May 13, 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, ON M5H 3S8
jstevenson@osc.gov.on.ca

Anne-Marie Beaudoin, Directrice du secretariat
Autorite des marches financiers
Tour de la Bourse
800 square Victoria
C.P. 246, 22e etage
Montreal, Quebec H4Z 1G3
consultation-en-cours@lautorite.com

Dear Sirs/Mesdames:

Re: Concept Paper 23-402: Best Execution and Soft Dollar Arrangements

Thank you for the opportunity to comment on Concept Paper (CP) 23-402, Best Execution and Soft Dollar Arrangements. The opportunities available to industry participants and the competitive success of the Canadian investment community in an increasingly global market will be determined in no small part by any actions you take in response to your concept paper.

The following summarizes the observations and recommendations that we discuss in our submission.

- Clients own the commission dollars and anything purchased with those commissions must benefit the client. Money manager policies on commission use and commission recapture must be understood and accepted by clients;

- Services eligible for commission payment should be clearly defined and prices fully disclosed;

- Independent research services should be treated the same as bundled research and the playing field leveled when competing with bundled research;

- It is time to eliminate the unfavorable optics, innuendo and general misunderstanding that is associated with investment terms like “soft dollars”;
- The investment industry must be structured so that the interests of investors, money managers and brokers are aligned;
- Regulation must not block industry entry from a monetary standpoint at the broker, analyst or money manager level;
- The dual pay system for money management through management fees and agency commissions on trade contracts has worked, is working and will work in the future. This structure is consistent with our international trading partners;
- Regulation must recognize the unique structure of the Canadian investment industry and the growing global competition that is eating our lunch;
- Market fragmentation has run its course in the USA. Consolidation quickly gains momentum – expect the same in Canada;
- “Best Execution” must have a definition in order to be measured. Regulators should provide guidance as to systems and/or procedures that will be examined when compliance audits take place;
- Exposed orders on the TSX at better prices, must be displaced by ATS participants before trades are executed on an ATS (do not allow trade-throughs);
- Rule changes by the FSA and the SEC are important to our competitive position and should be considered before finalizing rules in this country.

FSA Submission re Consultation Paper 176

We recently made a submission to the Financial Services Authority (FSA) in England, commenting on Consultation Paper 176 dealing with bundled brokerage and soft commission arrangements and welcome the opportunity to share some of our thoughts with Canadian Regulators.

As part of our submission to the FSA, we included the submission that we and other market participants made to the Ontario Securities Commission on October 17, 1995 and we include that the 1995 Submission with today’s submission.

We were gratified to see that the FSA adopted our **basic premise that commission dollars belong to the client and several of our recommendations including the recommendation that the term “soft dollars” be scrapped and that the rules and policies deal with the legitimate and acceptable use of Commission dollars to acquire goods and services that benefit the client**. We will try to persuade you to take the same action in setting policies for the future.

CP23-402 – Macro Issues

CP 23-402 raises three macro issues: (i) the use of commission dollars, (ii) best execution, and (iii) market structure. How these issues are dealt with will have a significant impact on competitive forces including the ease of entry to our industry on both the buy and sell sides of the street.

CP23-402 indicates that regulators have recognized two important principles: (i) the need to enhance and protect the interests of individual investors whether they are acting individually or as part of an investment fund/plan, and (ii) the options on how the individual elects to participate in the market must be flexible and left open to the individual investor's choice.

It follows then, that **the interests of investors, money managers and brokers need to be aligned so that portfolio decisions reflect a relationship geared to provide the best returns possible under various risk constraints**.

We believe that the regulators and the industry should take a principles-based approach and that transparency and disclosure should be the primary tools used to implement this approach. We believe that these tools will provide the audit trail necessary for the client to monitor the value received and for regulatory examination and compliance checks. We further believe that prescriptive rules should be used as a last resort.

For those who believe that making money with money is easy, try borrowing $10,000.00, putting it into an RRSP and doubling it ten times. If you want to challenge Bill Gates to become the richest person in the world, try to double it twenty times. The truth of the matter is that investing money successfully is extremely difficult – witness the number of professionally managed portfolios that miss targets or benchmarks.

Money management is a very competitive business and the stakes are high. Yet in its simplest form, the essence of money management is recognizing mispriced securities and executing trades with the least amount of leakage in order to enhance the value of the portfolio. The investment industry has to be structured to recognize these needs and to provide the most opportunity and flexibility in order for participants to succeed. **All participants must be able to recognize abuses so that investors are protected.** In this context, CP 23-402 has successfully targeted the primary industry challenges in this respect.

