



**CIBC**  
**World Markets**

April 26, 2005

**British Columbia Securities Commission**  
**Alberta Securities Commission**  
**Manitoba Securities Commission**  
**Ontario Securities Commission**

**c/o John Stevenson, Secretary**  
**Ontario Securities Commission**  
**20 Queen Street West**  
**Suite 1903, Box 55**  
**Toronto, Ontario M5H 3S8**

**RECEIVED**

**MAY - 9 2005**

**Ontario Securities Commission**  
**SECRETARY'S OFFICE**

Dear Sirs:

**RE: Comments on Concept Paper 23-402 Best Execution**  
**and Soft Dollar Arrangements**

CIBC World Markets Inc. appreciates the opportunity to comment on the CSA's concept paper 23-402 - Best Execution and Soft Dollar Arrangements (the "Paper"). You will note that our response consists of two sections. The first section contains our views concerning the various issues related to "best execution", while the second section contains our responses to the specific questions posed in the Paper.

**Section 1: CIBC World Markets' Views on "Best Execution"**

***Defining "Best Execution"***

We agree with the CSA's view, as stated in the Paper, that "there is no single, agreed upon definition of best execution" and that "best execution" is a process in which dealers, advisors, clients and the marketplace itself all play significant roles. In light of that statement, we trust that you agree that the process involves many elements including, but not limited to, obtaining the "best price" and that while obtaining the best possible price can be, and often is, an important factor in determining whether "best execution" has been achieved, it must be clearly understood that "best price" is not necessarily equivalent to "best execution". We would argue that, in fact, the criteria for assessing "best execution" should be defined primarily by the client's trade instructions. For example, in those cases where the client's primary concern is to get the best price available, it's fair and proper to assess best execution using price as the primary criteria.

Having said that, it's equally important to recognize that in many cases other criteria, such as the speed or certainty of execution, are of equal or greater importance to the client. In those cases, the criteria for assessing "best execution" will differ from the first example, highlighting the fact that the definition of "best execution" must be flexible enough to accurately reflect these differences- all of which ultimately depend on the client's instructions.

#### *The Impact of the Current Regulatory Framework on "Best Execution"*

We believe that it's important to recognize that existing trading rules can, at times, impede defining and enforcing "best execution" by imposing obligations that are counterproductive to the achievement of "best execution", however defined. For instance, the dealer's obligation to obtain the "best price" (UMIR 5.2) can, on occasion, impede a dealer's ability to obtain "best execution" by elevating the importance of one criteria of "best execution" (i.e. "best price") despite the fact that obtaining the "best price" may be inconsistent with the client's instructions. Furthermore, even in cases where the client's primary objective is to obtain the "best price", existing rules impose somewhat contradictory requirements. For example, UMIR Rules stipulate that, for retail-sized orders, every client is owed the best price available at the time the order is placed and that "where a security trades on a single market, this duty is fulfilled by *immediately* executing the order ... " In many instances, however, the currently displayed market is not considered a true indication of "best price". In those cases, dealers face a regulatory dilemma: If they execute the order "immediately," they leave themselves open to the allegation that they failed to comply with UMIR 5.2 because they failed to take reasonable steps, prior to execution of the client order, to ensure that the best price is obtained for the client. We believe that in order to avoid confusing and/or contradictory regulatory obligations, "best execution" rules must be flexible and must reflect the fact that the concept of "best execution" is based on many elements, and that the relative weightings of these elements will vary from trade to trade depending on the type of client, the type of order and the client's stated instructions. In other words, "best execution" rules should be process-based and less technical in nature, thereby giving dealers the flexibility necessary to consider all of the elements when seeking out "best execution". If "best execution" is to be something other than simply "best price", the trading rules must be amended to recognize this fact and support the seeking out of "best execution" and not simply "best price" or "immediate" execution.

#### *Measuring "Best Execution"*

A dealer's ability to measure "best execution" and, therefore, test for compliance with this requirement, is a key factor in the consistent provision of "best execution". At this time, there is no complete, electronic audit trail available for either the equity or the debt markets. In the equity market, historical trade and quotation data is available but there is no source for information regarding the depth of market at the time of the trade. The lack of trade and market information in the OTe debt market is even more profound thus making the assessment of "best execution" even more difficult.

