13.1.2 RS Market Integrity Notice – Request for Comments – Provisions Respecting Client Priority

REQUEST FOR COMMENTS

PROVISIONS RESPECTING CLIENT PRIORITY

Summary

On May 24, 2005, the Board of Directors of Market Regulation Services Inc. ("RS") approved amendments to the Rules and Policies under Universal Market Integrity Rules ("UMIR") to require that, subject to certain exceptions, a Participant give priority to a client order over all principal orders and non-client orders that are entered on a marketplace after the receipt of the client order:

- for the same security;
- at the same or better price;
- on the same side of the market; and
- on the same conditions and settlement terms.

Rule-Making Process

RS has been recognized as a self-regulatory organization by the Alberta Securities Commission, British Columbia Securities Commission, Manitoba Securities Commission, Ontario Securities Commission and, in Quebec, by the Autorité des marchés financiers (the "Recognizing Regulators") and, as such, is authorized to be a regulation services provider for the purposes of the National Instrument 21-101 (the "Marketplace Operation Instrument") and National Instrument 23-101.

As a regulation services provider, RS will administer and enforce trading rules for the marketplaces that retain the services of RS. RS has adopted, and the Recognizing Regulators have approved, UMIR as the integrity trading rules that will apply in any marketplace that retains RS as its regulation services provider. Presently, RS has been retained to be the regulation services provider for: the Toronto Stock Exchange ("TSX"), TSX Venture Exchange ("TSX VN") and Canadian Trading and Quotation System, each as a recognized exchange (an "Exchange"); and for Bloomberg Tradebook Canada Company, Liquidnet Canada Inc. and Markets Securities Inc., each as alternative trading system (an "ATS").

The Rules Advisory Committee of RS ("RAC") reviewed the proposed amendments respecting client priority and recommended their adoption by the Board of Directors. RAC is an advisory committee comprised of representatives of each of: the marketplaces for which RS acts as a regulation services provider; Participants; institutional investors and subscribers; and the legal and compliance community.

The amendments to UMIR will be effective upon approval of the changes by the Recognizing Regulators following public notice and comment. Comments on the proposed amendments should be in writing and delivered by **July 11, 2005** to:

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A copy should also be provided to Recognizing Regulators by forwarding a copy to:

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Background to the Proposed Amendments

Rule 5.3 of UMIR presently provides that a Participant need not give priority to a client order over a principal order or non-client order if the allocation has been made by the trading system of a marketplace. This approach is acceptable when all marketplaces utilize the same allocation algorithms. However, if there are multiple marketplaces trading the same securities there is a probability that each of the marketplaces will have variations in the priorities for the allocation of orders in respect of trades executed on the marketplace. With the possible introduction of new allocation algorithms, the interests of a client could be affected intentionally or unintentionally based on the marketplace on which either the client order or the principal order or non-client order is entered.

Presuming that a Participant has implemented a reasonable system of internal policies and procedures to ensure compliance with the client priority rule and to prevent misuse of information about client orders, nonetheless the Participant under the current version of Rule 5.3 may not rely on the allocation provided by the trading system of a marketplace if:

- any of the client order, principal order or non-client order has executed on a market other than on a marketplace (e.g. a foreign stock exchange or an organized regulated market outside of Canada);
- the client order was not immediately entered upon receipt; or
- the client order was subsequently changed or cancelled by the Participant (e.g. by the trader in response to market conditions in an attempt to get "best execution" for the client) other than on the instruction of the client.

The proposed amendments address the practical problems associated with the inability of a Participant being in a position to rely on the "trading system exemption" by tying client priority directly to the time of receipt of the client order.

