



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

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Mr. Jacques Tanguay
Vice-President, Regulatory Division
Bourse de Montréal Inc. (the Bourse)
Tour de la Bourse, P.O. Box 61
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Montreal, Quebec H4Z 1A9

Dear Mr. Tanguay:

Re: Clarifications on Large Open Position Reporting (LOPR) Issues

First, we wanted to thank you very much for the Regulatory Division's announcement of a delay in LOPR implementation, as described in the Regulatory Division's July 14th Circular 125-2011. We look forward to continuing to work together to implement LOPR.

Second, thank you for your letter of June 9, 2011. It has helped clarify some issues and suggest where further discussions would be fruitful. As you know, we have also met with the Office of the Privacy Commissioner of Canada (OPC), which amplified rather than addressed our concerns in one or two areas, causing us to revise our views on a number of points. While you have our response to the proposed Rule amendments, we wanted to provide some additional clarifications with respect to your June 9 letter, and list them below in the order in which they appear in your letter.

I. CHANGES

1.a Requirement to Provide Client's SIN

No comment.

1.b Confidentiality of Information Submitted

We hope we can discuss the content of the draft Confidentiality Agreement sent on May 27, 2011. We are sorry if it appeared that we saw the Bourse simply as another service provider as we recognize the important role that the Regulatory Division plays in the derivatives marketplace and know that it differs from that of service providers. The confidentiality agreements provided to service providers are more extensive than reflected in the first draft of the agreement proposed by the IIAC to the Bourse and in many cases there is little opportunity for a service provider to require significant amendment, which is not our view in the current discussions with the Bourse.

The agreement was requested because our member Approved Participants (APs) believed that the OPC would not consider the APs had done the requisite diligence expected of them given the highly sensitive nature of the information requested, lack of access to Bourse information security policies and results of the Bourse's CICA 5970 review (Auditor's Report on Controls at a Service Organization), and other information relevant to ensuring the ongoing privacy of Personal Information. We appreciate reference to the TMX Employee Code of Conduct, which is supportive and consistent with industry practice, but note that it does not cover all aspects of security, focusing on employee conduct with respect to data only. Furthermore, not only private-sector service providers, but also regulated market entities such as clearing houses, provide the full CICA 5970s, or equivalent, to their users on request.

The CICA 5970 will be replaced as of December 15, 2011 by a new Canadian Standard on Assurance Engagements (CSAE) called Reporting on Controls at a Service Organization (CSAE 3416). CSAE 3416, like CICA 5970, is an auditor-to-auditor report on internal controls intended to be used by auditors if their clients rely on the services of the other party for financial reporting.

We would like to discuss the confidentiality agreement and access to the technology policies of the Bourse for a number of industry experts.

We would like to ask the Regulatory Division to discuss with the Bourse ensuring that any future CICA 5970 or equivalent report include a review of the effectiveness of technology-related and operational controls in the context of the information security necessary for the client Personal Information required by LOPR.

In answer to the question of why IIROC has access to data without having signed a confidentiality agreement, IIROC (and the Regulatory Division) obtain small samples of data or data required for particular enforcement cases – information that does not approach the LOPR request in terms of frequency, quantity or electronic form. We think that this periodic limited access is what was intended by the December 3, 2003 Joint Regulatory Notice on Federal and Provincial Privacy Legislation (Circular 162-03).

As mentioned in our July 18 submission, we request that the Bourse and Division websites transparently hyperlink the Rule to the instrument prescribing details of reporting and that a website-accessible plain-language version of the prescribed reporting will explain what the Personal Information requirements under LOPR are, why the Division requires the data to be collected, used and disclosed, and how it is being stored, shared and disposed of once at the Regulatory Division.

We acknowledge that our requests to enhance security or efficiency are considered by the Regulatory Division to be out of scope at this time, but are still uncomfortable with this as the security issues remain of concern and we believe should be of concern to the Regulatory Division as well (e.g., all passwords for batch processing, as well as individual user logons, appear to be designed not to expire (and this may be true for Regulatory Division employee passwords as well); there is a lack of an AP identifier on the submitted files and may not be a log of AP and Regulatory Division security access; URLs and logon IDs are sent to APs in the same e-mail, etc.).

We hope to include these issues in discussions of future plans for LOPR (see IV. below). Our members would also appreciate receiving as soon as possible the MX LOPR Software License Agreements to ensure they remain in compliance with their internal technology policies.

2.a Position and Account Submission Time Extension

The OPC, in our meeting, referenced the importance of information accuracy and questioned the provision of unreconciled data as mentioned.

We believe that not correcting reported data is a conflict with privacy requirements and that this issue must be resolved between privacy and derivatives/market regulators.