Active vs. Passive Mandates

In choosing a money manager, the investor has a choice between whether to give that manager an active or passive mandate. If the choice is passive, then the investor expects the money manager to replicate a benchmarked index as closely as possible, recognizing that trade execution costs will impede the manager's ability to provide a 100% match. Various fund managers offer types of "portfolio tilts" to try to outperform the benchmark.

Monitoring the activities of passive managers for compliance and determining whether they are acting in the interests of their clients is relatively straightforward. Also, minimizing trade execution costs is of paramount importance to achieving success for this style of money manager.

If the choice is an active mandate, the money manager will choose investments based on the client's style mandate and risk tolerance. The question that an active mandate raises is whether the client expects the money manager to initiate all of its investment ideas from internal sources or does the client expect the manager to use its collective brain power to source investment ideas from wherever they can be found. If it is the latter (as it usually is), who pays for the external ideas (assuming nothing worthwhile is free)? Does the client expect the manager to budget a specific amount out of the management fee for external research (bundled or independent) and once that money has been spent, not to seek more ideas until the next year? Hardly. Therefore, the issue becomes what tools can the client make available to these managers so that they will not shirk their responsibilities to identify as many trading opportunities as possible.

More specifically, what role can trade commissions play in the overall scheme of things to enhance the ability of the manager to meet client needs and to ensure that the client is receiving value for its commission dollars. One question that has to be addressed in this respect is the fear that the money manager will enrich itself at the client's expense if the manager is permitted to use the commission dollars owned by the fund to pursue outside research. The second question that arises is whether the interests of the money manager and the client are aligned if the money manager is given an incentive to act with the least amount of research possible.

<u>The Welfare Effect of Soft Dollar Brokerage: Law and Economics</u>

These issues with respect to the use of commission dollars by money managers to acquire research and order execution services and the potential solutions to the problems were skillfully discussed by Stephen M. Horan and D. Bruce Johnsen in their book *The Welfare Effect of Soft Dollar Brokerage: Law and Economics* published in June 2000.

In their chapter on "The Unjust Enrichment Hypothesis" they discussed the conflicts of interest that could be created between advisors and clients. These are the same arguments used today by commentators outside the investment industry or those in the industry who fail to do their homework. Paying excessive commission rates, over-trading to generate commissions to pay money manager obligations, over-consumption of research, and directing trades to the wrong broker in violation of best execution rules are but a few of the charges laid. These charges sell newspapers and confuse or enrage the public. In the end, the authors conclude, and with our experience we agree, that over time, managers that succumb to these temptations under perform and lose their mandates. If you add to this consequence, the call to increase disclosure and transparency in the use of commissions, you give plan administrators and other clients the opportunity to discover abuses long before they can hurt the plan or portfolio. Money managers who unjustly enrich themselves would be quickly discovered and driven from the community.

The chapter on "The Incentive Alignment Hypothesis" relates to all brokerage arrangements where execution and research are linked, whether they are bundled at source or third party combinations.

Under this hypothesis, both money managers and brokers become agents of the fund participants. Relationships are established that address the concerns that money managers will shirk their responsibilities on trade monitoring and identifying mispriced securities. Brokers are given the monetary incentive to act in the best interest of their clients by providing superior research (bundled or third party) and trade execution. There is no question that commissions owned by the plan play a significant role in subsidizing research in this relationship. However, through disclosure and transparency, plan administrators can monitor the activities and performance of their money managers as well as their brokers to insure that they are getting value-added services and that commission dollars are not being wasted.

<u>Provision of Services</u>

In all industry, choices are made whether to outsource services or to create them internally. These choices are made based on economic and competitive criteria so that the intellectual and physical assets of a company are best exploited for profit. Usually the final product of a company is priced to the public reflecting all cost inputs and a profit margin.

However, some industries operate best on a cost plus structure because the final product is a result of continuing inputs or there is no final product but rather an on-going service. In these instances, the "general contractor" is retained at a fee and if external products or services are purchased, the cost is flowed through to the client. Some custom homebuilders, lawyers and consultants are examples of this type of structure where the service providers and services are contracted on set fee basis but pass on the cost of outside services directly.

The money management industry is particularly suited to this structure. Money managers bring certain skill sets to the table for which they collect a basic management fee. If external trade execution costs or outside research costs are incurred, they are passed on to their clients. Money managers do not have to be stock exchange members, nor do they have to maintain large internal research departments with global capabilities to be competitive. Functioning in this manner clearly lowers their operating costs.