Summary of the Impact of the Proposed Amendments

The following is a summary of the most significant differences between the client priority requirements under the proposed amendments as compared to the existing provisions of Rule 5.3 and Policy 5.3. Under the proposed amendments:

- a Participant would provide priority for a client order over a principal order or non-client order only if the client order is received prior to the entry of the principal order or non-client order and the client order is at the same or "better" price and is subject to the same conditions and settlement terms as the principal order or non-client order;
- the provisions would clarify that a trade permitted by the client priority rule would nonetheless be subject to any restrictions imposed by Rule 4.1 dealing with frontrunning;
- a principal order or non-client order would be exempted from the client priority requirement if the principal order or non-client order is:
    - o automatically generated by the trading system of an exchange or quotation and trade reporting system pursuant to market making obligations, or
    - o a Basis Order;
- a client would be deemed to have consented to the principal order or non-client order trading in priority if the client has instructed that their order is to be executed in part at various times during the trading day or at various prices during the trading day;

- a client may provide a "conditional consent" to the principal order or non-client order trading in priority which would require the Participant to "give up" all or part of its fills to the client order if the client's condition is not satisfied;

- if the security trades on more than one marketplace, the Participant would not be able to rely on an allocation made by the trading system of a marketplace unless the principal order or non-client order is a Call Market Order, an Opening Order, a Market-on-Close Order or a Volume-Weighted Average Price Order; and

- a principal order or non-client order could trade in priority to a client order if a Market Integrity Official requires or permits the trade.

Summary of the Proposed Amendments

The following is a summary of the provisions of the amendments to Rule 5.3 and Policy 5.3:

Same Conditions and Settlement Terms

Rule 5.3 currently provides that a Participant must provide priority to its client orders:

- for the same security;

- at the same or better price; and

- on the same side of the market.

The amendments propose that the requirements be varied such that priority would be provided only if the client order was on the same conditions and settlement terms as the principal or non-client order. The amendments recognize that unless the conditions and settlement terms are the same, the principal order or non-client order has not effectively taken away a trading opportunity from the client.

In order to prevent abuse, the Policy would specifically state that it would be unacceptable for a Participant to:

- add terms or conditions to a client order (other than on the instructions of the client) so that the client order ranks behind principal or non-client orders at that price; and

- put terms or conditions on a principal or non-client order for the purpose of differentiating the principal or non-client order from a client order that would otherwise have priority at that price.

Anonymous Orders

A Participant does not have to provide priority for a client order that has been entered directly by the client of the Participant on a marketplace that does not require the disclosure of the identifier of the Participant in a consolidated market display and the person who enters the principal order or non-client order has no knowledge that the "anonymous" order is from a client of the Participant until the execution of the client order.

With the introduction of "attribution choice" on the TSX in March of 2002, an intentional cross with an unattributed order on both the buy and sell side was exempt from interference. To the extent that a principal order or non-client order may be entered without the disclosure of the relevant identifier of the Participant, it may be possible for a principal account or non-client account to obtain an execution in priority to a previously entered client order where the identifier of the Participant has been disclosed on the entry of the client order. Under the current client priority rule, the Participant may not have to reallocate any fill obtained by the "unattributed" principal or non-client order to the previously entered client order as the allocation had been made by a trading system of a marketplace. However, RS has taken the position as set out in Market Integrity Notice 2003-024 dated October 31, 2003 that a Participant would be expected to provide priority to any "disclosed" client order. If the proposed amendments are approved, this position would be incorporated directly into the Policies and a Participant would be under an obligation to provide priority to any previous client order on the same terms.

Exemptions for Trades Pursuant to Market Maker Obligations

Presently, the requirement to provide priority to a client order has been interpreted not to apply in the event the principal order or non-client order has been automatically generated by the trading system of a marketplace in order to fulfil Market Maker Obligations imposed by that marketplace on the Participant or employee of the Participant in accordance with the applicable Marketplace Rules. In executing these trades, the market maker is not attempting to bypass client orders but to meet its obligations as a market maker. The amendments propose to incorporate this interpretation into the language of the rule.

Exemptions for a "Basis Order"

Effective April 8, 2005, UMIR was amended to provide recognition to a "Basis Order". A Basis Order will be subject to a number of conditions including that the price of the resulting trade is determined in a manner acceptable to a Market Regulator based on the price achieved through the execution on that trading day of one or more transactions in a derivative instrument that is listed on a recognized exchange or quoted on a recognized quotation and trade reporting system. Under these circumstances, a Participant that executes a principal order as a Basis Order is not attempting to bypass client orders at the same or a better price but merely completing a trade at a price which is determined by derivative transactions. The proposed amendments to the client priority rule provide an exemption for a principal order entered as a Basis Order.