While we recognize the U.S. requires reporting of LOPR files earlier in the day than does the Regulatory Division, we believe that the Regulatory Division requirement of aggregation at the beneficial holder level is more challenging than at the control level – the U.S. basis – and requires more development time. Moreover, many transactions and/or client name and address updates necessary for LOPR reporting are and will continue to be processed overnight in batch form in Canada – to change this system-wide has been examined and found to be extremely costly for a market the size of Canada's.

We would like to discuss the need for a change in the daily reporting deadline from 8:00 a.m. ET on the date following the transaction (T+1) to the end of the business day on T+1, moving to noon on T+1 as the systems and procedures improve the collection and aggregation of the data required by these rule changes.

2.b Aggregation and Completeness Of Data

Our members would like clarity from the Commission de l'accès à l'information (CAI) and OPC on how aggregation is perceived by the privacy regulators.

The necessary information to aggregate properly the relevant data requires the development and population of a full client-focused master file – a large, strategic initiative for most financial institutions and a multi-million-dollar spend for the largest. “Stop-gap” or “offline” measures will result in solutions that are more costly and difficult to maintain over the long run, and not reliable from a data integrity perspective.

The members we have spoken to, who we believe represent the major Bourse participants – those that added their firm’s name to our July 18 letter – do not believe that the aggregation problems are minor or that change is possible easily or cheaply. The rankings we are aware of show the leading market players as ones that have challenges. Specifically:

- While a small number of APs have more systems-friendly ways of aggregating certain information, others have been reviewing option position records firm-wide manually for non-individual accounts, finding out who the beneficial owners are, and then seeing if the beneficial owner has other accounts with positions as the reporting is once a week. This is not a practical approach for at least the larger or mid-size APs when the requirement has moved to daily reporting.
- Accounts are not formally cross-referenced at the time of account-opening. The data may not be added to systems at all where there is no over-arching business reason for this. While personal accounts of an individual would be found on a client reference system, we have yet to learn of any AP that regularly links personal and non-personal accounts this way or are comfortable that what linking there is would meet the standards required for regulatory reporting.
- While some may believe that the last four digits of the SIN and another identifier are interchangeable, systems design is much more complex as there is a hierarchy of approaches to reflect in systems changes, i.e., (1) use last four digits of a SIN; (2) if and only if the last four digits of the SIN are not available or cannot be used for non-tax purposes, then use X for owner ID; (3) if X is not available, use Y, etc. – all of which fields must be identified and populated.

Our member APs are working to make the changes effectively and, for the above reasons, we appreciate having more time to work on implementing this aspect of the reporting requirements. We would like to discuss a target implementation date that will allow for full resolution of these issues and concerns.

II. CLARIFICATIONS

1. Account Ownership

Renaming accounts to significantly shorten names would require client notification and re-papering of accounts, and have a considerable downstream impact on multiple systems at APs – and still not improve matching. We appreciate the Bourse's intention to extend the field size. Members will truncate name fields until the Bourse enhancement to the field size is completed.

2. Account Ownership ID

We appreciate what we understand is the adoption of a risk-based approach with respect to our suggestions regarding joint accounts, investment clubs, etc., that is, requesting an AP to obtain and report additional information where such an account repeatedly exceeds position limits. We also appreciate agreeing that institutional clients may use an 'in concert' number (e.g., in the U.S.) and, as well, we will continue to monitor development of legal entity identifiers (LEIs).

3. Account Aggregation

No additional comment.

4.a LOPR Exemption

No additional comment.

4.b LOPR Delegation to Clearing Broker/Other

It is our understanding that the Regulatory Division's estimates of clearing brokers with reportable positions is understated and, also, that the lack of a single-sign on, with no company header on files, is of broader interest than just clearing brokers: it is of interest to their client introducing brokers that are helping to broaden and deepen the overall market for derivatives.

We would like to reiterate that a single sign-on and single-file transmission for clearing brokers with a firm identifier for each record or section is, we believe, more likely to be accurate for the Bourse, APs and the firms the clearing firms clear for.

With respect to the procedures for obtaining, changing and getting forgotten passwords and user IDs, we would like to request staff birthdates and mother's maiden names, and the use of faxes to transmit this, no longer be a requirement. This is Personal Information and there are equally reasonable alternatives widely in use, such as the name of a childhood best friend, teacher or other question.

Please confirm that our members' staff can identify themselves by less intrusive questions and that any such information already provided will be purged after alternatives are in place.

4.c Omnibus Accounts

This represents a challenge for some of our members.

We hope that we can discuss options for this specialized category.