The unbundling that has occurred on the sell side of the street gives money managers the choice of executing trades on an execution only priced basis as well as to pay for external research by paying a higher commission on a trade by trade basis. Commissions paid for independent research are easy to track and audit trails already exist. Bundled dealers will have to price their research services on a product by product basis to provide the same disclosure. Pricing problems will occur as research providers recognize the difference in

ability to pay in large and small clients. Direct access to analysts and other tiered services could distinguish various categories of service.

The questions posed in CP 23-402 indicate that Canadian regulators want to provide the framework necessary to protect the interests of the individual as well as provide an industry environment that allows Canadian money managers and brokers to compete in the global markets. In fact, as we stated in our submission in 1995 and as we reiterate now:

> Due to the global nature of the marketplace, Canadian regulation of the use of commission dollars to acquire goods or services needs to be structured in a manner that does not drive business offshore to avoid compliance with its requirements but also is not so loose that it attracts business and encourages activities that result in abuse of investors' rights and discredits the Canadian capital markets.

Regulators in England (FSA) and Chairman Donaldson of the SEC in the USA have strongly signaled that commission payments for execution and research services will continue to be permitted, although their scope will be narrowed.

In regulating the scope of these services, regulators need to take into consideration the overall cost structure of the Canadian investment industry so that services can be created and delivered economically as well as efficiently from domestic and international sources.

Any regulation that blocks or significantly adds to the cost of entry to our industry inevitably will lead to consolidation and the formation of oligopolies and thereby lessen competition. Without competition from new entrants with new ideas, the money management industry will get tired and less competitive and clients will have fewer choices.

Fortunately, today's market structure parallels that of our trading partners and keeps ease of entry on both sides of the street at a minimum monetarily. Whether potential industry entrants are brokers, money managers or research analysts, they all compete for clients' commission payments. Although clients pay both money management fees and trade execution commissions, they have been declining significantly over recent years. There is no indication that these costs have stopped falling.

1995 Framework Submission

In our 1995 Framework Submission Respecting the Use of Commission Dollars to Acquire Goods and Services (a copy of which accompanies this letter), we dealt with the questions raised in CP 23-402 on soft dollars. We urge you to read this Framework as part of this submission. It was the result of work and contributions of a broad cross-section of Canada's investment industry that had strong opinions for and against the use of soft dollars as they applied to third party payments. In the Framework, we dealt with:

(i) the context in which basic principles should be framed, (ii) the basic principles under which commissions could be used by both money managers and the client, as well as (iii) disclosure requirements. I believe that we made a strong case for dropping the term "soft dollar" and for framing policies and rules around legitimate use of commission dollars to acquire execution and research goods and services.

The FSA has adopted this approach and, as noted earlier, we recommend that you follow the FSA in framing all future policies regarding the use of any part of commission payments around the legitimate use of commission dollars.

It is unfortunate but the term "soft dollar" has always been a "lightning rod" in attracting confusion and criticism and in creating the impression that you are paying somebody for something for which you are not getting full value.

Another reason for dropping the "soft dollar" term is that trade execution charges vary from trade to trade based on the difficulty of execution, inventory needs, capital commitment and market liquidity. Any effort to determine the "soft dollar" component of the commission by deducting the execution charge only adds to cost with no material benefit.

We agree with the recommendations of the FSA that eligible investment decision making services should not include "expected business expenses" like computer hardware, subscriptions to local newspapers and magazines and that the permitted list of goods and services that may be acquired with commission dollars should be shortened to execution services and research.

We think that money managers must be very specific in reporting the services acquired with commissions and the value derived from their use. We also think that money managers must disclose their policies aimed at treating all clients equitably in the purchase and benefits from the use of order execution and investment decision making services and that they must maintain and disclose commission records that that back this up. Disclosure documents should be mandated and regulators should take an active role in determining the scope and structure of these documents. It is essential that plan administrators and other clients review the commission policies of their money managers before accepting them and then audit commission use against those policies or this effort will be wasted.

<u>Directed Commissions</u>

The discussion of "Directed Commissions" in CP 23-402 adds to the confusion in how commissions are allocated. Any commission expense that does not meet the "investment decision making" test or trade execution test and benefits only the money manager (or mutual fund manager) must be viewed as an abrogation of fiduciary responsibility. This topic has been dealt with in the Framework.

We submit that a better definition of "Directed Commissions" is **one that defines them as the use of commissions by the fund/client to pay legitimate fund/client expenses**.

