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John Stevenson, Secretary  
Manager, Market Regulation  
Capital Markets Branch  
Ontario Securities Commission  
Suite 190, Box 55,  
20 Queen Street West  
Toronto, ON  
M5H 3S8  
e-mail: [jstevenson@osc.gov.on.ca](mailto:jstevenson@osc.gov.on.ca)

Autorité des marchés financiers (Québec):  
Madame Anne-Marie Beaudoin  
Directrice du secrétariat  
Autorité des marchés financiers  
800, square Victoria, 22e étage  
C.P. 246, tour de la Bourse  
Montréal, Québec H4Z 1G3  
e-mail: [consultation-en-cours@lautorite.qc.ca](mailto:consultation-en-cours@lautorite.qc.ca)

James E. Twiss,  
Chief Policy Counsel,  
Market Policy and General Counsel's Office,  
Market Regulation Services Inc.  
Suite 900,  
145 King Street West  
Toronto, ON  
M5H 1J8  
e-mail: [james.twiss@rs.ca](mailto:james.twiss@rs.ca)

**Re: Market Integrity Notice No. 2007-007  
Joint Canadian Securities Administrators / Market Regulation Services Inc.  
Notice on Trade-Through Protection, Best Execution and Access to Marketplaces**

BMO Capital Markets (BMO) is grateful for the opportunity to provide comments on the joint Canadian Securities Administrators and Market Regulation Services Inc.'s notice and request for comments on trade-through protection, best execution and access to marketplaces.

We would make the following general comments related to these issues:

- BMO supports the regulatory view that responsibility for trade-through protection should lie with marketplaces and that equity market structures should be integrated. Not only would this streamline the domestic marketplace, but it would also foster competitiveness with other global marketplaces.
- We believe the Canadian marketplace has evolved to the point where it can support a centralized data consolidator and market integrator which would enhance effective delivery of best execution, trade-through protection and monitoring. If a centralized data consolidator is implemented, then BMO is supportive of trade-through protection to all levels of displayed market data for transparent markets.

- Regulators should not introduce obligations to access a new marketplace until that marketplace has proved to be operationally sound and stable and has a demonstrated track record of order and trade activity. We believe that 6-12 twelve months is a realistic time frame. As part of BMO's Policies and Procedures with Respect to Multiple Marketplaces, criteria have been established for marketplace access which requires that security controls be in place a tested disaster recovery site, multiple, repeatable and successful Saturday testing dates to conduct connectivity, fail over and recovery, and performance testing.
- BMO believes that trade-through protection should not be applied to any special terms orders.
- Best execution and trade-through obligations should be applied equally to broker-dealers and clients, whether domestic or foreign.
- BMO does not support a regulatory cost-benefit analysis (CBA) on trade-through protection at this time. TREATS should be implemented first so dealers are able to leverage the development of systems to collect, store and report data. Introducing new and separate data collection and reporting requirements would be expensive and duplicative.
- Multiple marketplaces should be in operation for at least a year to determine the nature and frequency of trade-through issues. Since there is international attention on best execution and trade-through protection, BMO believes that business drivers will ensure the most efficient marketplace operation. It would be beneficial if the regulators focus on providing principles-based guidance on best execution rather than prescriptive rules. Prescriptive rules should be introduced based on empirical data rather than anticipated problems.
- Clients (DMA or other) should be subject to the same rules as broker-dealers under UMIR to ensure a level playing field.
- BMO is not supportive of a new class of member that accesses marketplaces directly given the increased reputation, financial and regulatory risk to the industry.
- Marketplaces must be responsible for ensuring accessibility on a consistent and reliable basis prior to launch involving the dealers, the marketplaces and the vendors. Since the Canadian marketplace relies on third party vendor technology for access to marketplaces and post trade processing, coordinated and successful industry-wide testing is a critical success factor to the introduction of new marketplaces in Canada.

#### A. Trade-through Protection

**Question 1:** *In addition to imposing a general obligation on marketplaces to establish, maintain and enforce written policies and procedures to prevent trade-throughs, would it also be necessary to place an obligation on marketplace participants to address trade execution on a foreign market?*

- BMO is not supportive of placing an obligation on participants to address trade-through protection when executing orders on a foreign market. Given the various factors to consider when assessing best execution, dealers are in the best position to determine the appropriateness of accessing foreign markets based on clients' instructions.
- Along with the increased trading and settlement risk of splitting orders among various domestic and foreign markets, the cost to monitor trading opportunities and subsequent compliance review would be onerous with little benefit accruing to the client.
- It is also our understanding that Canada would be the only jurisdiction to mandate such an obligation.

