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**Shaping STP<sup>SM</sup>**

July 13<sup>th</sup> 2004

To:

British Columbia Securities Commission  
Alberta Securities Commission  
Saskatchewan Financial Services Commission  
Manitoba Securities Commission  
Ontario Securities Commission  
Securities Administration Branch, New Brunswick  
Securities Office, Prince Edward Island  
Nova Scotia Securities Commission  
Securities Commission of Newfoundland and Labrador  
Registrar of Securities, Northwest Territories  
Registrar of Securities, Nunavut  
Registrar of Securities, Yukon Territory

c/o

John Stevenson, Secretary  
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Canada – M5H 3S8

Madame Anne-Marie Beaudoin  
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Dear Sir & Madame

Omgeo LLC (“Omgeo”)<sup>1</sup> is grateful for the opportunity to respond to the CSA Request for Comment on Discussion Paper 24-401 on Straight Through Processing (STP). Omgeo applauds this process as a means of fostering debate and gaining industry consensus.

Omgeo intends to apply to the Canadian authorities to become a Matching Service Utility, subject to the final definition of the terms of such application. This application would be made by Omgeo in order to offer the Omgeo Central Trade Manager<sup>SM</sup> system (“Omgeo CTM”) in the Canadian market. Omgeo CTM is a platform for post-trade processing that will be implemented globally in all markets in which Omgeo operates.

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<sup>1</sup> Omgeo is a joint venture between The Depository Trust & Clearing Corporation and The Thomson Corporation. Omgeo began operations in 2001. It combines in a single business the TradeSuite service formerly operated by The Depository Trust & Clearing Corporation’s subsidiary, The Depository Trust Company, with the post-trade pre-settlement services formerly operated by subsidiaries of The Thomson Corporation. Its wide range of services helps Omgeo’s clients achieve straight through processing of their trades. More information about Omgeo is available on its website, [www.omgeo.com](http://www.omgeo.com)

Omgeo provides critical post-trade processing services in 42 markets globally. Therefore the Request for Comment allows us an opportunity to share with the CSA not only our views on the various questions raised in the Request for Comment, but also some supporting data from the US market that we believe will be useful to the CSA and other interested parties in gaining a better understanding of the issues raised in the Request for Comment.

Our understanding is that STP for the Canadian market is a vital component of an efficient post-trade processing model, which helps to maintain and enhance the competitiveness of the Canadian capital markets. Many other markets have similar issues and we find many common themes, notably:

- The desire to reduce processing costs through greater processing efficiency
- The need to minimize operational, systemic and credit risk
- The need to reduce the rate of trade reclaims and/or trade failures, particularly as transaction volumes grow.
- The need to remain internationally competitive

We will address the questions raised by the CSA in the context of the issues noted above. Before answering the specific questions raised in the Discussion Paper, Omgeo would like to state its views towards this on this subject, starting with the question of the value and need for same day trade affirmation either by central matching or the more traditional confirm/affirm method.

Omgeo supports the process of same day trade confirmation. The term used by Omgeo to denote this process is “SDA” - Same Day Affirmation (SDA) - and we will use this term throughout this letter. SDA is the process of capturing and agreeing on details of a trade between the buyer and seller. It does not, in itself, imply how the process should be performed – either by matching or by confirmation/affirmation. Omgeo believes that SDA is a catalyst for improving post-trade processing efficiency and is one of the necessary steps to enable shorter settlement cycles.

It is important to note that the current market convention, in most markets for trades performed by institutional investors, is to confirm both the block trade details and the allocation details of a trade before the trade is instructed to the settlement agent. A Block Trade is defined as being the details of the trade executed in the market (price, quantity, settlement date, counterparty etc). The Allocation expands the information to include client and settlement data. There may be multiple allocations per Block trade. Therefore, the market trade (“Block”) and the settlement information (“Allocation”) are both confirmed before a settlement instruction is issued to a settlement agent (a custodian or clearing broker). When a trade is instructed to a settlement agent, it is likely to be confirmed again within the settlement system immediately prior to settlement. (This is often referred to as “pre-matching”). Owing to the current, standard, 3 day period between trading and settlement, most market participants believe that there is significant value in performing a trade confirmation as soon as possible after trading, independently of the settlement process. Omgeo supports this delineation and Omgeo’s systems are therefore designed around these principles.

Much of the historical debate in the area of post-trade, processing efficiency and shorter settlement cycles has centered on the desire and need to mandate the use of a central matching utility to facilitate STP. In such instances, the value, which could be realized by the industry from such a fundamental process change, was often overshadowed by the arguments for or against central matching vs. other methods of achieving prompt trade agreement. This tended to obscure the benefits of SDA. For this reason, we at Omgeo believe that a keener focus on SDA will allow us to shift the focus more to the desired outcome, rather than the means by which the outcome is achieved, and in so doing, create a broad consensus on the STP results the industry is trying to achieve. This applies equally to the US and Canadian markets and is also being debated in Europe, where the issues are very similar.