Reliance on Trading System Allocation

The current Rule 5.3 allows a Participant to rely on trading allocations made by a trading system of a marketplace provided:

- the client order was entered on a marketplace immediately upon receipt;
- the client order was not varied except on the instruction of the client; and
- the Participant has a reasonable system of internal policies and procedures to prevent misuse of information about client orders.

This provision was based on a previous requirement of the TSX which had adopted "time priority" as the basis for trade allocations. However, if there are multiple marketplaces trading the same securities and each marketplace has distinct allocation algorithms, the interests of a client could be affected intentionally or unintentionally based on the marketplace on which either the client order or the principal order or non-client order is entered. The amendments propose that a Participant will only be able to rely on the trading system exemption if:

- the security which is the subject of the orders trades on a single marketplace; or
- the principal order or non-client is a Call Market Order, an Opening Order, a Market-on-Close Order or a Volume-Weighted Average Price Order.

The exception for the Call Market Order, an Opening Order, a Market-on-Close Order or a Volume-Weighted Average Price Order recognizes that the price at which these orders will execute is generally not known at the time of the entry of the order. Provided the client order has been entered on receipt and not varied without the consent of the client, any allocation by the trading system of the marketplace for these "specialty orders" is not an attempt to bypass client orders.

Client Consent

Specific Consent

A Participant does not have to provide priority to a client order if the client specifically consents to the Participant trading alongside or ahead of the client. The consent of the client must be specific to a particular order and details of the agreement with the client must be noted on the order ticket. A client cannot give a blanket form of consent to permit the Participant to trade alongside or ahead of any future orders the client may give the Participant.

If the client order is part of a pre-arranged trade that is to be completed at a price below the best bid price or above the best ask price as indicated on a consolidated market display, the Participant will be under an obligation to ensure that "better-priced" orders on a marketplace are filled prior to the execution of the client order. Prior to executing the client order, the Participant must ensure that the client is aware of the better-priced orders and has consented to the Participant executing as against them in priority to the client. The consent of the client must be noted on the order ticket.

Deemed Consent

Under the proposed amendments, a client would be deemed to have consented to the principal order or non-client order trading in priority if the client has instructed that their order is to be executed in part at various times during the trading day or at various prices during the trading day. Unless the client has provided standing written instructions that all orders are to be executed at various times during the trading day or a various prices during the trading day, the client instructions should be treated as specific to a particular order and the details of the instructions by the client must be noted on the order ticket. This amendment would incorporate the existing administrative interpretation provided by RS with respect to client consent.

Conditional Consent

Under the proposed amendments to the Policies, a client may provide a "conditional consent" to the principal order or non-client order trading in priority which would require the Participant to "give up" all or part of its fills to the client order if the client's condition is not satisfied. For example, a client may consent to a principal order of Participant sharing fills with the client order provided the client order is fully executed by the end of the trading day. If the client's order is not fully executed, the client may expect that the Participant "give up" its fills to the extent necessary to complete the client order. In this situation, the Participant should mark its orders as "principal" throughout the day. Any part of the execution which is given up to the client should not be re-crossed on a marketplace but should simply be journalled to the client (since the condition of the consent has not been met, the fills in question could be viewed as properly belonging to the client rather than the principal order). To the extent that a Participant "gives up" part of a fill of a principal order to a client based on the conditional consent, the Participant shall report the particulars of the "give up" to the Market Regulator not later than the opening of trading on marketplaces on the next trading day.

The conditional consent of the client must be specific to a particular order. The details of the agreement with the client must be noted on the order ticket.

Application of the Frontrunning Rule

The amendments would clarify that a trade that is permitted by Rule 5.3 dealing with client priority would nonetheless be subject to any restriction imposed by Rule 4.1 dealing with frontrunning. In particular, if a Participant has knowledge of a client order that has not been entered on a marketplace that could, on entry on a marketplace, reasonably be expected to affect the market price of the security, the Participant would be precluded from:

- entering a principal or non-client order with respect to that security or a related security;
- soliciting an order from any other person for the purchase or sale of that security or any related security; or
- informing any other person, other than in the necessary course of business, of the client order.