## Section 2: Responses to Questions Posed in the PaDer

*Question 1: Are there any changes to current requirements that would be helpful in ensuring best execution? Do you think that clients are aware of their role in best execution or would some form of investor education be helpful?*

We agree with the CSA's stated view that "there is no single, agreed upon definition of best execution" and that "best execution" is a process in which dealers, advisors, clients and the marketplace itself all play significant roles." In light of that fact, we believe that the rules must reflect the fact that the process involves many elements including, but not limited to, obtaining the "best price" and that while obtaining the best possible price can be, and often is, an important factor in determining whether "best execution" has been achieved, it must be clearly understood that "best price" is not necessarily equivalent to "best execution". We believe that criteria for assessing "best execution" should be defined primarily by the client's trade instructions. For example, in those cases where the client's primary concern is to get the best price available, it's fair and proper to assess best execution using price as the primary criteria. Having said that, it's equally important to recognize that in many cases other criteria, such as the speed or certainty of execution, are of equal or greater importance to the client. In those cases, the criteria for assessing "best execution" will differ from the first example, highlighting the fact that the definition of "best execution" must be flexible enough that dealers can respond to clients' instructions as required, with traders using the appropriate level of skill and judgment demanded by their position without fear of regulatory reprisal. .

We do not believe that investors generally understand their role in this process and therefore, we believe that investor education would be useful.

*Question 2: Should there be more prescriptive rules than those which currently exist for best execution or should the methods for meeting the best execution obligation be left to the discretion of registrants?*

No. As we stated in our response to question 1 above, we believe that the criteria for assessing "best execution" should be flexible and allow dealers to determine what "best execution" is based on the client's trade instructions, on a case by case basis. More prescriptive rules would not reflect the fact that clients' have an infinite number of motivations and priorities for different trades ... all of which play a role in determining what "best execution" is in each particular case. Given that "best execution" is the outcome of a process that is unique to each trade, the rules must be flexible enough to embrace the importance of the discretion of the executing dealers in seeking "best execution."

*Question 3: Do you believe that there are other elements of best execution that should be considered? If so, please describe them.*

As stated above, the process of obtaining "best execution" involves many elements. It's important, therefore, that "best execution" rules reflect the fact that "best execution" is not limited to simply obtaining the "best price". In fact, while obtaining the best price can be, and often is, an important criteria in determining whether "best execution" has been achieved, the rules must reflect the fact that obtaining the "best price" for a client is not always equivalent to obtaining "best execution". We believe that "best execution" rules must recognize that the criteria for assessing "best execution" will vary from case to case depending on the needs and instructions of the particular client, and reflect that all other elements (speed, certainty of execution, size of the trade, nature of the trade, likelihood of settlement etc.) may be of equal or greater importance to the client under certain circumstances.

*Question 4: If audit trail information is not in easily-accessible electronic form, how is the information used to measure execution quality? Is there other information that provides useful measurement?*

A dealer's ability to measure "best execution" and, thus test for compliance with this requirement, is a key factor in the consistent provision of "best execution". At this time, there is no complete, electronic audit trail available for either the equity or the debt markets. In the equity market, historical trade and quotation data is available but there is no source of information regarding the depth of market at the time of the trade. In more global capital markets, where identical securities can be sourced through multiple jurisdictions, it is also important that historical market data from all sources be available in a consolidated form. The lack of trade and market information in the *aTC* debt market is even more profound making the assessment of "best execution" even more difficult. We cannot overemphasize the importance of this point and we hope that market regulators recognize that if dealers hope to test for "best execution" effectively, the issues of data access and market transparency must first be addressed.

*Question 5: Do you believe the suggested description emphasizing the process to seek the best net result for a client is appropriate and provides sufficient clarity' and, if not, can you suggest an alternative description?*

We agree with the suggested description.