**Question 2: *What factors should we consider in developing our cost-benefit analysis for the trade-through proposal?***

- BMO is not supportive of developing a cost-benefit analysis (CBA) on trade-through at this time. Although the regulators recognize that there will be a cost impact on some marketplace participants, it is premature to conduct a CBA to assess potential impact. BMO recommends that multiple marketplaces operate for at least a year, at which point, the feasibility of a CBA could be re-assessed.
- Although dealers retain trading information to support record of orders requirements, there is a cost difference between data acquisition/packaging and reporting and analysis.
- Given the similarities in the data proposed for marketplace quality statistics and that of TREATS, it is recommended that TREATS be implemented for equities first before introducing any additional obligations.

**Question 3: *Would you like to participate in the cost-benefit analysis by providing your input?***

- As noted above, BMO does not believe a CBA is justified at this time and that requirements for marketplace quality statistics be considered once TREATS is implemented.

**Question 4: *Should trade-through protection apply only during “regular trading hours”? If so, what is the appropriate definition of “regular trading hours”?***

- Trade-through protection should only apply to the regular trading hours of the principal marketplace i.e. 9:30 a.m. to 4:00 p.m.
- Re-directing orders to other markets outside of these hours would result in a loss of order priority along with introducing unjustified complexity and compliance monitoring. If the secondary markets have relevance, then dealers will access them outside of regular hours based on specific client instructions and/or business drivers.

**Question 5: *Should the consolidated feed (and, by extension, trade-through obligations) be limited to the top five levels? Would another number of levels (for example, top-of-book) be more appropriate for trade-through purposes? What is the impact of the absence of an information processor to provide centralized order and trade information?***

- We do not believe that a consolidated feed should be limited to the top five levels. We believe it should include all levels and by extension, that the trade-through obligations should apply to visible orders in the full depth-of-book for transparent markets only.
- BMO believes that a consolidated feed is essential to standardize market data and facilitate best execution. This would also simplify the handling of orders going through smart order routers to satisfy best execution and facilitate compliance with the trade-through obligation.
- We do not believe market participants will be able to fully comply with these obligations without a consolidated feed.

**Question 6: *Should there be a limit on the fees charged on a trade-by-trade basis to access an order on a marketplace for trade-through purposes?***

- Market forces should drive pricing to the most competitive level without regulatory intervention. There are too many variables associated with determining best execution outside that which a marketplace charges to access a quote.

**Question 7:** *Should the CSA establish a threshold that would require an ATS to permit access to all groups of marketplace participants? If so, what is the appropriate threshold?*

- BMO is supportive of the concept of a threshold but is unsure what it should be in the absence of a fully competitive environment.
- We recommend that regulators revisit the concept after a year of multiple marketplaces to assess the feasibility of establishing a suitable threshold for Canadian marketplaces.

**Question 8:** *Should it be a requirement that specialized marketplaces not prohibit access to non-members so they can access, through a member (or subscriber), immediately accessible, visible limit orders to satisfy the trade-through obligation?*

- *Should an ATS be required to provide direct order execution access if no subscriber will provide this service?*

No, as this effectively defeats the purpose of establishing specialized marketplaces.

- *Is this solution practical?*

No.

- *Should there be a certain percentage threshold for specialized marketplaces below which a trade-through obligation would not apply to orders and/or trades on that marketplace?*

We believe that 5% may be an appropriate threshold after one year of continuous trading.

**Question 9:** *Are there any types of special terms orders that should not be exempt from trade-through obligations?*

- No. All special terms orders should be exempted.

**Question 10:** *Are there current technology tools that would allow monitoring and enforcement of a flickering quote exception?*

- To our knowledge, there are no tools available to allow for monitoring and enforcement of a flickering quote exception.
- An intermarket sweep order would assist in addressing this issue.

**Question 11:** *Should the exception only apply for a specified period of time (for example, one second)? If so, what is the appropriate period of time?*

- Any flickering quote exemptions would depend on the time of day and the transaction load, e.g., additional time at market open and close would be reasonable over intra-day trading.

**Question 12:** *Should this exception only be applicable for trades that must occur at a specific marketplace's closing price? Are there any issues of fairness if there is no reciprocal treatment for orders on another marketplace exempting them from having to execute at the closing price in a special facility if that price is better?*

- We believe the trade-through obligation should only apply during regular trading hours. We support an exemption for trades executed in after-hours facilities.

**Question 13:** *Should a last sale price order facility exception be limited to any residual volume of a trade or should it apply for any amount between the two original parties to a trade? What is the appropriate time limit?*

- We believe that the last sale price exemption should be limited to the residual volume and believe that one minute is an appropriate time limit.

**Question 14:** *Should trade-throughs be allowed in any other circumstances? For example, are there specific types or characteristics of orders that should be subject to an exemption from the trade-through obligation?*

- We would suggest that specialty price crosses should be exempt. – This would include basis, VWAP, contingent and special trading session (STS) crosses. Opening orders and normal course issuer bids should also be exempt.

