CANADIAN SECURITIES ADMINISTRATORS

NOTICE OF AMENDMENTS
TO
NATIONAL INSTRUMENT 24-101
***INSTITUTIONAL TRADE MATCHING AND SETTLEMENT* AND**
COMPANION POLICY 24-101CP *INSTITUTIONAL TRADE MATCHING AND SETTLEMENT*

I. Introduction

The Canadian Securities Administrators (the CSA or we) have made amendments to National Instrument 24-101 *Institutional Trade Matching and Settlement* (NI 24-101 or the Instrument) and Companion Policy 24-101CP *Institutional Trade Matching and Settlement* (Companion Policy or CP).

The key amendment to the Instrument will maintain the current requirement to match DAP/RAP trades[1] by no later than noon on the business day following trade date (noon on T+1). Specifically, NI 24-101 will no longer provide for a transition to a requirement that DAP/RAP trades be matched by no later than midnight on trade date (midnight on T). We are also amending the documentation requirement, the provisions governing non-western hemisphere client trades, certain definitions and other provisions in the Instrument, including Forms 24-101F1, F2 and F5. Corresponding amendments to the CP have also been made.

We note that we are not implementing other proposals described in our Notice and Request for Comments published on October 30, 2009 (the CSA Request Notice),[2] in particular, a proposal to extend to 2 p.m. on T+1, for a transition period of two years, the current noon on T+1 deadline for matching DAP/RAP trades, and a proposal to simplify the calculation of the 90% target for exception reporting purposes.

Subject to Ministerial approval, the amendments to the Instrument will come into force on July 1, 2010 in all CSA jurisdictions. Additional information regarding the implementation or adoption of the amendments to the Instrument in each province or territory is included in Annex A. A list of the commenters, as well as a summary of comments and our responses to them, are included in Annex B. Annex C contains a report of industry compliance with NI 24-101. The amending instrument for NI 24-101 is in Annex D, with the corresponding blackline in Annex E. The amending instrument for the Companion Policy is in Annex F, with the corresponding blackline in Annex G. Where applicable, Annex H contains local material.

The materials are also available on websites of CSA jurisdictions, including:

www.lautorite.qc.ca
www.albertasecurities.com
www.bcsc.bc.ca
www.gov.ns.ca/nssc
www.nbsc-cvmnb.ca
www.osc.gov.on.ca
www.sfsc.gov.sk.ca
www.msc.gov.mb.ca

II. Background

The amendments were published on October 30, 2009 for a 90-day comment period. We received 15 comment letters in response to the request for comments. We have considered the comments received and thank all commenters for their submissions. We briefly discuss below some of the key stakeholder comments and CSA decisions made in respect of the proposed amendments to NI 24-101. More detail is provided in Annex B.

III. Discussion

A. Key amendments

The CSA Request Notice had proposed to defer the requirement to match a DAP/RAP trade no later than the end of T by an additional period of five years (that is, from July 1, 2010 to July 1, 2015). We had asked for stakeholders' views on the length of this deferral. We had also asked whether the requirement should be deferred indefinitely until such time as global markets shorten their standard T+3 settlement cycles. We had specifically sought input on the costs and benefits of moving on July 1, 2015 to matching by midnight on T.

Most commenters were of the view that moving to the midnight on T deadline from the current noon on T+1 deadline was not justified from a cost-benefit perspective without a clear indication that the standard T+3 settlement cycle in North American capital markets would be shortened. Many commenters felt that there was no inherent value or benefit from requiring institutional trade matching (ITM) by midnight on T compared to noon on T+1, given the standard T+3 settlement cycle.

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[1] A DAP/RAP trade is a trade executed for a client account that permits settlement on a delivery against payment or receipt against payment basis through the facilities of a clearing agency, and for which settlement is made on behalf of the client by a custodian other than the dealer that executed the trade. See definition of "DAP/RAP trade" in section 1.1 of the Instrument.

[2] See (2009) 32 OSCB 9059.

