



BC Notice 2012/11

**Second Notice and Request for Comment  
Maple Group Acquisition Corporation  
Proposed Acquisition of TSX Venture Exchange Inc.**

**I Introduction**

This is a request for comment about whether the British Columbia Securities Commission ought to grant an application by Maple Group Acquisition Corporation to amend the recognition order relating to the TSX Venture Exchange and, if so, the conditions and undertakings that ought to accompany any amendment. Maple's application is in connection with its proposed acquisitions of the TMX Group Inc. and other entities.

**II Background**

In June 2011, Maple offered to acquire all of the issued and outstanding common shares of TMX Group, a public company listed on the Toronto Stock Exchange.

TMX Group's principal subsidiaries are TSX Inc. (which operates the Toronto Stock Exchange), TSX Venture, the Natural Gas Exchange Inc., the Bourse de Montréal and the Canadian Derivatives Clearing Corporation (CDCC).

Maple also intends to acquire the parent of the Alpha Exchange Inc. and to acquire the Canadian Depository for Securities Limited (CDS) with a view to taking advantage of potential synergies between CDS and CDCC.

Maple's 13 owners are all large Canadian financial institutions. Maple's owners include the investment dealer subsidiaries of four Canadian chartered banks (CIBC, National Bank, Scotiabank, and TD Canada Trust) and five Canadian pension funds (Alberta Investment Management Corporation, Caisse de Depot et Placement de Québec, Canada Pension Plan Investment Board, Fonds de Solidarité des Travailleurs de Québec, and Ontario Teachers' Pension Plan). One Maple investor is based in Alberta. The rest are based in Ontario and Québec. None is based in British Columbia.

We held consultations in the summer of 2011 about Maple's proposed acquisitions. We also published for comment in October 2011 Maple's application (see BCN 2001/27). We have considered the comments received from these sources, as well as those made to other securities regulators, including those made during public hearings. We have participated in discussions between Maple and the Ontario Securities Commission, the Alberta Securities Commission, and the Québec Autorité des Marchés Financiers (AMF).

### **III Risks Associated with the Proposed Acquisitions**

#### **A Risks Relating to Canada's Securities and Derivatives Markets Generally**

If the proposed acquisitions are completed, Maple will control:

- all of the significant equities trading facilities in Canada
- one of the most significant derivatives trading facilities in Canada, and
- the significant clearing agencies in Canada.

This concentration of control of the mechanism of securities and derivatives trading and clearing in Canada raises significant public interest issues in the context of securities regulation. It creates the opportunity for significant conflicts of interest, for anti-competitive behaviour, for inappropriate access to market information by Maple owners that is unavailable to competitors, and for increased systemic risk.

These issues are under consideration by the Ontario Securities Commission. The AMF is also considering them in connection with Maple's proposed acquisition of CDS.

The OSC is proposing recognition orders for Maple, TMX Group, TSX, and CDS containing a comprehensive set of conditions and undertakings intended to address these risks. For example, the orders would specify the number of independent directors on the boards of Maple, TMX Group, TSX, and CDS. They contemplate significantly increased oversight of all of these entities by the OSC. They would impose a fee model for CDS and a significant governance role in CDS for industry committees. The OSC has published these draft orders for public comment.

We will consider the comments of those responding to the OSC's request for comment. We encourage those with an interest in the proposed acquisitions to respond to the OSC request for comments.

#### **B Risks Relating to the Canadian Venture Market**

The Commission is particularly interested in the impact that Maple's acquisition of the TMX Group and CDS could have on the Canadian venture market.

The Canadian venture market is critically important to the economy of British Columbia. The venture market owes its vigour to the presence of TSX Venture in British Columbia. TSX Venture is recognized internationally as the leading exchange for venture capital raising in the world.

British Columbia companies also have a significant presence on TSX Venture – they make up 50% of its listed issuers and 44% of its total market capitalization. British Columbia companies also comprise 35% of the listed companies on the combined TSX Venture and TSX.

The strength of the venture market also benefits the economy of Canada. Venture market companies create more jobs across Canada than any other group of employers. TSX Venture is the single largest source of new listings on the Toronto Stock Exchange.