Since the fund/client owns the commissions, there is no reason why an agreement cannot be worked out between the money manager and the fund/client where the money manager "directs" trades to a broker that is willing to give up part of the commission to pay fund expenses.

In fact, in order for the fund to have a better audit trail on the use of commissions and the payment of fund expenses, many funds have directed that the commission give-up be credited back to the fund (commission recapture). The fund's internal audit system then takes over to track the payments and match them with legitimate fund expenses.

In the past, performance measurement, actuarial consulting fees and custodial fees were common expenses paid by directed commissions. More and more these expenses are being paid directly by the fund with recaptured commissions.

Commission recapture programs are important tools to level the playing field on the purchase of research by money managers. They enable money managers to treat their larger clients more equitably by allowing them to recapture a portion of the commissions that they pay for research since their portfolio will look the same as the portfolio of smaller clients who do not incur the same commission payment.

It is imperative that money manager commission recapture policies be fully disclosed to all clients as part of their commission policies. Fund administrators who qualify for recapture must participate or disclose to their constituents why they declined to participate. Commission audit trails will prove that only the commissions generated by a fund can be recaptured to that fund.

Finally, commission expenses are probably now the smallest component of best execution but their influence on trade order placement must be recognized. Most public commentators dwell on the impact of commission expenses on a portfolio rather than on the factors that have a far greater impact on portfolio performance such as the market impact on a trade through information leakage, lack of trading skills and bad decision-making (each trade has two sides).

Best Execution

CP 23-402 correctly focuses on "best execution" (including market impact) in conjunction with commission expenditures. However, it is important not to lose sight of the fact that a good (meaning highly profitable) investment with poor trade execution will most likely have more positive impact on a portfolio than a bad investment (a real loser) with great trade execution. Best execution measurement has to reflect all circumstances including analyst access. Therefore, the SEC definition that **"The money manager must execute securities transactions for clients in such a manner that the client's total**

cost or proceeds in each transaction is the most favorable under the circumstances" states the obligation of both the money manager and the broker.

Without a distinct definition of "best execution", it is impossible for fund administrators/clients and regulators to determine whether abuses exist. By sending a strong signal that certain processes should be in place and that a trade oversight committee that meets regularly is created, regulators can elevate the recognition that best execution is important and must be examined.

Recommendations on Commission Use and Best Execution

Now for our recommendations on commission use and best execution.

Regulators have stated that subject to the feedback received from interested parties regarding CP 23-402, the appropriate "next steps" will be considered if any are deemed necessary.

We assume that you will consider, and urge you to consider in defining the Canadian landscape, the steps taken and to be taken by the FSA and the SEC.. In that regard, we have already seen what the FSA has proposed and we expect that the SEC will disclose its policy changes later this year.

We recommend that Canadian regulators delay their final policy proposals until the SEC publishes its consultation paper. It is important that Canadian regulators consider the potential changes in regulation of those markets before finalizing domestic changes if any. This is not to say that we have to parrot changes in these markets, but clearly, the Canadian investment community should not be disadvantaged by policy changes. Nor should our policies encourage activity or attract business that could result in investor abuses and discredit the Canadian capital markets. (see Framework)

We urge that regulators recognize the value of research in making investment decisions. This recognition would be consistent with the FSA proposals and the settlement between the New York Attorney General's Office and major U.S. investment dealers that requires independent research to be provided in parallel with dealer research to American investors. The SEC has signaled that it recognizes the importance of research as well.

The FSA rules allow commission dollars to be used to pay for research. **This policy endorses the dual payment system for money management, money management fees and the use of client commissions to buy research and trade execution services. The FSA has also recognized the confusion and "lightning rod" effect of the term "soft dollar" and has removed it or is in the process of removing it from its commission use policies.** We strongly recommend that Canadian regulators adopt that stance as well.

This does not mean that we recommend that money managers should have unlimited full access to commissions to purchase any product that they deem to be "research".

Regulators must give some guidance as to the definition of research and acceptable products. This guidance must recognize changes that have taken place in the investment industry and industry in general as to expected business expenses. The FSA eliminated newspaper and magazine subscriptions, computer hardware, performance measurement for an advisor's use, dedicated phone lines, and seminar fees as permitted services to be paid for with commission dollars. They also removed services that are already banned in Canada because they are not "investment decision making services" that include travel, accommodation, entertainment expenses, office administrative computer software, membership fees, office equipment rentals, and employee salaries.