While we still encourage industry to work towards a same-day ITM goal, we acknowledge that a regulatory requirement to achieve this goal may no longer be appropriate at this time. Industry stakeholders appear almost unanimous in their view that it will take a compression of the settlement cycle to provide both a strong business and regulatory rationale to invest in the necessary resources and technological upgrades for moving to same-day matching. According to the industry, in the current settlement cycle of T+3, there may be no clear benefit to matching trades 12 hours earlier. While one commenter provided strong arguments that same-day matching would further reduce settlement fails and back-office costs in the Canadian markets, others indicated that it was not clear that matching trades 12 hours earlier would further mitigate any settlement risk or further enhance current settlement efficiency.

As there are no plans to shorten the T+3 settlement cycle in global markets at this time, we have decided to maintain the current ITM noon on T+1 deadline. Therefore, NI 24-101 will no longer provide for a transition to an ITM deadline of midnight on T. However, we would propose to consider re-introducing the midnight on T matching deadline into the Instrument through subsequent amendments if circumstances were to change. For example, as noted in the CSA Request Notice, a change in circumstances would include a shortening of standard T+3 settlement cycles in global markets.

In the CSA Request Notice, we had also sought input on whether we should extend the current ITM noon on T+1 deadline to 2 p.m. on T+1 for an interim period of two years. We had suggested that extending the current deadline by an additional two hours for two years may provide market participants with additional time to address delays and other ITM challenges that they are currently experiencing. However, most commenters were of the view that, although well intentioned, moving the current deadline to 2 p.m. on T+1 for two years might actually create more hardship than help for market participants to achieve their ITM goals. The commenters were almost unanimous in their view that such a change would require firms to incur additional costs, involve more scarce resources and be disruptive, only to have the industry revert back to noon on T+1 in two years. Most commenters support maintaining the noon on T+1 target. Another commenter noted that a change in the matching deadline, from 12:00 p.m. to 2:00 p.m. on T+1, would not make a material difference in matching rates for many of the participants. We acknowledge these strong views, and consequently will not implement this proposal.

In addition, the CSA Request Notice had sought input into a number of potential industry-wide infrastructure issues. We noted that a large number of dealers and advisers that actively trade on a DAP/RAP basis in Canada seemed unable to match 90% of their institutional equity trades by noon on T+1 due in part to such industry-wide infrastructure issues, which in turn directly impacted the adequacy of their ITM policies and procedures. For example, we had suggested that if ITM processing could continue beyond the 7:30 p.m. system shutdown time at CDS Clearing and Depository Services Inc. (CDS) until later in the evening, more trade-matching parties and their service providers might be willing to tighten their policies and procedures, including shifting their resources and reconfiguring their systems, to complete the ITM processes in the evening of T rather than in the morning of T+1. In the CSA Request Notice, we had asked what would be the costs and benefits of extending the current industry ITM processing times to allow market participants to process their trades beyond the CDS 7:30 p.m. cut-off time until later in the evening on T.

Most commenters questioned the need to change the current CDS 7:30 p.m. system shutdown time to a later time in the evening. They shared the view expressed by CDS that the closedown of its online system for approximately two hours or less does not have a negative impact on matching rates. CDS stated that, once the system is back up after the closedown period, there is sufficient time to process all trade instructions received during the closedown period and typically well before the 11:59 p.m. deadline for end-of-T matching. It added that there could be many downstream impacts on changing the timing of CDS' current delivery schedule as well as on external participants, service bureaus and vendors. It further suggested that, unless a complete end-to-end review is undertaken by all affected parties in the processing chain to determine the operational impacts and costs associated with changing CDS' processing schedules, it would be difficult to ascertain whether there is an overall benefit to be achieved by the industry.

We had also suggested that the inability to track non-western hemisphere trades may have had an adverse effect on dealers' ITM performance, forcing some to needlessly complete and deliver quarterly exception reports on Form 24-101F1 and that, if specific trade identifiers were made available, certain dealers might be able to demonstrate that at least 90% of their trades in a quarter were matched by the deadline. In the CSA Request Notice, we had asked what would be the costs and benefits of having a specific industry-wide trade identifier to enable dealers to track and segregate their non-western hemisphere trades from western hemisphere trades.