If that part of a client order that has not been entered on a marketplace could "reasonably be expected to affect the market price of the security", the frontrunning rule would preclude the entry of a principal or non-client order even if the client had given consent for the Participant to trade alongside or ahead of the client order for the purposes of the client priority rule. A Participant must determine the extent to which a client order, including a limit order, that is to be entered in part at various times during the trading day (e.g. an "over-the-day" order) or at various prices throughout the day (e.g. to approximate a volume-weighted average price) would, upon entry on a marketplace, reasonably be expected to affect the market price of the security. If the client has provided specific consent, deemed consent or conditional consent to the Participant trading alongside or ahead of the client order that could reasonably be expected to affect the market price of the security, a Participant would be able to rely on the exemptions from the frontrunning rule that would permit the entry of a principal or non-client order if:

- no director, officer, partner, employee or agent of the Participant who made or participated in making the decision to enter a principal order or non-client order or to solicit an order had actual knowledge of the client order;
- an order is entered or trade made for the benefit of the client for whose account the order is to be made;
- an order is solicited to facilitate the trade of the client order;
- a principal order is entered to hedge a position that the Participant had assumed or agreed to assume before having actual knowledge of the client order provided the hedge is:
    - commensurate with the risk assumed by the Participant, and
    - entered into in accordance with the ordinary practice of the Participant when assuming or agreeing to assume a position in the security;
- a principal order is made to fulfil a legally binding obligation entered into by the Participant before having actual knowledge of the client order; or
- the order is entered for an arbitrage account.

Client Priority in the United States

In the United States, client priority rules are made by each marketplace. Generally, marketplace rules prohibit a dealer from entering an order where the dealer has knowledge of an unexecuted customer order at same price.

New York Stock Exchange

The New York Stock Exchange ("NYSE") prohibits a member from entering an order for a NYSE-listed security for an account in which the member is directly or indirectly interested, if the person responsible for the entry of the order has knowledge of a particular unexecuted customer order on the same side of the market which could be executed at the same price.

The rule does allow members to "trade along" with customer orders under specified conditions, such as when the customer has given express permission for the member or member organization to do so. The express permission of the customer must be obtained on an order-by-order basis and it must include an understanding by the customer of the relative price and size of the allocated execution.

The rule also makes exceptions for special types of orders. For example, a member organization may enter proprietary limit-on-close orders with the same limit price as its customer limit-on-close orders, however, if the member organization order executes and any customer order does not, the member organization is required to give up its execution to the customer. There is no restriction on proprietary market-on-close orders, as all NYSE market-on-close orders must be executed and receive the same closing price.

NASDAQ

NASD Rules prohibit a member from personally buying or selling an exchange-listed security for its own account while such member holds an unexecuted market order to buy or sell such security for a customer. NASD Rules also prohibit members from trading ahead of their customer limit orders in exchange-listed securities traded over-the-counter.

NASD Policy IM-2110-2 (referred to as the Manning Rule) currently generally prohibits members from trading for their own account at prices that would satisfy a customer's limit order unless the member immediately thereafter executes the customer limit order. In 2004, NASD proposed amendments to the Manning Rule which will prohibit a member from trading for its own account in a Nasdaq or exchange-listed security at a price that is better than an unexecuted customer limit order in that security unless the member immediately thereafter executed the customer limit order at the price at which it traded for its own account or better. In other words, under the amendments, where a member trades at a price better than an unexecuted customer limit order, the member will be required to pass along such price improvement to the unexecuted customer limit order. The proposed amendments will also apply the Manning Rule to exchange-listed securities.

In 2004, NASD also proposed to introduce a rule which will prohibit members from trading ahead of customer market orders. With this proposal, NASD would apply the same principles underlying the Manning Rule to the treatment of customer market orders. Under the proposed rule, a member will be prohibited from trading for its proprietary account in a Nasdaq or exchange-listed security if the member has not executed a customer market order in that security unless it immediately thereafter executes the customer market order up to the size and at the same or better price at which it traded for its own account.