The debate on the best way of achieving SDA can sometimes be confused by terminology problems where different markets use similar terms to mean different processes. As stated above Omgeo uses the term Same Day Affirmation (“SDA”) to identify the generic process of same-day trade confirmation. The term SDA does not imply how the trade is confirmed. SDA can be achieved by a “confirm/affirm” process as currently used in many markets or a central matching process as used in Omgeo CTM (or OASYS-TradeMatch in the US).

Omgeo believes that central matching, where both the broker/dealer and institutional client submit a trade to a central system for comparison, is superior to confirm/affirm. This belief is reinforced by statistics we are able to produce from the US market. The below data is taken from the OASYS-TradeMatch<sup>SM</sup> system in the US market, but we believe the lessons are applicable to other markets.

TABLE 1: March, 2004 TradeSuite Transactions

<b>Affirmation Rate:</b>	<b>Via Current Confirm/Affirm Process</b>	<b>Via Electronic Allocations &amp; Central Matching</b>
<b>T-0</b>	<b>16.5 %</b>	<b>77.8 %</b>
<b>T+2</b>	<b>85.7 %</b>	<b>95.5 %</b>
<b>Failure rate</b>	<b>1 %</b>	<b>0.5 %</b>

Note: "Failure Rate" above refers to the reclaim process within the DTC system by which a receiver of securities returns them to the deliverer.

The findings with regards to this analysis are,

- Centrally matched trades that utilize an electronic allocation process (e.g., OASYS) experience a superior SDA rate than transactions processed via the traditional confirm/affirm method (77.8% vs. 16.5%)
- Similarly, in terms of T+2 affirmation rates, centrally matched transactions that also utilize electronic allocations experience a higher affirmation rate (95.5%) vs. transactions processed via the traditional confirm/affirm method (85.7%).
- The above data also suggests that it is more beneficial to centrally match a trade, as the overall affirmation statistics, and vastly different failure rates result in central matching users experiencing two times fewer trade failures than traditional confirm/affirm trades.

In conclusion we hope the staff of the CSA will agree with our beliefs that SDA is proven to be the most effective way of improving post-trade processing efficiency.

### **Specific CSA Questions**

We will now address the specific questions posed by the CSA staff in its Discussion Paper, focusing on those we believe are particularly relevant to Omgeo.

#### **Q1 – If the CSA were to implement mandatory STP readiness certificates, what should be the subject matter of such certificates?**

As a vendor, it is not appropriate for Omgeo to comment on the use of mandatory sign-off of STP readiness. However, if the CSA were to implement such certificates, it is our view that any statement of readiness should focus on three areas:

- **Real-time system availability:** Can an operations person identify the real-time confirmation status of a trade and apply updates also in real-time?
- **Operations readiness:** Is the operations function organised to allow real-time processing e.g. are there any end-of-day batch processes that prohibit real-time processing?
- **Service level agreements:** Is an SLA in place with counterparties that contain procedures to ensure SDA?

#### **Q2 – Is it important to the competitiveness of the Canadian capital markets to reach STP at the same time as the US? Please provide reasons for your answer. Are there any factors or challenges unique to the Canadian capital markets?**

It is clearly in the interests of all markets to remain competitive. However, there is an unusually close linkage between the US and Canadian markets that is not found in many other locations globally. It would therefore seem appropriate to coordinate any such changes with the appropriate US regulatory bodies.

**Q3 – Should it be one of the CCMA’s tasks to identify the critical path to reach specific STP goals? If so, what steps and goals should be included?**

From our experience in many markets, it is clearly essential, for change to happen that one organization is prepared to lead the industry and take ownership of a project such as this. It is vital that a market uses a single set of regulations and a consistent approach. The issue of which organization in Canada is appropriate is an issue for the Canadian market participants to resolve. However, Omgeo would like to endorse the prior CCMA activities and applaud its progress.

**Q4 – Should the CSA require market participants to match institutional trades on trade date? Would amending rules to require trade matching on T be more effective than the proposed instrument? Is the effective date of July 1<sup>st</sup> 2005 achievable?**

Our experience tells us that for the benefits of STP to be applied equitably across the community a mandate is required. This is because there will always be some participants that will not voluntarily adopt best practices. Relying on best practice recommendations often also produces a state of inertia where participants are waiting for every other participant to move first. The result is that everybody waits and nobody takes a lead.