Most commenters addressing this question were of the view that the cost of building an industry-wide specific trade identifier for distinguishing between western and non-western hemisphere trades may not justify the investment required and other business costs involved. A number of commenters also made the point that, from an operational perspective, in many cases it is unclear how to identify the source of a trade.

B. Other amendments

In the CSA Request Notice, we had proposed a number of other amendments that were intended to:

- lessen the regulatory burden of certain requirements of the Instrument,
- clarify certain provisions as a result of issues that were raised by stakeholders, including during the discussions of the CSA-Industry Working Group on NI 24-101 (Working Group), and
- modify the ITM reporting requirements of clearing agencies and matching service utilities (MSUs) under the Instrument.

Stakeholders who provided feedback on such other amendments were generally in favour of them, in part because of the above noted considerations. We discuss the final amendments below.

(a) Amending the quarterly exception reporting requirement

Because of our decision to maintain indefinitely the current ITM noon on T+1 deadline, NI 24-101's transitional rules will no longer be required. As a result, we are making the following amendments to the Instrument:

- References to "the end of T" and "the end of T+1" in Part 3 of the Instrument are being changed to "12 p.m. (noon) on T+1" and "12 p.m. (noon) on T+2" respectively.
- As proposed in the CSA Request Notice, the references to "95 percent" in Part 4 of the Instrument governing the exception reporting requirement are being changed to "90 per cent".

In the CSA Request Notice, we had proposed to amend the Instrument, including Exhibit A of Form 24-101F1, to simplify the method for determining the 90 per cent threshold for exception reporting by (i) eliminating the need to determine the threshold based on the total value of equity trades (thus retaining the total number of trades method only for equity trades) and (ii) eliminating the need to determine the threshold based on the total number of debt trades (thus retaining the total value method only for debt trades). While some commenters supported this proposal, others suggested the changes were not useful. The industry is currently using both methods for determining the threshold for both equity and debt securities trades, and have built their reporting processes to measure both volume and value. Some stakeholders suggested that this change will not have a positive effect on most market participants, and may even be counterproductive as many market participants use the processes currently in place for purposes beyond compliance with NI 24-101 and will continue to calculate both regardless of modifications to the regulatory requirements. As a result of these comments, we have decided not to proceed with these proposed amendments.

However, CSA Staff will, in consultation with the Working Group, consider making further amendments to Exhibits B and C of Form 24-101F1 later this year.

(b) Amending the pre-DAP/RAP trade execution documentation requirements and related key definition

As proposed in the CSA Request Notice, we are making the following amendments to the Instrument:

- The definition of "trade-matching party" in Part 1 of the Instrument is being amended in two ways. First, paragraph (a) of the definition is being amended to include a registered adviser only where it is acting for the institutional investor in *processing* the trade.

  Second, paragraph (b) of the definition is being amended by excluding institutional investors that are (i) individuals or (ii) persons and companies with total securities under administration or management not exceeding $10 million. The language for the latter exclusion is different from the version proposed in the CSA Request Notice. We made a slight modification to ensure that the language is similar to existing paragraph (5) of the definition "Institutional Customer" in the dealer member rules of the Investment Industry Regulatory Organization of Canada (IIROC). One commenter had suggested that, under the proposed language described in the CSA Request Notice, dealers would have an additional responsibility to monitor their clients' accounts or assets "under administration or management of less than $10 million". As dealers are already required under IIROC rules to monitor the accounts of non-individuals with total securities under administration or management exceeding $10 million, we do not expect this to be an additional burden for dealers.

- Sections 3.2 and 3.4 of the Instrument are being amended to make it clear that the documentation requirements of such sections support, and are part of, the primary ITM policies and procedures requirements of sections 3.1 and 3.3 of the Instrument. The drafting of the amendments to sections 3.2 and 3.4 differs slightly from the text in the CSA Request Notice, but no substantive change is intended.

