



British Columbia Securities Commission
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Dear Ms. Tassie,

RE: Comment re BCN 2013/09 Proposed Amendments to Conditions of Registration

I am Chief Compliance Officer and general counsel to PI Financial Corp. ("PI"). I am pleased to provide the following comments, on behalf of PI, to the British Columbia Securities Commission ("BCSC") on the proposed amendments to the *Conditions of Registration for Dealers with a BC Office that Trade in the U.S. Over-the-Counter Markets* contained in BCN 2013/09 (the "proposed amendments").

By way of introduction, PI is a member of the Investment Industry Regulatory Organization of Canada and is registered as an Investment Dealer in all provinces and territories of Canada. PI has approximately 250 employees in six major cities across Canada, and we have over 30,000 clients. PI conducts a minimal amount of its business trading OTC issuer securities (on average less than 3% of its other equity commission revenue as measured by the *Conditions of Registration*).

PI supports the BCSC's efforts to protect the integrity and reputation of British Columbia's capital markets. PI shares the concern that difficulties in obtaining, or an outright inability to obtain, information on clients of financial institutions that are resident in jurisdictions which are not IOSCO MMOU signatories could reduce the effectiveness of the BCSC's investigations and enforcement efforts. PI feels that those concerns extend not only to activities of those financial institutions in OTC issuers but also to activities of those financial institutions on every marketplace, including Canadian ones.

On the other hand, PI is concerned that the proposed amendments would require a number of compliance steps which can only be accomplished through manual intervention (these steps are discussed below). It is axiomatic that any steps requiring manual intervention, including human review or judgment, are subject to the potential for human error. Accordingly, in our opinion, a requirement for dealers to absolutely prohibit certain activities of those financial institutions in OTC issuers would be subject to a significant number of sources of potential human error, and therefore virtually impossible to comply with as a strict rule (for which dealers could be subject to enforcement action for non-compliance).

In addition to the concerns over the possible sources of human error, PI has concerns about the restrictions on transfers, as well as the cost of compliance with the proposed amendments (these concerns are also discussed below).

PI has determined that the basic steps required to comply with the proposed amendments are as follows:



- 1) **Identify** accounts of “financial institutions” in non-IOSCO MMOU jurisdictions (“restricted financial institutions”). Existing systems do not capture this information, so identification of these accounts would require the following steps:
 - a) the dealer must identify *existing* accounts that **might** be “financial institutions” in non-IOSCO MMOU jurisdictions. This could be performed by conducting a search using existing systems for corporation-type accounts, in jurisdictions which exclude IOSCO MMOU signatories. This search could be based on the assumption that all “financial institutions” are corporations, otherwise further detail on the types of entities which could fit within the category of “financial institution” would be required (for example partnerships, trusts, etc.); and
 - b) the dealer would then be required to have staff manually review the account opening documents for each account on the list generated in step 1)a) to determine whether they qualify as a “financial institution”. In some cases this might be obvious, but in other cases this would require the judgment of the reviewer and be subject to potential error; and
 - c) the dealer must perform the steps in 1)a) and 1)b) for every *new* account at account opening time. It might be possible for such an account to slip through in error, and again the identification as a “restricted financial institution” could be subject to error.

- 2) **Code** the “restricted financial institution” accounts so that the dealer’s staff are able to identify those accounts when reviewing for the “account activities” described in the proposed amendments (deposit, transfer, or trade). This could be accomplished using existing systems; provided that each “restricted financial institution” account had been correctly identified in step 1).

- 3) **Restrict** the “restricted financial institutions” from conducting the “account activities”:
 - a) **Deposits** - While the receiving dealer has the ability to review positions being delivered to it physically or electronically, and reject unwanted positions, each position would require manual review by the dealer’s staff to determine:
 - whether the receiving account is coded as a “restricted financial institution”; and
 - whether the securities to be deposited are of an OTC issuer or not.

Both of the above would be subject to possible error.

 - b) **Transfers** - (We assume this refers to transfers-out from an account, as opposed to a deposit-in. If not please advise, as our response may be different.) For OTC issuer positions existing prior to the effective date of the proposed amendments, we query the principle by which a client could be prohibited from transferring such a position out to another dealer, or taking physical delivery out of the account (if the client chooses not to liquidate the position as permitted by the proposed amendments).

Similarly, for a position where an error has been made in the 3)a) stage and a deposit has been permitted in error, we query the principle by which a client could be prohibited from transferring that position out to another dealer, or taking physical delivery of that position out of the account. If the client is unable to liquidate the position through the BC dealer, it follows that they should have the ability to transfer the position out.

- c) **Trades** – There are two methods for entering orders on OTC issuers as follows:
- **Orders entered through an electronic order management system (“OMS”).** Using existing systems, orders for “restricted financial institutions” can be blocked from execution on a particular marketplace;
 - **Orders entered using a physical ticket delivered to the firm’s trading desk.** These could be manually reviewed by: the investment advisor who originates the order, and by the firm’s trading desk, for whether the account is coded as a “restricted financial institution” and whether the order relates to an OTC issuer. Again, these reviews would be subject to possible error, by which prohibited orders could be entered, and transacted, in error by the dealer.

I note parenthetically that manual reviews such as this (by the trading desk) would also have the effect of slowing down the execution process for legitimate orders.

To place the proposed amendments into the proper context, complying with a Cease Trade Order (“CTO”) is a much simpler task. For example, when a CTO is issued the issuer is expressly identified, creating a bright line test whereby: the dealer’s security master is coded to indicate that the issuer has a CTO; the dealer’s OMS system automatically excludes orders in any CTO’d issuers; and, any error at the trade desk is excluded from processing and easily corrected. There are far fewer sources for error with CTOs because the restricted issuer is expressly identified and compliance is mostly automated. Unfortunately, the proposed amendments do not lend themselves to similar electronic solutions.

Finally, I note that the BCSC has expressed its view that the costs of compliance with the proposed amendments to dealers are outweighed by the benefits. When additional manual reviews are required, either more staff is required, or the new reviews must be delegated to existing staff. In our view, the proposed amendments would require dealers to commit virtually the same resources to compliance regardless of the amount of OTC issuer business conducted by the dealer. This would be challenging in the current negative market environment when any additional costs, or workload burden, could have a significant negative impact on small and medium sized BC dealers. Ultimately, additional costs are passed on to clients.

In summary, we respectfully submit that the numerous possible sources for human error are such that the proposed amendments would be virtually impossible for dealers to implement as a strict rule, and the costs or additional workload involved could have a significant negative impact on some BC dealers.

That having been said, PI would be pleased to participate in discussions with the BCSC to determine what steps dealers could reasonably take to assist in alleviating the concerns expressed in BCN 2013/09.

Yours truly,
PI FINANCIAL CORP.

Richard Thomas
Senior Vice President Compliance & Corporate Secretary

RWT/ej

Cc: Executive Committee
Compliance Committee