Implementation and ongoing enforcement of any such SDA regulation must take into account where the Canadian market is today when it comes to affirming trades on trade date and further, how any precipitous change to trade affirmation rules could disrupt the trade settlement process, at least in the short term. With regard to SDA rates, it would seem to make sense for the CSA to consider a “phased approach” to any such regulation. For example, it could be determined by the regulator overseeing this new regulation that the industry should aim for 50% SDA within 12 months of the effective date of this new rule, with a subsequent target of 80% after 24 months. This minimum level of SDA would then continue to ratchet upwards over the next few years until the stated objective of 99% SDA is ultimately achieved.

The best way to achieve SDA in Canada is primarily an issue for the Canadian market participants and we therefore would prefer not to comment on the two methods proposed. We have also stated elsewhere our preference for phased projects with achievable targets. It is clear that moving from an SDA rate below 5% to 99% will involve a considerable amount of effort for the whole market. However, it is essential that a target date be set towards which all participants aspire. It will only become clear if the target date is achievable, once the project work has started and the majority of participants have written their detailed business requirements and scoped the amount of operational and systems work needed.

Omgeo does not wish to comment as to which is the appropriate regulator to enforce any such rule.

**Q5 – Is a close of business definition required? If so, what time should be designated?**

This is primarily a matter for Canadian market participants, but in principle, we believe a close of business definition is required. The current 7.30PM cut-off time would appear to be appropriate but we would stress the importance of having procedures that work within a global market-place and facilitate cross-border trading.

**Q6 – Should the proposed instrument expressly identify and require matching of each trade data element, or is it sufficient for Proposed Instrument to impose a general requirement to match on T and rely on industry best practices and standards to address the details.**

Omgeo believes that the number of industry mandated fields should be kept to a minimum. Omgeo CTM has mandatory and optional fields which allow the investment manager to determine the most appropriate matching model.

**Q7 – Should the CSA rely on the best practices and standards established by the CCMA ITPWG?**

Yes – we have analyzed the CCMA ITPWG best practices and believe they are appropriate for the market. Omgeo has also incorporated the best practices into the design of Omgeo CTM to ensure compliance with the CCMA rules. Our intention is to make Omgeo CTM compliant with the best practices in as many markets as possible. Therefore it is vitally important that regulators co-operate on a cross-border basis to ensure best practice and ease of implementation.

**Q8 – The CSA seek comments on the scope of the Proposed Instrument. Have we captured the appropriate transactions and types of securities that should be governed by requirements to effect trade comparison and matching by the end of T and settlement by the end of T+3? Have we appropriately limited the rule to public secondary market trades?**

Our advice to the CSA would be to, wherever possible, adopt a cautious, phased approach to the target of 99% SDA. Therefore, it is appropriate that the scope at launch be confined to public secondary market trades.

**Q9 – Is the contractual method the most feasible way to ensure that all or substantially all of the buy side of the industry will match their trades by the end of T?**

From our experience over the years in providing electronic allocation, confirmation and central matching solutions to the industry, it is certain that many active and automated firms (be they broker, investment manager or bank) will voluntarily take whatever steps may be necessary to comply with any such new and voluntary industry objective, or code of best practice. However, it is equally evident that some firms will delay implementing any such changes barring a regulatory mandate. And since the overall processing of any firm is as much a function of the efficiency of its trading counter party as it is its own processing efficiency, the weaknesses of the few will tend to negatively impact the overall processing effectiveness of the many. In the end, the efficiencies hoped for across a broad spectrum of the industry will probably not occur without some form of regulatory mandate.

The view of Omgeo is that the decision on how to mandate SDA should be taken by Canadian market participants.

**Q10 – Should an exception to the requirements to match trades on T be allowed when parties are unable to agree to trade details before the end of T and are required as a result to correct the trade elements before matching?**

Yes – there should be no penalty for a mismatch. The rule should be that participants should enter the trade for the purpose of a match on T. A mismatch occurs because the participant has actively tried to enter the trade for affirmation but there is a genuine disagreement between the two sides to the trade. It may not be physically possible to resolve the issue before the end-of-day. This would be particularly true for participants in other time-zones.

**Q11 – Should registrants be required to report all exceptions from matching by the close of business on T? If so, who should receive the report (e.g.: recognized clearing agency, SRO's and or securities regulatory authorities?**

This is an issue for the Canadian market participants to decide. We would seek to discuss this requirement in more detail with the staff of the CSA. Our recommendation would be to receive status reporting on a monthly or quarterly basis.

**Q12 – Is it necessary to mandate the use of a Matching Service Utility in Canada? If so, how would the appropriate centralized trade matching system be identified? Are there institutional investors or investment managers that may not benefit from being forced into an automated centralized trade matching system? Can STP trade matching be achieved without a Matching Service Utility?**

We refer to our response to Question 9.