The changes proposed by NASD in 2004 would exclude certain activities. For example, members may negotiate specific terms and conditions applicable to the acceptance of an order with respect to an order for customer accounts that are "institutional accounts" or an order that is for 10,000 shares or more unless the order is less than $100,000 in value. Under the proposed changes to the Manning Rule, members may not trade ahead of their customer limit orders in their market-making capacity even if the member had in the past fully disclosed the practice to its customers prior to accepting limit orders.

Strategic Review of UMIR / Regulatory Review of Frontrunning and Client Priority Issues

By Market Integrity Notice 2004-026 issued on October 4, 2004, RS sought input from the public, including market participants, buy-side firms and their advisors, in connection with a number of strategic issues related to UMIR. One of the topics which is included in the strategic review are various aspects of client priority. The outcome of the strategic review may result in additional amendments being proposed related to client priority. During 2004, RS conducted a detailed trading review of the handling of large block orders in the Canadian equity markets to assess whether there is a previously undetected problem of systematic frontrunning or issues related to client priority. The report related to that review was issued by RS on March 31, 2005. Additional analysis of the recommendations of that report also may result in additional amendments to the rules governing client priority. Additional comments therefore are welcome on aspects of client priority that are not otherwise addressed by the amendments currently being proposed.

Appendix

The text of the amendments to the Rules and Policies respecting client priority is set out in Appendix "A".

Questions

Questions concerning this notice may be directed to:

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ROSEMARY CHAN,
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Appendix "A"

Universal Market Integrity Rules

Amendments Related to Client Priority

The Universal Market Integrity Rules are amended by repealing Rule 5.3 and substituting the following:

5.3 Client Priority

(1) A Participant shall give priority to a client order of the Participant over all principal orders and non-client orders of the Participant that are entered on a marketplace or an organized regulated market after the receipt of the client order for the same security that is:

(a) at the same price or a higher price in the case of a purchase or a lower price in the case of a sale;

(b) on the same side of the market; and

(c) on the same conditions and settlement terms.

(2) Despite subsection (1) but subject to Rule 4.1, a Participant is not required to give priority to a client order if:

(a) the client specifically has consented to the Participant entering principal orders and non-client orders for the same security at the same price on the same side of the market on the same settlement terms;

(b) the client order has not been entered on a marketplace as a result of:

(i) the client specifically instructing the Participant to deal otherwise with the particular order,

(ii) the client specifically granting discretion to the Participant with respect to entry of the order, or

(iii) the Participant determining in accordance with Rule 6.3(1)(e) that, based on market conditions, entering the order would not be in the best interests of the client,

and no director, officer, partner, employee or agent of the Participant with knowledge that the client order has not been entered on a marketplace enters a principal order or a non-client order for the same security on the same side of the market on the same conditions and settlement terms;

(c) the principal order or non-client order is:

(i) automatically generated by the trading system of an Exchange or QTRS in accordance with the Marketplace Rules in respect of the applicable Market Maker Obligations, or

(ii) a Basis Order;

(d) the client order has been entered directly by the client of the Participant on a marketplace that does not require the disclosure of the identifier of the Participant in a consolidated market display and the director, officer, partner, employee or agent of the Participant who enters a principal order or a non-client order does not have knowledge that the client order is from a client of the Participant until the execution of the client order;

(e) the principal order or non-client order is executed pursuant to an allocation by the trading system of a marketplace and:

(i) either:

(A) the security which is the subject of the order trades on no marketplace other than that marketplace, or

(B) the principal order or non-client order is a Call Market Order, an Opening Order, a Market-on-Close Order or a Volume-Weighted Average Price Order,

(ii) the client order was entered by the Participant on that marketplace immediately upon receipt by the Participant, and

(iii) if the client order was varied or changed by the Participant at any time after entry, the variation or change was on the specific instructions of the client; or

(f) a Market Integrity Official requires or permits the principal order or non-client order to be executed in priority to a client order.