*Question 6: Do you believe that there are any significant issues impacting the quality of execution for:*

*(a) Listed equities - whether Canadian-only, inter-listed or foreign-only;*

We don't see any serious issues with respect to Canadian or inter-listed equities. With foreign listed equities, there are issues around the availability and quality of information which make assessment of "best execution" difficult.

*(b) Unlisted equity securities-*

The lack of market transparency is the single biggest factor affecting the quality of execution in this market and while large, institutional investors can generally overcome the inherent problem of any *aTC* market (i.e. lack of market transparency), retail clients generally lack

the ability to effectively "shop the market" and are, therefore, more significantly impacted by this market limitation.

*(c) Derivatives-*

Listed derivatives:

We do not see any significant issues with listed derivatives.

OTe Derivatives - Again, the lack of market transparency is the single biggest factor affecting the quality of execution in this market and while large, institutional investors can generally overcome the inherent problem of any aTC market (i.e. lack of market transparency) retail clients generally lack the ability to effectively "shop the market" and are, therefore, more significantly impacted by this market limitation. Additionally, the fact that fewer dealers may be able to execute trades in derivatives, there is less comparative information available with which to measure "best execution."

*(d) Debt securities -*

The lack of market transparency is the single biggest factor affecting the quality of execution for debt securities generally. The same challenges exist for debt securities as with aTC equities, as described previously.

*Question 7: How should dealers in Canada monitor and measure the quality of executions received from foreign executing brokers?*

Canadian dealers using foreign executing brokers are, as a result of a lack of available market and execution data in the foreign market, hampered in accurately assessing the quality of executions provided by the foreign dealers used. As a result, when Canadian dealers select foreign executing brokers, it's important that dealers make every effort to determine whether the foreign firm will provide high quality of executions. Dealers should also ensure that they do not select a foreign executing dealer based on criteria unrelated to quality of execution. For instance, a Canadian dealer should not select a foreign executing dealer based on shared market making revenue or any payment for order flow arrangement. The Canadian dealer has a fiduciary obligation to ensure that foreign dealer selection is based on the quality of their executions. Furthermore, dealers should be required to demonstrate the rationale for their routing decisions, if requested.

*Question 8: Do you think that internalization of orders represents an impediment to obtaining best execution?*

Assuming that the order handling rules are abided by, we do not believe that internalization of order flow represents an impediment to obtaining "best execution".

*Question 9: Should there be requirements for dealers and advisers to obtain multiple quotes for OTC securities? Should there be a mark-up rule that would prohibit dealers from selling securities at an excessive mark-up from their acquisition cost (similar to National Association of Securities Dealers, Inc. (NASD) requirements dealing with fair prices)?*

We believe that this may be feasible, but only in an fully automated environment where multiple quotes can be obtained electronically and simultaneously. Failing this ability, the

requirement may impede a dealer who is seeking best execution where immediacy of execution is the primary goal. While we do not object to regulated mark-up regulations, it is important to ensure that any such requirement would consider different order sizes.

*Question 10: How is best execution tracked and demonstrated in a dealer market that does not have pre- or post-trade transparency such as the debt or unlisted equity market?*

Without access to full market data, it is extremely difficult to determine "best execution" with any certainty. Failing access to this information, any determination of "best execution" is based solely on internal dealer data, which is insufficient to make an accurate assessment.

*Question 11: How does an adviser ensure that its soft dollar arrangements are consistent with its general obligations to its clients?*

Clearly, "soft dollar" arrangements have the potential to impede "best execution" given that traditional soft dollar arrangements encourage order flow decisions to be based less on the quality of the dealer's execution and more on which dealer will award the most soft dollar income to the investment manager. In light of that fact, in order for soft dollar arrangements to survive in a "best execution" environment, mechanisms must be designed and implemented that will ensure that order routing decisions are made solely with regard to what is in the client's best interests irrespective of allocation commitments, and that the commissions used to pay for the soft dollar expenses will benefit the same investors that have generated the commissions. Further, advisers are required to comply with OSC Policy 1.9 in making use of soft dollars. If advisers apply a strict interpretation to the definitions of allowed "soft" goods and services under OSC Policy 1.9, they will be better able to monitor their soft dollar arrangements and ensure they are fulfilling their general obligations to their clients.