**Q13 – Should the scope of functions of a Matching Service Utility be broader?**

We suggest that the CSA should focus from a regulatory perspective on the two core functions of a MSU: trade matching and delivery to the depository. These are the fundamental components of an MSU, which will allow for significant improvement in the Canadian post-trade environment. It is very likely that commercial opportunities will lead to MSU providers enhancing their services with additional functionality, but wherever possible this should not fall within the regulatory ambit.

**Q14 – Are the filing and reporting requirements set out in the Proposed Instrument for a matching service utility sufficient, or should a matching service utility be required to be recognized as a clearing agency under provincial securities legislation.**

Trade affirmation is a separate process from clearing - therefore a MSU should not be required to also register as a clearing agency.

**Q15 – Can the Canadian capital markets support more than one matching service utility? If so, what should be the interoperability requirements?**

We at Omgeo plan to take whatever regulatory steps necessary in order to offer our central matching services in Canada. We will do so knowing full well that other service providers may do likewise. Our decision is based on the basic commercial belief that it makes good business sense for Omgeo to have a presence in the Canadian market and that the Canadian market can support multiple matching utilities.

As we see it, the Canadian regulators should focus not so much on the question of allowing multiple matching utilities (for that will be decided by the marketplace), but rather on the regulatory climate necessary for multiple MSU's to operate effectively.

It appears that the CSA's stated intention to have all interested MSU's register as such, is a positive step in this direction. Setting a baseline regulation for interoperability among MSU's would likewise seem to be an appropriate action for the CSA. However, a few words of caution on this last point seem appropriate as well.

Interoperability has proven to be a very simple topic to discuss, but not so simple to implement. Omgeo's previous work in this area showed the project to be both complex and costly. This was evident both in the US with GSTPA a few years back and also in Europe with the ETC Inter Vendor Link in the 1990's. Moreover, this level of complexity (and cost) would only be exacerbated by differing regulatory requirements in each Country that is considering the need to require a level of Interoperability among MSU's. Without a consistent approach vendors such as Omgeo may find it extremely difficult (or impossible) to manage its business in multiple jurisdictions.

Omgeo is subject to certain interoperability requirements in the April 17, 2001 order of the US Securities and Exchange Commission that granted Omgeo an exemption from registration as a clearing agency in the US. We recommend that the CSA coordinate its interoperability requirements with other national regulatory bodies such as the US Securities and Exchange Commission.

**Q16 – Should T+3 be mandated? Should the CSA mandate T+1 when the US moves to T+1?**

Omgeo believes that the most benefit for all market participants can be gained from achieving SDA. Therefore, given the amount of work needed to achieve SDA, it would be premature and possibly detrimental at this time to set a target date for implementation of a shorter settlement cycle. This position would clearly need to be reviewed if the US market announced a definitive decision to move to T+1 settlement, especially if the implementation timetable differed from the policy chosen by the Canadian market.

Questions 16-25 are not applicable to Omgeo and we therefore make no comment on these issues.

**Responses to Proposed Instrument 24-101**

We have analysed the draft National Instrument and in addition to the responses to specific questions listed above we would like to make the following comments.

**Part 1 – Definitions and Interpretation**

The Proposed Instrument does not state conclusively if a confirm/affirm or central matching model is preferred. As stated elsewhere Omgeo proposes to become a MSU using the Omgeo CTM platform. In Omgeo CTM a trade is "matched" when the Block Trade and Allocations that belong to the Block Trade have been centrally matched. We therefore agree with the definitions contained in Part 1 but would seek to have more detailed discussions about the precise method of trade affirmation.

**Part 2 – Application**

We have no comment.

Part 3 – Trade Matching

We have provided our views on Trade Matching in pages 3 and 4 and we have no additional comment to make.

Part 4 – Requirements for a Matching Service Utility

In broad terms we believe that Omgeo as a firm and Omgeo CTM as a system already comply with the majority of the requirements specified or can put such features into production. We have some specific questions about the scope of the requirements, which we will seek to clarify with the staff of the CSA. These questions concern the cost and time periods for compliance with some of the proposals.

Part 5 – Trade Settlement

We have no comment.

Part 6 – Exemption

We have no comment.

Part 7 – Effective Date

We have provided our views on time periods in pages 3 and 4 and we have no additional comment on the extra points raised in this section.

We at Omgeo thank the CSA for this opportunity to respond to your proposals. We would welcome any further discussion the staff of the CSA may wish to have with us.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'A. Bryan', with a stylized flourish extending to the right.

Adam Bryan  
President and CEO