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BY EMAIL

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WITHOUT PREJUDICE

Dear Sirs/Mesdames:

RE: Comments Concerning Proposed Amendments Respecting the Reasonable Expectation to Settle a Short Sale (the "Proposed Amendments")

We are writing in response to the request for comments on the Proposed Amendments, which were developed in response to the feedback received through the response letters to the Joint CSA/IIROC Staff Notice 23-329 regarding short selling in Canada.

We thank you for the opportunity to provide comments on the Proposed Amendments. Please note that this letter reflects the collective views of certain members of our securities practice rather than the firm as a whole or any of its clients. These comments are provided without prejudice to any stance our firm has taken or may adopt in the future, either independently or on behalf of any client.

Wildeboer Dellelce is one of Canada's premier corporate, securities and business transaction law firms. We are recognized in the Chambers Canada 2024 Guide as Highly Regarded for Corporate/Commercial in Ontario, one of Canada's Best Law Firms for 2024 by The Globe and Mail, and one of the 'Top 10 Corporate Law Boutiques in Canada' by Canadian Lawyer Magazine. In addition, the Canadian legal LEXPERT Directory and Best Lawyers Canada recognize Wildeboer Dellelce lawyers in several areas, including mergers and acquisitions, corporate finance, securities, and technology.

We acknowledge the efforts of the Canadian Investment Regulatory Organization ("CIRO", formerly the Investment Industry Regulatory Organization of Canada or IIROC) in its attempt to refine the regulatory framework for short selling through the Proposed Amendments. While these changes mark a step in the right direction, they may not substantially address pitfalls in the short selling landscape. In the subsequent sections, we outline our perspectives on the limitations of the Proposed Amendments and offer suggestions for more far-reaching reforms in hopes of better aligning the regulatory framework with stakeholder interests.

The Ambiguity of "Reasonable Expectation to Settle"

We wish to highlight the ambiguity of the regulatory language as evidenced by the misinterpretation by a previous commenter, which you acknowledged in Staff Notice 23-332, who misunderstood the language of Staff Notice 22-0130. This instance serves as an example of how such vague language may lead to confusion and underscores the need for clarity to ensure consistent compliance. As such, we urge staff to consider a more prescriptive approach in this regard.

The guidelines in Staff Notice 22-0130 provided guidance on the meaning of "reasonable expectation" by stating that "IIROC expects that prior to the entry of a short sale order, a Participant has *reasonable certainty* [emphasis added] that it can access sufficient securities for it to settle any resulting trade on settlement date."[1]

With regard to the terms "reasonable expectation" and "reasonable certainty" in Staff Notice 23-332 Summary of Comments and Responses to Joint CSA, it states that "[a] commenter viewed this notice as requiring a new higher standard for "reasonable certainty" that a participant can access sufficient securities to settle any resulting trade by settlement date"[2] to which CIRO responded that "[n]o new interpretation was provided in CIRO Notice 22-0130. The guidance only clarified the existing UMIR Policy 2.2 requirement."[3] In this situation, CIRO sought to clarify the requirement of having a "reasonable expectation" to settle trades by equating it with "reasonable certainty." This misinterpretation underscores the vagueness of the language, and, as such, we urge staff to consider a more prescriptive approach.

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[1] IIROC Staff Notice 22-0130 - *Guidance on Participant Obligations to Have Reasonable Expectation to Settle any Trade Resulting from the Entry of a Short Sale Order* (August 2022), online: <Guidance on Participant Obligations to have Reasonable Expectation to Settle any Trade Resulting from the Entry of a Short Sale Order | Canadian Investment Regulatory Organization (ciro.ca)>

[2] CSA/CIRO Staff Notice 23-332 - *Summary of Comments and Responses to CSA/IIROC Staff Notice 23-329 Short Selling in Canada* (November 2023), online: < https://www.ciro.ca/news-room/publications/csaciro-staff-notice-23-332-summary-comments-and-responses-csaiiroc-staff-notice-23-329-short> [The Summary].

