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CSA Notice

Amendments to National Instrument 24-101 *Institutional Trade Matching and Settlement* and Changes to Companion Policy 24-101CP to National Instrument 24-101 *Institutional Trade Matching and Settlement*

April 27, 2017

Introduction

The Canadian Securities Administrators (the **CSA** or **we**) are adopting amendments to National Instrument 24-101 *Institutional Trade Matching and Settlement* (**Instrument** or **NI**) and changes to Companion Policy 24-101 *Institutional Trade Matching and Settlement* (**Companion Policy** or **CP**) (collectively, the NI and CP are referred to as **NI 24-101**). The amendments to the NI and changes to the CP are referred to collectively in this Notice as the **Revisions**.

Some of the Revisions are being made in anticipation of shortening the standard settlement cycle for equity and long-term debt market trades in Canada from three days after the date of a trade (**T+3**) to two days after the date of a trade (**T+2**). The move to a T+2 settlement cycle is expected to occur on September 5, 2017, at the same time as the markets in the United States are expected to move to a T+2 settlement cycle.

In some jurisdictions, government ministerial approvals are required for the implementation of the amendments to the Instrument. Provided all necessary approvals are obtained, we expect the amendments will come into force, with certain transitional relief, in all CSA jurisdictions on September 5, 2017 (see "**Discussion – 3. Effective date of Revisions and transitional provisions**"). Additional information regarding the adoption of the amendments to the NI in each province or territory is, where applicable, included in Annex G. The text of the amendments to the NI, and text of the changes to the CP, follow after this Notice in Annexes C and D, respectively, and will also be available on websites of CSA jurisdictions, including:

www.lautorite.qc.ca
www.albertasecurities.com
www.bcsc.bc.ca
www.nssc.novascotia.ca
www.fcnb.ca
www.osc.gov.on.ca
www.fcaa.gov.sk.ca
www.mbsecurities.ca

This Notice includes the following Annexes:

- Annex A: list of comment letters
- Annex B: summary of comments on "Proposed Revisions" (defined below) and CSA responses
- Annex C: amendments to the NI (including the Forms)
- Annex D: changes to the CP
- Annex E: blackline version of the NI reflecting the amendments to the NI (including the Forms)
- Annex F: blackline version of the CP reflecting the changes to the CP
- Annex G: local matters (where applicable)

Background

We published for comment on August 18, 2016 for 90 days proposed amendments to the Instrument and changes to the Companion Policy (collectively, the **Proposed Revisions**). As we explained in the *Notice and Request for Comments* (the **Request Notice**),[1] the purposes of the Proposed Revisions were twofold:

- To facilitate the move to a T+2 settlement cycle (while NI 24-101 does not currently expressly mandate a T+3 settlement cycle, nor would prevent the migration to T+2, there are a number of provisions that require revision to facilitate the move to T+2), and

- To update, modernize and clarify certain provisions of NI 24-101.

In addition to seeking comment on the Proposed Revisions, we published at the same time CSA Consultation Paper 24-402 *Policy Considerations for Enhancing Settlement Discipline in a T+2 Settlement Cycle Environment* (**Consultation Paper**).[2] The Consultation Paper sought stakeholder views on the adequacy of today's settlement discipline regime for the Canadian equity and debt markets that are moving to a standard T+2 settlement cycle. The Consultation Paper explored, for regulatory consideration, possible new measures that might enhance settlement discipline and mitigate potential risk of increased settlement fails as the markets move to T+2. Such measures were to be over and above the Proposed Revisions.[3]

We received seven comment letters on both the Proposed Revisions and Consultation Paper. A list of the commenters is attached in Annex A to this Notice. We have considered the comments received, and thank all commenters for their submissions. We provide a summary of the comments on the Proposed Revisions, together with our responses, in Annex B to this Notice.

We briefly discuss some of the key comments and our responses below under "Discussion". CSA staff propose to bring forward for publication later in 2017 a summary of the feedback we received on the Consultation Paper, together with staff's analysis of such feedback (**Feedback Analysis**).

The Revisions being adopted today by the CSA are based solely on the Proposed Revisions. We do not propose to implement at this time any additional measures arising from the Consultation Paper to prepare for the move to T+2 as a result of the feedback received.[4] The Feedback Analysis will provide further details.

Recent developments on investment fund settlement timelines

The CSA has held ongoing discussions with the conventional mutual fund industry regarding the industry's transition to a T+2 settlement cycle. Three industry associations, an industry outsourcing and technology vendor and a clearing agency have been consulted in this regard. These industry stakeholders and service providers have requested that the CSA provide guidance regarding the adoption of a T+2 settlement cycle by conventional mutual funds. The CSA jurisdictions anticipate addressing this in a separate publication.