One potential solution to the "best execution" / soft dollar quandary would be the U.S. version of a "Step Out". That is, the ability to execute a trade with one dealer but then "give-up" the trade to another dealer. This would allow a fund manager to direct an order to the dealer that they believe will provide the best execution without the concern of not being able to fulfill allocation obligations.

*Question 12: Are there any other additional benefits or concerns with soft dollar arrangements that are not noted above?*

No

*Question 13: If it is acceptable to pay for goods or services using soft dollars, which services should be included as "investment decision-making services" and "order execution services" and which services should specifically not be included?*

It is our view that the definitions of "investment decision making services" and "order execution services" in OSC Policy 1.9 are too general and require too much subjective interpretation. It is our view that the Canadian rules should move in the same direction as

those in the U.S and the U.K. which seek to limit such goods and services to execution and research.

*Question 14: Should there be additional disclosure requirements beyond those specified in OSC Policy 1.9 and AMF Policy Statement Q-20, National Instrument 81-101 and proposed in National Instrument 81-106? Should the disclosure requirements be the same for third party soft dollar payments and bundled commissions?*

It is our view that investment managers should be required to disclose their soft dollar arrangements to their clients and should implement processes to ensure that the soft dollar expenses that are paid for with investor funds are tracked back to, and specifically benefit, the investors whose trades generated the commissions.

*Question 15: What, if any, are the practical impediments to an adviser:*

*(a) splitting into their component parts commission payments that compensate for both order execution and "investment decision-making services" as a result of either third party soft dollar arrangements or bundled commissions; or*

We have no comment on this issue.

*(b) making a reasonable allocation of the cost of "investment decision-making services" to the beneficiaries of those services (for example, allocating across mutual funds)?*

We have no comment on this issue.

*Question 16: If the split between order execution and "investment decision-making services" cannot be measured reliably, should the entire commission be accounted for as an operating expense in the financial statements? If it can be measured reliably, should the "investment decision-making services" portion of commission payments be accounted for as an operating expense in the financial statements?*

We have no comment on this issue.

*Question 17: Would it be appropriate for the MER to be based on amounts that differ from the expenses recognized in the audited financial statements? For example, should the entire commission continue to be accounted for as an acquisition/disposition cost in the financial statements but the MER calculation be adjusted either to include all commissions or to include only that portion that is estimated to relate to "investment decision-making services"?*

We have no comment on this issue.

***Question 18: Should directed brokerage or commission recapture arrangements be limited or prohibited?***

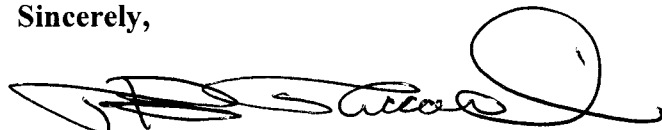
Like soft dollar arrangements, both directed brokerage arrangements as well as commission recapture agreements have the potential to impede achieving “best execution”. In all three scenarios, parties to these arrangements (i.e. both the dealers and the investment managers) have a vested interest in directing trade flow to a particular dealer for reasons which conflict with their fiduciary obligation to the investing client. It is our view that such arrangements should not be prohibited. It is incumbent on both dealers and investment managers to ensure these arrangements do not compromise their duties to their clients. It is our further view that all such arrangements where another party (other than the dealer) receives a portion of the commission on a trade, are fully disclosed to and authorized by the end clients.

***Question 19: Should disclosure be required for directed brokerage or commission recapture arrangements?***

Yes, we believe that these arrangements have a potential impact on the performance of an investor’s portfolio and should, therefore, be disclosed to investors so that they can make a fully informed decision in this regard.

We hope that the foregoing comments and observations are of assistance to you in your deliberations regarding these important subjects. Please feel free to contact us if you’d like any further information.

Sincerely,

A handwritten signature in black ink, appearing to read "Paul Riccardi", with a large, stylized flourish at the end.

**Paul Riccardi**  
**Vice President, Head of Institutional Compliance**