[3] *Ibid.*

It is our view that the Proposed Amendments do not sufficiently clarify the existing ambiguities as highlighted above and, at least to some extent, do not eliminate the potential for varied interpretations of the rules.

In response to advocates of pre-borrow requirements, CSA/CIRO Staff Notice 23 – 332 noted that "mandatory pre-borrow requirements may have a more adverse effect on certain types of dealers and their clients, who may not have access to the same pools of securities available to be borrowed as other dealers. This could create an uneven playing field."[4] We are concerned that the ambiguity in the regulatory language may exacerbate inequalities in the competitive landscape. First, it can lead to varied interpretations of what constitutes compliance, with different firms, broker-dealers and short-sellers adopting differing and contrasting standards for what they consider "reasonable certainty" or "reasonable expectation." Secondly, it causes some participants to bear higher compliance costs than others based on their interpretation of the requirements.

Explicit Locate or Pre-Borrow Requirements

By contrast to the ambiguity surrounding the concept of "reasonable expectation," explicit pre-borrow requirements provide a clear and unequivocal standard, thereby enhancing market fairness and integrity.

We have been advised by a number of our clients and we are of the view that the current Universal Market Integrity Rules and the Proposed Amendments are insufficient for ensuring that short sellers verify the availability of securities for settlement before placing orders. As financial markets evolve, our regulatory practices must adapt. Adapting, in this sense, means finding ways to maintain investor protection and confidence and maintain alignment with international standards. Anecdotally, there also appears to be support for a reintroduction of the uptick rule.

The absence of pre-borrow requirements for short selling increases the chances of settlement failures, which could cause disruptions within the industry. This poses a significant systemic risk that could undermine investor confidence. We support the approach of the European Union under Article 12 of the Short Selling Regulations, and more specifically, we strongly endorse Canada's adaptation of the approach taken by the EU. Additionally, we support the exploration of a regulatory framework that investigates the potential benefits of a short sale regime differentiating between junior and senior issuers.

The EU, under Article 12, states a person may only enter into a short sale of a share admitted on a trading venue where one of the following conditions is fulfilled:

(a) The person has borrowed the shares or made similar arrangements;
(b) The person has entered into an arrangement or has an enforceable claim to obtain ownership of the securities; or
(c) The person has an arrangement where a third party confirms the shares have been located.[5]

[4] *Ibid.*
[5] Regulation (EU) No 236/2012.

Canada's standard currently lacks the specificity of the EU standard and allows for a greater degree of subjectivity and uncertainty. In essence, Canada's standards rely on proper judgement calls by participants rather than verifiable arrangements. The strength of the EU's approach lies in its clear-cut and enforceable criteria, which not only reduces the incidence of failed trades but also enhances market integrity and the interests of all market participants.

While we advocate for the adoption of the EU's standards, as outlined above, we acknowledge that a less stringent approach may be preferred, and thus, we endorse the study of research and analysis into the costs and benefits of a short sale regime that differentiates junior and senior issuers.

The CIRO study mentioned in Staff Notice 23-329 showed a stronger link between short sales and trading settlement challenges for junior companies as opposed to senior ones.[6] However, as per Staff Notice 23-332, there was not much support for adopting a regime that differentiates junior and senior issuers.[7] Yet, there is a lack of research into whether differing rules are necessary or how they could be effectively implemented, suggesting the idea should not be so quickly dismissed. Without thorough studies specifically focusing on this differentiation and its potential impacts, it is premature to conclude that a one-size-fits-all approach is the best course of action. We believe that further investigation is crucial in ascertaining if distinct regulations for different types of issuers are necessary and appropriate.

If you wish to discuss this letter further, please contact Geoffrey Cher (gcher@wildlaw.ca), who would be pleased to speak to you at your convenience.

Thank you,
Wildeboer Dellelce

[6] CSA/CIRO Staff Notice 23-329 – *Short Selling in Canada* (December 2022), online: <Joint CSA and IIROC Staff Notice 23-329 - Short Selling in Canada (osc.ca)>
[7] The Summary, *supra* note 2.