Discussion

Defined terms or expressions used in this Notice, which are not otherwise defined or given a meaning in this Notice, share the meanings provided in the Request Notice.

This section of the Notice is divided into three parts.

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[1] See CSA Notice and Request for Comments: Proposed Amendments to NI 24-101 *Institutional Trade Matching and Settlement*, Changes to Companion Policy 24-*101 Institutional Trade Matching and Settlement*, and CSA Consultation Paper 24-402 *Policy Considerations for Enhancing Settlement Discipline in a T+2 Settlement Cycle Environment*, August 18, 2016, (2016), 39 OSCB 7225.

[2] See Annex E of Request Notice, at p. 7276.

[3] Such measures were also over and above the changes being made by the industry to the rulebooks, procedures, standard agreements and other documentation of the marketplaces, SROs and clearing agencies to reflect the move to T+2 from T+3. For a discussion of these industry changes, see the Request Notice at p. 7226-7, and Consultation Paper at p. 7280. For example, the Investment Industry Regulatory Organization of Canada (**IIROC**) has proposed amendments to its Universal Market Integrity Rules, Dealer Member Rules, and Form 1 to facilitate the investment industry's move to T+2 settlement. See IIROC Notice 16-0177 *Amendments to facilitate the investment industry's move to T+2*, available at: http://www.osc.gov.on.ca/documents/en/Marketplaces/iiroc_20160728_iiroc-notice-16-0177.pdf.

[4] Almost all commenters say that the existing settlement discipline regime is adequate and largely capable of meeting a T+2 settlement cycle.

- In part 1, we discuss key Revisions that relate to the migration to T+2 settlement. These Revisions do not affect NI 24-101's current institutional trade matching (**ITM**) deadline of noon on T+1, nor its exception reporting ITM threshold of 90 percent.

- In part 2, we discuss key Revisions that clarify or modernize certain provisions of NI 24-101.

- In part 3, we describe the effective date for implementing the Revisions and certain transitional provisions in response to concerns expressed by commenters with implementing the Revisions on September 5, 2017.

1. T+2-related Revisions

(a) References to "T+3"

While the primary focus of the Instrument is on having ITM policies and procedures to match institutional trades no later than noon on T+1, NI 24-101 contains a number of references to T+3. We are removing these references or, where appropriate, replacing them with references to "T+2".

(b) Non-North American trades

We proposed in the Request Notice to repeal the provisions that extend the ITM deadline to noon on T+2 where a DAP/RAP trade results from an order to buy or sell securities received from an institutional investor whose investment decisions or settlement instructions are usually made in and communicated from a geographical region outside the North American region (**non-North American trades**). Most commenters agreed with repealing these provisions. Some commenters noted that a longer deadline could subject market participants, who are waiting for a trade to settle on T+2, to increased risks of a failed trade. Some who commented about removing the extended deadline for matching non-North American trades also indicated that such a change should not be onerous given that it would align Canada with T+2 settlement cycles in other jurisdictions. This includes the T+2 settlement cycle in use today in Europe, Hong Kong, Australia and New Zealand, as well as the T+2 settlement cycle standard proposed for the United States and Mexico as of September 5, 2017.[5]

As a result, we are repealing the provisions of NI 24-101 relating to non-North American trades. These provisions are no longer appropriate in a standard T+2 settlement environment. The extended deadline of noon on T+2 for non-North American trades leaves insufficient time to solve problems and avoid failed trades; instead, parties need to match earlier on T+1 regardless of the cross-border nature of the trade, so that they have time to address issues and avoid failed trades.

2. Revisions to clarify or modernize NI 24-101

(a) Application to ETFs

As noted in the Request Notice, NI 24-101 does not currently apply to a trade in a security of a mutual fund to which National Instrument 81-102 *Investment Funds* (**NI 81-102**) applies. Mutual fund trades were originally carved out of NI 24-101 because traditional purchase and redemption transactions in mutual fund securities were not cleared and settled through the facilities of a clearing agency, such as CDS Clearing and Depository Services Inc. (**CDS**). As exchange traded funds (**ETFs**) are mutual funds and therefore subject to NI 81-102, ETF securities that are bought

[5] Since the publication of our Request Notice in August 2016:

- The U.S. Securities and Exchange Commission (**SEC**) published for comment in September 2016 a release (**SEC Proposed Release**) proposing to amend SEC Rule 15c6-1(a) *Settlement Cycle* under the Securities Exchange Act of 1934 to shorten the standard settlement cycle for most broker-dealer transactions from T+3 to T+2. See SEC Release No. 34-78962; File No. S7-22-16 (RIN 3235-AL86), *Amendment to Securities Transaction Settlement Cycle*; Proposed rule; September 28, 2016; available at: https://www.sec.gov/rules/proposed/2016/34-78962.pdf. The SEC adopted these amendments on March 22, 2017 in a final release (**SEC Final Release**). See SEC Release No. 34-80295; File No. S7–22–16 (RIN 3235–AL86), *Securities Transaction Settlement Cycle*; Final rule; published in Federal Register, March 29, 2017; available at: https://www.gpo.gov/fdsys/pkg/FR-2017-03-29/pdf/2017-06037.pdf. The "compliance date" set out in the SEC Final Release for meeting the new T+2 standard is September 5, 2017.
- Grupo Bolsa Mexicana de Valores (the Mexican Stock Exchange) recently announced that it will change trade settlement dates for many equity products and warrants to T+2 from the current T+3 starting September 5, 2017, subject to the approval and implementation by the U.S. financial services industry of the move to T+2 on such date (according to a Notice from Grupo Bolsa Mexicana de Valores dated February 16, 2017 to "Traders and Head Traders of the Mexican Equity Market", as set forth in a widely distributed email dated February 21, 2017 from the Canadian Capital Markets Association (**CCMA**)).

and sold like any other stock on the secondary markets and settled through the facilities of CDS, are not subject to NI 24-101.

In the Request Notice we expressed the view that a secondary-market trade in an ETF security that settles through the facilities of CDS should be subject to NI 24-101, particularly the trade matching requirements of the Instrument (Parts 3 and 4). Such trades bring the same risks to our markets and the clearing and settlement infrastructure that serves our markets as any other typical trade in equity or fixed-income securities. In addition, non-redeemable investment funds that trade on a marketplace and settle through CDS are currently subject to the Instrument. We are of the view that all investment funds that are traded on a marketplace should be treated in the same way under the Instrument. Some commenters noted that, since NI 24-101 came into force in 2007, the volume of ETF issuers and transactions has increased, but has not posed a challenge in respect of the timely matching of these trades. Commenters also said that ETFs are already included in the ITM matching data published by CDS.

We are narrowing the scope of the current exception for investment funds by amending paragraph (f) of section 2.1 of the NI to clarify that the Instrument does not apply to a purchase governed by Part 9, or a redemption governed by Part 10, of NI 81-102. Part 9 governs purchases of securities of a mutual fund, and Part 10 governs redemptions of investment fund securities. Moreover, the Forms and Companion Policy are being amended to clarify that DAP/RAP trades in ETF securities are to be included in the exception reports under Form 24-101F1 by registered firms as "equity" DAP/RAP trades, and not as "debt" DAP/RAP trades.

(b) Clearing agency definition

In the Request Notice, we expressed our view that the defined term "clearing agency" needed to be updated, given the growing number of, and the broader range of services provided by, clearing agencies operating in Canada since 2007. Accordingly, we have amended the definition as proposed.

(c) MSU systems and business continuity planning requirements

We proposed in the Request Notice to amend section 6.5 of the NI and related CP provisions, which set out systems and business continuity planning requirements for matching service utilities (**MSU**). The purpose of such Proposed Revisions was to align them with similar provisions in other rules applicable to marketplaces, information processors, clearing agencies and trade repositories. However, some commenters expressed concerns with these Proposed Revisions. Among other reasons, one commenter noted that regulators should not impose new obligations on MSUs that are overly onerous, as they could jeopardize the continuity and availability of MSU services to Canadian market participants. One commenter also suggested that a formal "substitute compliance" regime be considered with respect to these requirements in circumstances where an MSU is already complying with analogous requirements of its home regulator in a foreign jurisdiction.

CSA staff will consider further policy work on systems and related requirements applicable to MSUs at a later time. Consequently, we will not proceed at this time with the Proposed Revisions to section 6.5 of the NI and section 4.5 of the CP.