(c) Amendments to the provisions governing non-western hemisphere institutional investors

As proposed in the CSA Request Notice, we are making amendments to subsections 3.1(2) and 3.3(2) of the Instrument to clarify that they apply to an institutional investor whose *settlement instructions* are usually made in and communicated outside the geographic region specified in those subsections. The geographic region specified in those subsections is presently described as the "western hemisphere". We agree with a number of commenters that this description is not sufficiently precise. Consequently, we are amending those subsections so that the geographic region is described instead as the "North American region", comprising Canada, the United States, Mexico, Bermuda and the countries of Central America and the Caribbean. In the context of the Canadian markets, it is appropriate to distinguish trades in this region from trades elsewhere in order to apply the different ITM deadlines of Part 3.

(d) Amendments to clarify certain other definitions and concepts and to modify Forms 24-101F2 and F5

As proposed in the CSA Request Notice, we are making non-substantive amendments to the definitions of "clearing agency", "institutional investor", "T+1", "T+2" and "T+3" in Part 1, paragraph (f) of section 2.1, Forms 24-101F1, 24-101F2 and 24-101F5, and other minor changes. Blackline versions of the Instrument and CP reflecting these amendments are in Annexes E and G.

C. Other stakeholder comments

The summary of comments and responses in Annex B describes other comments made by stakeholders. A number of stakeholders acknowledged the positive impact of NI 24-101 on ITM and settlement processes in Canada. They support the CSA's ongoing efforts to implement a framework for the timely and efficient processing and settlement of trades.

We had noted in the CSA Request Notice that NI 24-101 may have contributed to the overall decline of the fails-to-deliver rates in Canada since April 2007, when the Instrument came into force. We had also noted that NI 24-101 contains, in addition to the ITM requirements, a principle-based settlement rule that requires registered dealers to establish, maintain and enforce policies and procedures designed to facilitate settlement of trades by no later than the standard settlement date, which is typically T+3. We had explained that, while we are not proposing any amendments at this time to NI 24-101's settlement rule, a working group comprised of staff from a number of CSA jurisdictions and IIROC is assessing, among other things, whether Canada's trade settlement discipline regime may need to be strengthened in light of recent international developments. We had sought comments in the CSA Request Notice on whether our settlement discipline regime may need to be strengthened, including whether NI 24-101's settlement rule should be amended.

Unfortunately, we received few comments on this topic. However, one commenter suggested that, in their experience, on a daily average over a six month time frame, fully 99% of a given day's trades are settled by the contractual settlement date. The commenter said that, of the remaining one per cent of unsettled trades (fails), three quarters of these trades were confirmed by their counterparties, but placed on hold by the same counterparties for lack of funds or securities – suggesting that high matching rates do not necessarily guarantee settlement of any given trade. Another commenter, however, made strong arguments that same-day ITM and improved levels of automation lead to reduced operational risk and improved settlement efficiency.

D. CSA Staff Report

At the same time as we are publishing this notice and the final amendments to the Instrument and CP, we are publishing in Annex C a report of CSA Staff's findings of an analysis of the data from the quarterly exception reports submitted by registered firms on Form 24-101 F1, and from quarterly reports submitted by CDS and an MSU on Forms 24-101 F2 and F5, respectively. The report also contains some high-level observations of CSA Staff's discussions with stakeholders, including discussions with the Working Group.

E. Repeal or revocation of local transitional rules or orders

The amendments will mean that the extended transitional phase-in periods that were put in place in 2008 by local rules or blanket orders in the various jurisdictions are no longer necessary. Concurrent with the amendments coming into force, each of the jurisdictions will repeal or revoke its local rule or blanket order, as the case may be. Where applicable, full details of the specific rules or blanket orders impacted in each jurisdiction are set out in Annex H to this Notice. In British Columbia, this will mean the revocation of BC Instrument 24-502 *Extension of transitional phase-in period for National Instrument 24-101 – Institutional Trade Matching and Settlement*.

F. CSA Staff Notice 24-305

As a result of the amendments to the Instrument and CP, CSA Staff propose to amend and republish CSA Staff Notice 24-305 *Frequently Asked Questions About NI 24-101 -- Institutional Trade Matching and Settlement and Related Companion Policy* later this year.

IV. Questions

Please refer your questions to any of the following:

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