## **B. Best Execution Requirements**

BMO appreciates the expanded definition of best execution to include price, speed of execution, certainty of execution and overall cost of the transaction as opposed to a trade-by-trade definition.

**Question 15:** *Are there other considerations that are relevant?*

- Anonymity is an important factor for clients.

**Question 16:** *How does the multiple marketplace environment and broadening the description of best execution impact small dealers?*

- Multiple marketplaces will increase technology and compliance costs for all dealers. This will place a proportionally greater financial burden on smaller dealers.

**Question 17:** *Should the best execution obligation be the same for an adviser as a dealer where the adviser retains control over trading decisions or should the focus remain on the performance of the portfolio? Under what circumstances should the best execution obligation be different?*

- We believe the best execution obligation should be uniform for all market participants including advisers.

**Question 18:** *Are there any other areas of cost or benefit not covered by the CBA?*

- As noted in question two, BMO is not supportive of a CBA being performed by the regulators at this time.

**Question 19:** *Please comment on whether the proposed reporting requirements for marketplaces and dealers would provide useful information. Is there other information that would be useful? Are there differences between the US and Canadian markets that make this information less useful in Canada?*

- Multiple marketplaces should be in operation for at least one year before determining the usefulness of reporting information and the differences between the US and Canadian markets. Marketplace information on best execution and trade-throughs would be beneficial to the industry, however, we do not believe a CBA is required to identify the relevant data.

**Question 20:** *Should trades executed on a foreign market or over-the-counter be included in the data reported by dealers?*

- No. See our responses to questions 2 and 19.

**Question 21:** *Should dealers report information about orders that are routed due to trade-through obligations?*

- No. See our responses to questions 2 and 19.

**Question 22:** *Should information reported by a marketplace include spread-based statistics?*

- No. See our responses to questions 2 and 19.

**Question 23:** *If securities are traded on only one marketplace, would the information included in the proposed reporting requirements be useful? Is it practical for the requirement to be triggered only once securities are also traded on other marketplaces? Would marketplaces always be in a position to know when this has occurred?*

- No. See our responses to questions 2 and 19.

### **C. Direct Access Issues**

**Question 24:** *Should DMA clients be subject to the same requirements as subscribers before being permitted access to a marketplace?*

- No, as sponsoring dealers already assume this responsibility on behalf of clients.

**Question 25:** *Should the requirements regarding dealer-sponsored participants apply when the products traded are fixed income securities? Derivatives? Why or why not?*

- These requirements should only apply to exchange-traded securities.

**Question 26:** *Would your view about the jurisdiction of a regulation services provider (such as RS for ATS subscribers or an exchange for DMA clients) depend on whether it was limited to certain circumstances? For example, if for*

***violations relating to manipulation and fraud, the securities commissions would be the applicable regulatory authorities for enforcement purposes?***

- We believe the securities commissions would be the logical regulatory authority for enforcement, however, this is complicated and made difficult by the current Canadian Securities regulatory structure with no national regulator.

***Question 27: Could the proposed amendments lead dealer-sponsored participants to choose alternative ways to access the market such as using more traditional access (for example, by telephone), using foreign markets (for inter-listed securities) or creating multiple levels of DMA (for example, a DMA client providing access to other persons)?***

- Yes. There is risk that clients may attempt to avoid the additional regulatory requirements which could place a greater compliance burden on the sponsoring dealers and could ultimately hinder the competitiveness of Canadian marketplaces.

***Question 28: Should there be an exemption for foreign clients who are dealer-sponsored participants from the requirements to enter into an agreement with the exchange or regulations services provider? If so, why and under what circumstances?***

- No. Domestic and foreign dealer-sponsored clients should be treated equally.

***Question 29: Please provide the advantages and disadvantages of a new category of member of an exchange that would have direct access to exchanges without the involvement of a dealer (assuming clearing and settlement could continue to be through a participant of the clearing agency).***

- BMO does not see any advantages in creating a new category of member of an exchange that would have direct access to exchanges without the involvement of a dealer.
- BMO believes that creating such a new member category would introduce additional risk to the industry. The risks associated with electronic trading without dealer oversight could not be addressed satisfactorily even with real-time regulatory or marketplace supervision. If this new classification of client were approved, then some of the dealer gatekeeper responsibilities would have to shift from the dealer to the regulators and/or marketplace.

Once again, we appreciate the opportunity to comment on these issues. Please do not hesitate to contact us if you have any questions.

Yours truly,

James Ehrensperger  
Managing Director, Equity Products  
**BMO Capital Markets**  
1 First Canadian Place, 3<sup>rd</sup> Floor Podium  
Toronto, ON, M5X 1H3

Tel: 416-359-4351  
Fax: 416-359-4484  
Email: [james.ehrensperger@bmo.com](mailto:james.ehrensperger@bmo.com)