Regulators must also recognize that advisors can only consume a finite amount of research and still be getting value. Therefore, money managers must provide their clients with a list and description of the research services that they consume and how much was paid for them. We will deal more with this subject when we discuss the changing responsibilities of money managers on disclosure.

Canadian regulators must also provide guidance in their expectations regarding "best execution". As mentioned earlier, we believe that "best execution" has to have a definition and that specific policies and procedures should be in place to ensure compliance with this requirement. Money management and security trading methodologies are constantly evolving with new tools and services developing. Trade desk audits will continue to grow in importance to ensure compliance with best execution needs, but regulators should signal changes in expectations to the money management and dealer communities so that policies and procedures keep pace with competition.

Canada's uniqueness must be recognized when regulators create or change the rules on best execution. This is particularly true in relation to Alternative Trading Systems (ATS). We were one of the first markets to go to electronic trading on our exchanges. Also, we do not have a broad number of stock exchanges competing for order flow as exists in the USA. Automatic Trading Systems are only now entering the Canadian market even though several liquidity gathering systems tried but failed to gain traction in the past. It is interesting to observe that just as market fragmentation has started to become an issue in Canada, consolidation is taking place in the USA. The NYSE is attempting to become a public for profit company by merging with Archipelago. The NASDAQ is buying Instinet.

It is imperative that Canadian investor expectations are recognized and their rights protected. **The current exemption afforded ATSs because of the lack of a trade-through rule must be changed**.

As it stands today, an investor could expose a bid or offering for a security on the TSX, have institutional trades executed on an ATS lower than the bid or higher than the offering and not be able to participate. **This is wrong**.

It may be understandable that the trade-through rules may be changed in the USA because the NYSE is a slow market (not electronic). Specialists on the NYSE floor have far too much power to get in the middle of trades with total knowledge of supply and demand for stocks. The growth in demand for ATS services from institutional investors in the USA recognizes this advantage given to specialists as well as the growing information leakage problem regarding institutional trading.

In Canada, the exchanges are electronic. The investment community is small compared to the USA. An effective upstairs market exists among the dealer who must expose their orders to the floor before executing a trade. Better bids and offerings for securities have to be filled before a trade can take place, thus protecting investors who expose their orders on the exchange. The ATSs rely on the exchanges for price discovery. It is difficult to see how any trade levels could be established for an ATS without knowledge of the market for a stock on an exchange. There is no reason why a party participating in an ATS trade should not have to satisfy demand for securities as disclosed on the bid or offering side of the market at prices better than the proposed trade exercise price.

Today's electronic trading systems can take out bids and offerings on an exchange almost simultaneously with ATS execution. Exposed orders from investors would be filled. Iceberg orders would only be filled on the exposed portion of the order. (Such a trade-through rule would either discourage iceberg orders or improve the exposed portion of the order thus adding to apparent market depth)

Canadian investors must know that their exposed orders will be executed before trade executions at lower bids or higher offering can be completed or they will lose confidence in the capital markets system. Furthermore, it will be impossible to measure best execution by institutional investors if they cannot protect their interest on the Canadian Exchanges.

There is another way to achieve trade anonymity for institutional traders without having to resort to doing trades away from the TSX. Commission Direct Inc. recently introduced IOI Direct, a service that allows institutional traders to access market liquidity on an anonymous basis.

Traders enter Indications of Interest (IOI) into an independent matching computer vault on an encrypted basis. These indications of interest are just that; they are not trade orders. They indicate that a trader will buy or sell a security (at least 25,000 shares). The Commission Direct trading desk only sees that an indication has gone in from that client. It does not see that it is a buy or a sell and does not see the name of the security in the IOI. If the contra side of that indication is entered by another trader, the computer vault unencrypts the indications and a message is sent to the Commission Direct trading desk disclosing the traders involved, the name of the security and any price indications. The CDI traders then contact the traders involved in an attempt to convert the IOIs into trade orders and to execute a trade on the TSX. There is no need for relief from any trade-through rule because the trade cannot go up unless all better bids or offering are taken out. We are not suggesting that the TSX should exist without competition. We are only

pointing out that ATSs could adjust their technology to displace posted bids and offerings at better prices than the trade price.

Pricing Research

If regulators and plan administrators are to demand more accountability in the use of client commissions to acquire research, it follows that research will have to be priced. This is not a problem for third party or independent research providers. They already price their product but incur the disadvantage of having to add GST to that price. More on that later.