It is in the public interest that the venture market's presence and strength in British Columbia be preserved and that it operate in an environment that fosters its future growth and prosperity.

Today, the TMX Group is a widely-held public company. Its board need focus only on the best return for its shareholders. Management applies the expertise necessary for its exchanges, including TSX Venture, to be successful. The international reputation that TSX Venture has established shows that the current ownership structure has served TSX Venture well.

If the acquisitions proposed by Maple are completed, the dynamics will be different. The control of TMX Group will be concentrated in the hands of only 13 major financial institutions, who would control almost all aspects of trading and clearing of securities and derivatives in Canada. It does not necessarily follow from that alone that the TMX Group board's focus will change. However, Maple nominees would hold 8 of 17 seats on the Maple board (which Maple proposes be the same board as TMX Group, TSX, and TSX Venture). There is a risk that the Maple nominees could influence the board to direct TSX Venture management to make decisions that suit objectives of the Maple owners but are not necessarily optimal for the success of TSX Venture.

Today, CDS focuses on efficiencies to keep clearing costs low. It operates on a cost-recovery basis. If the proposed acquisition of CDS by Maple is completed, Maple will operate CDS on a for-profit basis.

We have identified these as the major risks associated with the proposed acquisitions that relate to the Canadian venture market:

1. Maple's owners are all large financial institutions and all but one are based in central Canada. The experience, expertise, and innovation associated with the Canadian venture market reside primarily in western Canada. Has the Maple owners' investment and operational experience prepared them to believe in the critical importance of the venture market in Canada? Will Maple owners understand the vital

role of the venture market to the Canadian capital markets and understand what it takes to make a venture market successful?

If not, there is a risk that Maple-nominated directors may influence the board to make decisions about fees or services, or adopt policies or practices that, although perhaps beneficial (or at least tolerable) to the senior market, are damaging to the venture market.

2. Will Maple's owners understand the particular sensitivity of the venture market to fees and charges, as measured by their impact on the competitiveness of TSX Venture? Will they understand how rules can also erode competitiveness by stifling innovation?

If not, there is a risk that Maple-nominated directors may influence the board to make decisions about fees, charges and rule requirements that will damage TSX Venture's competitiveness.

3. Will Maple's owners understand the contribution of the non-bank dealers who underwrite, finance, and trade the venture business, and whose role is essential to the health of the venture market? Will they understand the potential damage that can be done to those dealers, and by extension to the venture market itself, by increases in CDS clearing and settlement fees or capital and collateral requirements?

If not, there is a risk that Maple-nominated directors may influence the CDS board to make decisions about these changes that could compromise the ability of those dealers to carry on the business that is essential for the venture market to thrive.

4. Will Maple's owners be motivated to make the financial and operational commitments necessary to ensure the continued health and growth of the venture market, based on the existing experience and expertise in British Columbia?

If not, there is a risk that the vigour of TSX Venture could be dissipated through benign neglect.

The Commission has to decide whether any of these risks, or a combination of them, constitute a threat to the Canadian venture market sufficiently serious to conclude that Maple's proposed acquisitions would, if completed, be prejudicial to the public interest in British Columbia.

#### **IV Conditions and Undertakings Related to the Risks**

##### **A Risks Relating to Canada's Securities and Derivatives Markets Generally**

As noted above, the OSC has proposed recognition orders that contain a comprehensive set of conditions and undertakings intended to deal with the risks associated with director independence, conflict of interest, anti-competitive behaviour, and inappropriate access to information.

These conditions and undertakings do not extend to TSX Venture. We think that the conditions and undertakings proposed by the OSC for Maple, TMX Group, and TSX ought to apply as well to TSX Venture. Our draft recognition orders and undertakings would do so, and we have generally followed the language used in the Ontario orders to avoid the risk of differing interpretations of what is intended to be the same requirements.

##### **B Risks Relating to the Venture Market**

We have considered a set of conditions and undertakings that may address the risks to the venture market we identified above. Among the questions we are asking commenters to consider is whether these conditions and undertakings are adequate to address the risks.

