the different firms who delegated the LOPR report submissions, and must review and validate in a manual fashion multiple LOPR submissions communicated to the Regulatory Division.
- The timing of the Regulatory Division in implementing the LOPR special examination has also created further unwarranted pressure on our members. The LOPR special examination requires approved participants to certify as of August 31, 2017, that their LOPR reports comply with the Bourse's requirements and that their supervisory system is reasonably designed to achieve compliance. However, Circular 124-17 mentions that starting August 31, 2017, participants will be able to monitor the submitted account and position information through the LOPR Portal enhancement. We believe this LOPR Portal enhancement should have been implemented before the LOPR special examination to provide a chance to participants who delegate their LOPR report submission to review their reports and put in place their supervisory controls. We feel the Regulatory Division did not properly assess the impact of its timing for our members when implementing the LOPR special examination.

LOPR - Guidelines for Supervision and Compliance Obligations

Similar concerns and questions arose with the issuance of the draft version of the Guidelines which was sent out to the Regulatory User Group members by the Regulatory Division. We note that the final Guidelines were issued without an official request for comments, which we find disappointing.

Verbal comments were made at the Regulatory User Group meeting and were somewhat dismissed by the Regulatory Division. The Guidelines, as issued, triggered many questions as they lack clarity for implementation.

During the Regulatory User Group meeting, the Regulatory Division explained that it is moving to a principle-based approach, which is acceptable for our members. However, we feel that the Guidelines must be supplemented by examples and guidance. Furthermore, the current guidelines are somewhat vague, including in regards to the LOPR system.

In the Guidelines, the Regulatory Division often refers to “reasonable” or “appropriate” supervision and compliance without giving the criteria that will be used to assess such reasonableness or appropriateness. When requesting the criteria that the Bourse will use to assess “reasonableness” and “appropriateness”, the IIAC and its members do not feel they received sufficient clarity to enable firms to operationalize processes and/or policies. We were told that criteria could not be given out as “it depended on each firm” and that the systems would not be expected “to catch everything”.

During the Regulatory User Group meeting, a member asked if minimum requirements, similar to what IIROC provides, would be added and if areas to cover would be introduced in the final version. The Regulatory Division answered that no minimum requirements or areas of coverage would be added – this to give “flexibility to the members”. We understand that flexibility is needed but unfortunately the Guidelines lack clarity which, once again, increases our members’ concerns.

We believe the Guidelines should be amended by the Regulatory Division in order to provide better clarity to our members. Clearer guidelines would also help in assessing the LOPR system. We look forward to discussing this topic with the Regulatory Division during the CADC Compliance Forum Workshops. We are hoping to find solutions to these industry issues.

Large Open Position Reporting (“LOPR”) – Waiving late filing fees

Another concern regarding LOPR is related to the late filing fees. The Regulatory Division recently mentioned that, when a firm cannot submit a LOPR filing by the deadline, if contacted prior to the deadline, the late filing fees “may” be waived. When IIAC asked in which cases could the fee be waived vs not, the members were told that “it depends”, it will be analyzed on a “case-by-case basis”.

When asking for examples to better understand the process, members were told that fees may be waived for a “power outage” but would not for “being late for work”. We understand that the Regulatory Division cannot possibly list all potential reasons in one category or the other. Furthermore, industry members are not against the waiving of fees. However, the lack of clarity does create concern. We urge the Regulatory Division to apply consistent decisions for all members.

LOPR for Single Stock Futures

Our industry has been struggling with the aggregation of options and futures on the same underlying product for months. We have had many discussions with the Regulatory Division on this topic. Despite postponing the implementation for aggregation to June 2018, we feel that the impact on our members is still not well understood by the Regulatory Division.

The Regulatory Division’s request to aggregate positions is extremely costly for some of our members. We believe firms should be allowed to send separate reports for options and futures. We believe the Regulatory Division could easily aggregate the positions and would save our industry great time and money.

Solutions needed

We hope the Regulatory Division can provide clear guidance to our members and answer all concerns and questions.

Furthermore, we are hoping that the Regulatory Division better assess the impact of new requirements on our members. Each new rule or requirement should be supplemented with:

- Reason(s) why a rule/requirement is now deemed necessary;
- Risks the Regulatory Division is trying to mitigate;
- Operational and financial Impact on members.

Industry Request – Postponing the LOPR Certification Deadline

In order for the Regulatory Division and our industry members to discuss the issues listed above and find solutions that are acceptable for all parties, we request that the LOPR certification (or gatekeeper) deadline be postponed until further notice.

We also urge the Regulatory Division to show each type of firm how to perform the testing required (which sources must be reconciled) and provide further information such as the testing period, sample size, error percentage deemed acceptable (following extrapolation).

As previously mentioned, the Bourse asked that some firms compare the ISV reports to CDCC and SOLA reports. No accurate reconciliation can be done with the help of CDCC and SOLA reports since the reports do not contain all necessary information. A reconciliation could be done between ISV, SOLA and CDCC reports but no valid conclusion could be reached.

We hope the Regulatory Division can provide guidance to our members.

Conclusion

As previously mentioned, our industry members have increasing concerns based on:

- The considerable effort required by members to understand this new regulatory requirement and to try to comply;
- The vagueness of the testing required to achieve LOPR certification;
- The vagueness of the type of issues that should be mentioned through a gatekeeper report filing;
- The lack of clear guidance from the Regulatory Division;
- The vagueness of the Guidelines for Supervision and Compliance Obligations, including as they relate to LOPR;
- The lack of examples and guidance for the Guidelines for Supervision and Compliance Obligations – needed to understand principle-based rules;
- The possible discretion used for waiving LOPR late filing fees;
- The timing of the LOPR special examination, of the LOPR Portal enhancement and of the required LOPR certification.

We hope to receive clear answers to our questions and hope the Regulatory Division can address our concerns.

We also reiterate our request for postponement of the LOPR certification (or gatekeeper) deadline until the LOPR certification issues have been discussed and solutions have been found.

Lastly, we would like to mention the increased collaboration of the Regulatory Division with our members, through recent participation in IIAC forums. We commend the Regulatory Division on these efforts and hope the collaboration will continue and lead to a stronger, more efficient and effective derivatives market which is beneficial to all market participants.

Please note that the IIAC and its Members, as always, remain available for further consultations.

Yours sincerely,



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