3. Effective date of Revisions and transitional provisions

(a) Effective date of Revisions

As mentioned above, we expect the amendments to the Instrument will come into force on September 5, 2017 in all CSA jurisdictions, subject to obtaining government ministerial approvals in certain CSA jurisdictions. We chose this date so that the Revisions are implemented at the same time as the markets in the United States are expected to transition from a T+3 settlement cycle to a T+2 settlement cycle.[6] The U.S. securities industry has identified September 5, 2017 as the target date for the transition to a T+2 settlement cycle to occur. Similarly, the SEC has determined a "compliance date" of September 5, 2017 for meeting a new T+2 settlement standard for broker-dealer transactions under recently adopted amendments to SEC Rule 15c6-1(a) *Settlement Cycle* enacted under the Securities Exchange Act of 1934.[7] However, while remote, it is possible that this target or compliance date may be extended if certain regulatory and industry contingencies are not achieved on time.[8]

[6] See "Priorities" on the CCMA Website, at: http://ccma-acmc.ca/en/priorities/. See also CSA Staff Notice 24-312 – *Preparing for the Implementation of T+2 Settlement* dated April 2, 2015, available at: http://www.osc.gov.on.ca/en/SecuritiesLaw_sn_20150402_24-312_t2-settlement.htm.
[7] See the SEC Final Release.
[8] See the SEC Proposed Release, at pages 76-77.

As a result, while we have specified September 5, 2017 as the earliest date when the Revisions will become effective, the amending instrument that implements the Revisions contains language that will allow for the effective date to be extended in order to match a delay of the U.S. transition to a T+2 settlement cycle, should the U.S. target-compliance date be extended for whatever reason. In the event that the U.S. compliance date is extended, for transparency purposes the CSA jurisdictions expect to publish a subsequent notice to highlight such a date extension.

(b) Transitional provisions for delivery of Forms 24-101F1, 24-101F2 and 24-101F5 for calendar quarter that includes the effective date

Under section 4.1 of the Instrument, each calendar quarter is a reporting period for the purposes of delivering an exception report in Form 24-101F1. Commenters expressed concerns that, because September 5, 2017 falls within the calendar quarter ending September 30, 2017, registered firms delivering exception reports in Form 24-101F1 for that quarter could potentially be subject to two different sets of reporting requirements in that quarter. Essentially, if the Revisions related to reporting were brought into force on September 5, 2017, firms might report their ITM rates based on two different methodologies: first, using their current methodology for reporting ITM rates for the period from July 1, 2017 to September 4, 2017, and second, using a different methodology for reporting ITM rates for the period from September 5, 2017 to September 30, 2017.

We have considered these comments, and included specific transitional provisions in the instrument amending the NI to address this issue. The transitional provisions also apply to the reporting requirements of clearing agencies and MSUs with respect to Forms 24-101F2 and 24-101F5, respectively. The transitional relief for registered firms relates only to determining whether an exception report is necessary for the calendar quarter and, if it is, the form required for that report. However, September 5, 2017 (or such later date, as discussed above) remains the effective date for having policies and procedures to reflect the amended matching requirements regarding ETFs and non-North American trades. A registered dealer or a registered advisor must establish, maintain, and enforce policies and procedures designed to achieve matching as soon as practical after a DAP/RAP trade for an institutional investor is executed and in any event no later than 12 p.m. (noon) on T+1.

The transitional relief would permit a registered firm to calculate its relevant ITM percentages for determining whether it needs to file an exception report for the calendar quarter during which the Revisions are implemented, and, where applicable, for completing the report, as if the Revisions do not come into force until the beginning of the following calendar quarter. Therefore, if the effective date is September 5, 2017, registered firms would be entitled to continue to use their current methodologies for calculating whether they meet the 90% ITM threshold for the entire calendar quarter ending September 30, 2017. For example, to the extent that a firm currently differentiates between North American DAP/RAP trades and non-North American DAP/RAP trades, or between ETF DAP/RAP trades and other equity DAP/RAP trades, for the purposes of its exception reports, it would not need to change mid-quarter its methodology for completing the report for the calendar quarter ending September 30, 2017.

As revised, section 3.4 of the Companion Policy encourages registered firms to complete their Form 24-101F1 through the NI 24-101 on-line portal on the CSA website.[9] It is important to note that the CSA will not modify the on-line version of Form 24-101F1 to reflect the relevant changes made to the Form in the Revisions until after 45 days following the end of the calendar quarter during which the Revisions are implemented. Therefore, we encourage registered firms to file their on-line exception reports for the calendar quarter during which the Revisions are implemented on the current version of the Form, and not the revised Form.

CSA Staff Notice 24-305

In order to reflect the Revisions, CSA staff plan to update and republish CSA Staff Notice 24-305 *Frequently Asked Questions About National Instrument 24-101 – Institutional Trade Matching and Settlement and Related Companion Policy* later this year.

[9] In Ontario, it is mandatory to file the Form electronically through the on-line portal on the CSA Website. See OSC Rule 11-501 *Electronic Delivery of Documents to the Ontario Securities Commission*.

Questions

Questions with respect to this Notice may be referred to:

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