#### **1. Venture Market Commitment and Understanding**

##### ***Mission statement***

The conditions and undertakings would require Maple, TMX Group, TSX and TSX Venture to adopt a mission statement objective that they maintain and grow a competitive Canadian public venture market that leads the world in venture financing.

The conditions and undertakings would require Maple, TMX Group and TSX to ensure there is meaningful and ongoing consideration of, and support for, the venture market by TSX Venture's parent companies. This would include the allocation of sufficient financial and other resources to TSX Venture to ensure that it can perform its functions in a manner consistent with the mission statement, the conditions and undertakings, and the public interest.

##### ***Corporate governance***

Maple proposes that Maple, TMX Group, and all of the companies within the TMX Group, including TSX and TSX Venture, would have "mirror boards" – that is, the same individuals would constitute the board of each company. This would be a continuation of the board structure that the TMX Group has had to date.

We considered requiring that TSX Venture have a separate board with a majority of its directors having venture market qualifications. This would, we thought, ensure significant venture experience on the TSX Venture board to ensure that the TSX Venture

board was sufficiently independent and could focus specifically on the venture market and venture issues.

Representatives of TMX Group and TSX Venture have persuaded us that it is not necessary, and indeed could be counterproductive, to require that the TSX Venture board be constituted differently. They say the current structure ensures that venture market issues inform the overall corporate strategy, and they credit the board structure as one of the key factors in establishing a unified corporate culture.

On the basis that Maple and TMX Group will continue to have mirror boards – in other words, one board would function as the board of all the companies in the group – the conditions and undertakings require that at least 25% of the directors on that board have Canadian venture market experience and expertise.

A person would be considered to have Canadian venture market experience and expertise if he or she has currently relevant and direct experience developed through a significant period of employment in:

- operating and financing an issuer in the Canadian venture market, or
- underwriting or financing Canadian venture issuers or advising Canadian venture issuers on financing, trading, or mergers and acquisitions.

Whether an individual has Canadian venture market experience and expertise would be assessed from the perspective of whether a reasonable person actively engaged in the Canadian public venture capital market would consider the individual to have currently relevant and direct experience.

#### ***Advisory committees***

The conditions and undertakings would require TSX Venture to have one or more industry advisory committees comprised of Canadian public venture market participants, with reporting obligations to the Maple/TMX Group board and the Commission. In any case where the Maple/TMX Group board has not followed a committee's advice, the board would be required to provide an explanation to the Commission. Annually, the Maple/TMX Group board would provide a report to the Commission summarizing the recommendations and advice of the advisory committees and how the board responded.

The Public Venture Market Committee of the Maple/TMX Group board would also report annually to the Commission about its recommendations and advice to the Maple/TMX Group board. The Maple/TMX Group board would provide a written explanation to the Commission as soon as practicable in each case where it has not followed the recommendation or advice of that Committee.

## **2. Fees, Charges and Rules**

The conditions and undertakings would require that the Commission approve any changes to TSX Venture rules or fees.

## **3. Impact of CDS on the Role of the Dealers in the Venture Market**

Maple intends to operate CDS for profit. To date, CDS has been operated on a cost-recovery model, with the result that clearing costs in Canada are among the lowest in the world. The conditions and undertakings would include a fee model, requirements to ensure independence from Maple in CDS' governance structure, strong marketplace committees, and ongoing regulatory oversight of any changes to fees, collateral requirements, and terms of access. These requirements would closely follow those proposed by the OSC, and we would intend to coordinate our oversight of CDS with the OSC.

More specifically, the conditions and undertakings would require that:

- the Commission approve all changes to access, fees, capital and collateral requirements, the risk model, and membership criteria,
- at least two directors on the CDS board, and one director on the CDS board Risk Management and Audit Committee, have venture market experience and expertise,
- at least one member of each CDS marketplace advisory committee have venture market experience and expertise, and
- if the CDS board does not follow a committee's advice, it provide an explanation to the Commission.

## **4. Ongoing Health and Growth of the Venture Market**

TSX Venture currently has significant venture market expertise and infrastructure in Vancouver and Calgary. Oversight of TSX Venture is shared between the Commission and the Alberta Securities Commission.