(3) For the purposes of clause (2)(a), a client shall be deemed to have consented to the Participant entering principal orders and non-client orders for the same security at the same price on the same side of the market on the same conditions and settlement terms if the client order, in accordance with the specific instructions of the client, is to be executed in part at various times during the trading day or at various prices during the trading day.

The Policies under the Universal Market Integrity Rules are amended by repealing Policy 5.3 and substituting the following:

POLICY 5.3 – CLIENT PRIORITY

Part 1 – Background

Rule 5.3 restricts a Participant and its employees from trading in the same securities as a client of the Participant. The restriction is designed to minimize the conflict of interest that occurs when a Participant or its employee compete with the firm's clients for execution of orders. The Rule governs:

- *trading ahead* of a client order, which is taking out a bid or offering that the client could have obtained had the client order been entered first. By trading ahead, the pro order obtains a better price at the expense of the client order.

- *trading along* with a client, or competing for fills at the same price.

The application of the rule can be quite complex given the diversity of professional trading operations in many firms, which can include such activities as block facilitation, market making, derivative and arbitrage trading. In addition, firms may withhold particular client orders in order to obtain for the client a better execution than the client would have received if the order had been entered directly on a marketplace. Each firm must analyze its own operations, identify risk areas and adopt compliance procedures tailored to its particular situation.

A Participant has overriding agency responsibilities to its clients and cannot use technical compliance with the rule to establish fulfillment of its obligations if the Participant has not otherwise acted reasonably and diligently to obtain best execution of its client orders.

Part 2 – Prohibition on Intentional Trading Ahead

Rule 5.3 provides that a Participant must give priority of the execution to client orders over all principal orders and non-client orders of the Participant that are entered on a marketplace or an organized regulated market after the receipt of the client order for the same security at the same price on the same side of the market on the same conditions and settlement terms. The requirement is subject to certain exceptions necessary to ensure overall efficiency of order handling.

In particular, exceptions to the client priority rule are provided if the principal order or non-client order that is entered after the receipt of the client order is:

- automatically generated by the trading system of an Exchange or QTRS in accordance with the Market Maker Obligations of that marketplace;

- a Basis Order; or
- required or permitted to be executed by a Market Integrity Official in priority to the client order.

A principal order which is automatically generated by the trading system of an Exchange or QTRS in accordance with that marketplace's rules on market-making activities is not an intentional attempt by a Participant to trade ahead of or along with a client order. An exemption from the client priority rule is therefore provided in order to ensure overall market liquidity in accordance with established Market Making Obligations.

A Basis Order is undertaken at a price that is determined by prices achieved in related trades made in the derivatives markets. As such, the execution of a Basis Order is not an intentional attempt by a Participant to trade ahead of or along with a client order.

An exception to the client priority rule is also provided where the trading system of a marketplace allocates the fill to a principal order or non-client order. In order to be able to rely on this exception the following three conditions must be met:

- either:
    - the security does not trade on any marketplace other than the one on which the client order and the principal order or non-client order is entered, or
    - the principal order or non-client order is a Call Market Order, an Opening Order, a Market-on-Close Order or a Volume-Weighted Average Price Order;
- the client order was entered immediately upon receipt by the Participant; and
- after entry, the client is not varied or changed except on the specific instructions of the client.

The exception that is provided for a principal or non-client order which is a Call Market Order, Opening Order, Market-on Close Order or a Volume-Weighted Average Price Order recognizes that the price at which such an order may execute will not generally be known at the time the principal or non-client order is entered on a marketplace. Provided the client order has been entered on receipt and not varied without the consent of the client, any allocation by the trading system of the marketplace for these particular types of orders is not an attempt to bypass client orders.