5. Hedger versus Speculator

For a retail client to trade options, the advisor must be options licensed and the client must sign an options trading agreement where he or she specifies what type of trading they will do (i.e., Level 1, 2, 3, or 4 – levels that do not directly translate into Hedger or Speculator). An account must be coded for options before it can trade options and the AP knows whether the account is low, medium or high risk. However, an account that is 80% medium and 20% high risk will be permitted to speculate or hedge.

For example, someone purchasing calls (i.e., Level 1) might be considered a speculator unless he or she are using the call to protect a short position in the underlying security or other basis, in which case they would be a hedger. Likewise, someone writing covered calls (i.e., Level 2) would probably be considered a 'mild' hedger. But Level 2 accounts are also permitted to do trades in each of the levels below it, so Level 1 or 2 in the case of a Level 2 client. The typical Level 2 client does both types of transactions routinely. In the retail world of options trading, hedger/speculator is not a client-, but rather is a trade-specific attribute and most clients routinely do both types of trades.

As this is the case, we again request the addition of N/A, meaning not available, to the selection list. The Regulatory Division can verify with any AP that regularly uses N/A for non-personal accounts.

6. Snapshot of Positions

No additional comment.

7. LOPR May 2, 2011 Deployment

No additional comment.

8. Readiness of Service Providers

No additional comment.

9. Virtual Private Network (VPN) Connection Availability

Technical Notice 013-011 (June 10, 2011) announced a \$2,400 (plus tax) annual fee for the LOPR GUI option. We appreciate your efforts to defer the charge for at least six months.

We also understand that a second SAIL fee will apply if a firm chooses to send LOPR reporting through a separate connection from the trading connection. Since the speed of trading connectivity is critical to APs and their clients, we hope that you will agree that best practice is not to add any additional traffic to trading lines.

For future reference, we would like to understand how fees are set (recognizing the Regulatory Division is self-financing) and the approval process, as well as discuss the appropriateness of charging anything other than strict cost recovery for either reporting option.

III. Other Issues

Thank you for the explanations in a number of areas.

IV. Project Management

We appreciate the Bourse's willingness to undertake a post mortem after some period of working with LOPR. Cross-industry projects are never straightforward given the varying systems and multiple service providers involved, however, we think more general communication or a self-serve database of issues raised by those responsible for developing changes and solutions would prove useful.

In anticipation of the future changes to LOPR – although many may be on the Regulatory Division side only – we would like to discuss the planned LOPR changes and timing that are already known, and to confirm a process for future communications of refinements in the reporting requirements.

To clarify why we think this is important, a better appreciation by the appropriate parts of AP organizations of what was intended would have enabled us to explain that, whereas it may appear to have made sense to use SAIL given that the SAIL protocol is used for trading and can be fully automated, its use for reporting does not offer the AP the efficiencies that may have been expected, especially if there is a further charge per SAIL line. Development of the SAIL protocol file transmission is measurably more difficult and carries a cost of several hundred thousand dollars per larger AP.

For both GUI and SAIL, the same work is required to extract the data, aggregate it, and format it to the MX file layout, a not insignificant process. After that, all that is necessary in the case of the GUI from a development effort perspective is to install the GUI and

verify that it works. Then an authorized individual signs on to the GUI, selects the file created, checks that the right file is selected and that any manual amendments to the information have been made, and submits it ("pushes the button") to the Bourse (given the nature of the responsibility, we suspect that it is highly unlikely an AP would request a service provider, or a service provider would agree, to submit the file data, e.g., for our western members).

For the SAIL protocol to transmit a file to the Bourse, in contrast, APs must develop a system that mimics the activity of the GUI in establishing connectivity to the MX and then send individual entries across that connection, in the proprietary format used for trading, essentially re-developing what the Bourse developed in providing a GUI and completely specific to the proprietary nature of the SAIL protocol – in other words, of no benefit to other areas of the AP's business.

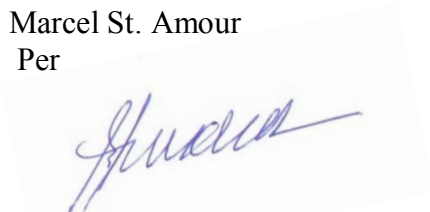
To the extent the goal of LOPR was security, secure FTP is a standard file transfer protocol used extensively in the financial services industry that, for perhaps 10% of the cost, would have allowed APs to provide the data.

We hope that this and other open architecture approaches can be considered in future.

We realize that it is vacation time but hope we will have an opportunity for a teleconference call or meeting in the near future to discuss a number of items. We will call to determine what may be a convenient time for you and would be pleased to answer any questions that you have in the meantime.

Yours sincerely,

Marcel St. Amour
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Cc: Anthony Tamvakologos, Frank Barillo