The conditions and undertakings require Maple and TMX Group to:

- maintain TSX Venture's existing operations in Vancouver
- develop the TSX Venture Vancouver office as the center of TSX Venture's efforts to maintain and grow a competitive Canadian public venture market that leads the world in venture financing
- locate in TSX Venture's Vancouver office executive leadership, management, and significant operational talent for:
  - developing innovations in the venture market
  - developing policy that enhances the competitive position of TSX Venture
  - ensuring TSX Venture's continued expertise in the venture market

- ensuring TSX Venture's continued capacity to operate the TSX Venture Exchange

TSX Venture's compliance with this requirement does not imply that it will need to alter its current operations or staff complement in Alberta, nor will it prevent TSX Venture from having operational talent in any jurisdiction outside British Columbia. This requirement will not alter the shared oversight arrangement with Alberta.

## **5. Other Risks**

### ***Conflicts of interest, anti-competitive behaviour, inappropriate access to information***

To address conflicts of interest and the opportunities for anti-competitive behaviour and inappropriate access to information, we have, as mentioned above, included in the draft conditions and undertakings requirements relating to TSX Venture that correspond to those the OSC proposes for Maple, its owners, TMX Group, and TSX. These could:

- address conflicts of interest raised by Maple shareholders' ownership of TSX Venture
- address anti-competitive behaviour, including in setting fees and incentives, and relating to clearing and settlement
- protect the confidentiality of information Maple shareholders access through their ownership

### ***Systemic risk***

The proposed acquisitions would result in a concentration of control of Canada's equity and derivatives markets and clearing facilities that could significantly increase systemic risk in Canada's equity and derivatives markets. The proposed acquisitions risk the creation of an entity "too big to fail". Were something to occur that put Maple at financial risk, the consequences to the securities and derivatives markets would be unpredictable.

The conditions and undertakings described in this notice do not directly address the issue of systemic risk.

These circumstances demand rigorous risk management by Maple and increased oversight by Canadian securities regulators as the primary means of identifying and addressing emerging systemic risks before they significantly affect the Canadian markets.

### ***Increased regulatory oversight***

Although the conditions and undertakings described in this notice may address the risks associated with the proposed acquisitions, it is not possible to contemplate in advance all of the implications and consequences that may result should the proposed acquisitions be completed.

The conditions and undertakings therefore require that the Commission must approve any change to the business or operations of TSX Venture or CDS that:

- is outside the ordinary course of its business, or
- is inconsistent with its past business or operational practices.

### ***Alpha***

We do not have enough information about Maple's plans for Alpha to evaluate the risks of that acquisition. If Maple acquires Alpha, we would consider whether it would be appropriate to continue Alpha's exemption from recognition in British Columbia, or whether we should recognize Alpha. We would further consider whether the terms and conditions we propose for TSX Venture would also be appropriate for Alpha.

## **V Appendices**

Appendix A is the draft recognition order that contains the conditions described above.

Appendix B contains the draft undertakings described above.

Appendix C contains the draft undertakings of the original Maple shareholders.

Appendix D contains a summary of the comments received in response to the October 2011 request for comment on the Maple application.

## **VI Questions for Comment**

We encourage all market participants – including dealers, advisers, issuers, investors, and professionals – to comment on the conditions and undertakings described in this notice, including those relating to CDS and those presented in detail in Appendices A, B and C.

In particular, we seek comment on these questions:

1. Have we identified all of the most significant risks associated with Maple's proposed acquisitions? Have we overstated any of the risks?
2. Would the conditions and undertakings in Appendices A, B and C, and those this notice describes relating to CDS, be adequate to address the risks? Are any of those conditions and undertakings unnecessary or counter-productive?
3. Do the proposed acquisitions present risks to the venture market that cannot be adequately addressed by any conditions or undertakings?
4. Will rigorous risk management by Maple and enhanced regulatory oversight be adequate tools for identifying and addressing emerging systemic risks?

Please submit your comments in writing to the Commission on or before June 22, 2012.

Deliver your comments or refer your questions to:

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We cannot keep submissions confidential.

May 24, 2012

Brenda M. Leong  
Chair