A Participant can never intentionally trade ahead of a client market or tradeable limit order received prior to the entry of the principal order or non-client order without the specific consent of the client. Examples of "intentional trades" include, but are not limited to:

- withholding a client order from entry on a marketplace (or removing an order already entered on a marketplace) to permit the entry of a competing principal or non-client order ahead of the client order;
- entering a client order in a relatively illiquid market and entering a principal or non-client order in a more liquid marketplace where the principal or non-client order is likely to obtain faster execution;
- adding terms or conditions to a client order (other than on the instructions of the client) so that the client order ranks behind principal or non-client orders at that price;
- putting terms or conditions on a principal or non-client order for the purpose of differentiating the principal or non-client order from a client order that would otherwise have priority at that price; and
- entering a principal order or non-client order as an "anonymous order" (without the identifier of the Participant) which results in an execution in priority to a previously entered client order where the identifier of the Participant has been disclosed on the entry of the client order.

Part 3 – No Knowledge of Client Order

Rule 5.3 also contains four exceptions to client priority that require the director, officer, partner, employee or agent of the Participant who enters the principal order or the non-client order to be unaware that the client order has not been entered. The exceptions are:

- the client specifically instructs the Participant to withhold entry of the order;

- the client specifically grants discretion to the Participant with respect to the entry of the order;
- the Participant withholds the client order from entry in accordance with Rule 6.3 in a *bona fide* attempt to get better execution for the client; and
- the client enters the order directly on a marketplace that does not require the disclosure of the identifier of the Participant in a consolidated market display.

In these circumstances, the Participant must have reasonable procedures in place to ensure that information concerning client orders is not used improperly within the firm. These procedures will vary from firm to firm and no one procedure will work for all firms. If a firm does not have reasonable procedures in place, it cannot rely on the exceptions. Reference should be made to Policy 7.1 – Policy on Trading Supervision Obligations, and in particular Part 4 – Specific Procedures Respecting Client Priority and Best Execution.

If a client has instructed a Participant to withhold an order or has granted a Participant discretion with respect to the entry of an order, details of the instruction or grant of discretion must be retained for a period of seven years from the date of the instruction or grant of discretion and, for the first two years, the consent must be kept in a readily accessible location.

Part 4 – Client Consent

A Participant does not have to provide priority to a client order if the client specifically consents to the Participant trading alongside or ahead of the client. The consent of the client must be specific to a particular order and details of the agreement with the client must be noted on the order ticket. A client cannot give a blanket form of consent to permit the Participant to trade alongside or ahead of any future orders the client may give the Participant.

If the client order is part of a pre-arranged trade that is to be completed at a price below the best bid price or above the best ask price as indicated on a consolidated market display, the Participant will be under an obligation to ensure that "better-priced" orders on a marketplace are filled prior to the execution of the client order. Prior to executing the client order, the Participant must ensure that the client is aware of the better-priced orders and has consented to the Participant executing as against them in priority to the client order. The consent of the client must be noted on the order ticket.

If the client has given the Participant an order that is to be executed at various times during a trading day (e.g. an "over-the-day" order) or at various prices (e.g. at various prices in order to approximate a volume-weighted average price), the client is deemed to have consented to the entry of principal and non-client orders that may trade ahead of the balance of the client order. Unless the client has provided standing written instructions that all orders are to be executed at various times during the trading day or a various prices during the trading day, the client instructions should be treated as specific to a particular order and the details of the instructions by the client must be noted on the order ticket. However, if the un-entered portion of the client order would reasonably be expected to affect the market price of the security, the Participant may be precluded from entering principal or non-client orders as a result of the application of the frontrunning rule.

In certain circumstances, a client may provide a conditional consent for the Participant to trade alongside or ahead of the client order. For example, a client may consent to a principal order of Participant sharing fills with the client order provided the client order is fully executed by the end of the trading day. If the client's order is not fully executed, the client may expect that the Participant "give up" its fills to the extent necessary to complete the client order. In this situation, the Participant should mark its orders as "principal" throughout the day. Any part of the execution which is given up to the client should not be re-crossed on a marketplace but should simply be journalled to the client (since the condition of the consent has not been met, the fills in question could be viewed as properly belonging to the client rather than the principal order). To the extent that a Participant "gives up" part of a fill of a principal order to a client based on the conditional consent, the Participant shall report the particulars of the "give up" to the Market Regulator not later than the opening of trading on marketplaces on the next trading day. The conditional consent of the client must be specific to a particular order. The details of the agreement with the client must be noted on the order ticket.