Bundled brokers face a greater dilemma in having to price their research. There are many options as to how to price it including individual services by each analyst, accessibility to analysts on a tiered basis, various research packages that may or may not include global opinions and access to corporate management meetings. The size of the client measured by funds under administration will also be a factor just like our tax system that charges on ability to pay even though the services offer by the government is the same.

It is unlikely that bundled research product will be available on a cash basis, at least initially because dealers need to "feed" their trading desks with order flow. Good research will attract trade. Since money managers will only be able to account for a finite amount of research, it follows that dealers will offer execution only prices for trades to protect their market share and service growing demand. Also, in the spirit of full disclosure, dealers will price the use of capital in trades. Research pricing will lead to total unbundling – providing a strong incentive to dealers to offer competitive product and trade execution.

Accountability of Money Mangers

Money managers will be more accountable for the use of commissions for the purchase of research and trade execution services. Their commission policies will receive far more scrutiny from plan sponsors/clients and regulators looking for consistency and savings. Many managers that we have interviewed already report commissions as a percentage of assets under administration to current and prospective clients. For the most part, they have set up commission and trade oversight committees that meet at least quarterly in order to determine that commission use is consistent with their policies. Those money managers who have not advanced to this stage of compliance will have to improve their reporting and accountability. These managers will rank the trading capabilities of their brokers on a formal basis to reward those brokers who provide the most value as far as best execution. It follows that money managers will expand their dealer list to improve trade execution and that they tap into liquidity from all sources. As well, money managers must provide their clients with a full description of the research services, including prices, that they purchase with commissions.

Money managers must fully disclose their commission recapture policies so that clients that qualify for them can participate. If money managers offer commission recapture,

they must be able to do so under best execution constraints. As mentioned earlier, commission recapture is a powerful tool in the hands of money managers who want to treat their larger clients equitably in the purchase of research. It is a preferable policy to directing commissions to pay for plan expenses because the plan's accounting system takes over to provide the necessary audit trails to plan administrators and participants. It is imperative that commissions can be tracked to prove that only the plan that paid the commissions receives the commission recapture.

Finally, all the changes in limiting as well as tracking the use of commissions under best execution constraints will be in vain if plan administrators/clients fail to monitor these expenses. These plan administrators/clients must review money manager commission policies and be comfortable that active managers are getting value for commissions spent.

We have interviewed plan administrators who advised us that they chose to "just say no" to commission recapture opportunities with no valid reason. These administrators have come under far more pressure recently to enhance the value of their funds by all means as the funds have moved from surplus to deficit positions.

Independent Research – Leveling the Playing Field

Earlier we mentioned that independent research does not have a level playing field with regards to pricing. We made a submission to the Ontario Securities Commission on February 10, 2004, suggesting that a new class of registrants be created – "Research Services Dealer" to level the playing field with respect to pricing. A copy of this submission accompanies this letter.

As noted in our February 10, 2004 submission, we strongly believe that the playing field should be leveled between independent and bundled research providers. Currently, independent research providers have to charge GST on their products and services because they do not qualify for the GST exemption granted registered dealers. If the new registrant category we suggested be created was created and compliance audits initiated, regulators would have a much tighter control on the services eligible for commission allocation. Only research services provided by registrants would qualify for commission payments. As we state in our submission, registration fees for this new registrant category would more than cover any additional expenses incurred by regulators.

This simple restructuring of the Canadian market would enhance disclosure, address best execution concerns, and place Canada in a leading role in setting a regulatory framework for its money management industry. We believe that regulators should reconsider our recommendation and take a more active role in framing the rules for the Canadian investment industry. We believe that the benefits to investors (lowering costs and clarifying acceptable services) as well as defining permitted services over-ride regulatory concerns about the number of categories of registration.

Uncertain optics, unfavorable innuendo and general misunderstanding of investment industry terms currently plague our industry. All participants must work together along

with regulators to make changes that will instill investor confidence, eliminate distractions and create industry opportunities that attract our most talented youth. It must not go unnoticed that five years ago, only one of our top forty money managers was foreign owned. Now thirteen of the top forty are foreign owned and control more than twenty-five percent of the money under management. These firms set compliance standards that not only respect Canadian rules but also reflect the regulatory standards at their headquarters.

The structure of the Canadian investment industry must be fully transparent and free from inappropriate conflicts of interest. The legitimate tools available to money managers using client commissions to pay for them must be well defined and their use fully disclosed. Trade execution standards must be set and defined that clearly exemplify the "client first" rule.

Yours very truly,
Commission Direct Inc.

Wayne B. McAlpine
President & Chief Executive Officer