Shorcan ATS

September 19, 2005

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
New Brunswick Securities Commission
Registrar of Securities, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory

c/o John Stevenson, Secretary
Ontario Securities Commission
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Dears Sirs and Mesdames:

Re: Request for Comments – CSA Discussion Paper 23-403 "Market Structure Developments and Trade-Through Obligations" (the "Discussion Paper")

1. *Introduction*

This letter comments on the Discussion Paper published in the Ontario Securities Commission Bulletin of July 22[1].Shorcan ATS Limited ("Shorcan ATS") wishes to participate in the public forum to be held next month.

Shorcan ATS has applied to the Ontario Securities Commission to operate a specialized equities marketplace in which Canadian investment dealers will have access for the purpose of managing risk in the trading of their inventories of TSX-listed and TSXV-listed equity stocks. Investment dealers that participate in the marketplace will engage in anonymous principal trading. Shorcan ATS will apply the trading methodology employed by Shorcan Brokers Limited ("Shorcan"), its parent company, in the market for government debt securities and other fixed income instruments in Canada.

When investment dealers buy and sell equity securities into or out of trading inventories, they are often facilitating trading activity by their institutional clients. In practice, investment dealers voluntarily use their trading inventories to add to the liquidity of organized Canadian equities marketplaces. Investment dealer clients expect them to fulfill this obligation and when they do so, institutional investors are often able to transact in size which helps institutions to reduce market impact costs and lower market risk. Fulfilling client needs in this way exposes investment dealers to risks that are different from those faced by institutional investors. Institutional investors do not use their inventories to facilitate trading by others.

Shorcan ATS believes that because of the special risks faced by investment dealers when engaged in principal trading, those investment dealers need a specialized market where they can trade on a basis that allows them to more effectively manage the market risk that dealers incur supplying liquidity to investors. Shorcan has offered a similar inter-dealer trading facility for the trading of Government of Canada fixed income instruments since the late 1970's. For the reasons given below, the utility of the Shorcan ATS marketplace will be seriously compromised for participating dealers if trade-through obligations apply to principal trading in respect of dealers' trading inventories. The telephonic trade negotiation process and, specifically, "trade

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[1] (2005) 28 0SCB 6910 – All page references provided in this comment letter are to the version of the Discussion Paper provided in the bulletin.

expansion protocol" utilized by Shorcan ATS to enable dealers to more efficiently manage trading risk will not be able to perform its risk management function if there is a "contingent liability" to another marketplace. Accordingly, the issues addressed by the Discussion Paper are of vital importance to Shorcan ATS.

2. *Commentary on Discussion Paper*

The Discussion Paper poses both general policy questions and much more specific and pointed questions. Shorcan ATS proposes to address most but not all of the questions. To avoid providing responses that are either excessive in length or repetitive, we propose to divide our commentary in two parts: the first is devoted to general observations, the second presents our responses to the questions on which we have an opinion to offer. Each question addressed is reproduced in full. For ease of comparison, we number each question that we have chosen to address with the same number as in the Discussion Paper.

(a) General Observations

Despite the fact that the Discussion Paper invites comment on the current structure of the Canadian market[2], it can fairly be said that the most important, most controversial and most extensively analyzed issue presented by the paper is the "trade-through" obligation and the scope of its application.

Because "trade-through" is an issue that applies *across* markets, it needs to be understood in light of the general principles of marketplace operation that operate in Canada. These principles are expressed mainly in National Instrument 21-101, *Marketplace Operation* ("NI 21-101"). NI 21-101 creates a framework for the operation within Canada of multiple marketplaces. As the Discussion Paper itself recognizes, NI 21-101 is meant to facilitate competition and choice[3]. Marketplaces are meant to compete and, to that end, marketplaces can choose from a variety of regulatory models such as the relatively lightly regulated "ATS" model or the relatively more heavily regulated "exchange" model. NI 21-101 does not dictate what particular services should be offered by the marketplace. Also, NI 21-101 does not champion the interests of any particular class of investor. It does not, for example, distinguish between retail users and institutional users of marketplace services. It promotes broad access to all marketplaces and contains restrictions on unreasonable access barriers.

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[2] Discussion Paper at 6334.
[3] Discussion Paper at 6344.

These general principles are crucial. As a matter of policy, trading rules such as the trade-through obligation addressed in the Discussion Paper cannot be allowed to undermine these principles. A balance needs to be struck between trading rules and competition/innovation[4]. This need for balance has been recognized in the Discussion Paper by the securities regulators who administer NI 21-101 and by Market Regulation Services, Inc. ("RS")[5] which enforces rules that apply across marketplaces.

RS's role as a proactive rule maker needs to be revisited by the supervising regulators in light of these principles and in light also of its intended function as a neutral enforcer of rules. RS operates under a recognition order granted by the OSC among others[6] that requires that all the UMIR rules that RS administers not "impose any burden on competition that is not necessary or appropriate in furtherance of securities legislation". RS itself has conceded[7] that UMIR should be "sufficiently marketplace neutral" so as not to impede the development of competitive marketplaces. Also, to the extent that RS is making rules concerning trade-through, those rules should not be more far-reaching than securities legislation. It is very significant that National Instrument 23-101, *Trading Rules* ("NI 23-101") deals explicitly with trade-through in Part 4 under the heading of "Best Execution":

4.2	Best Execution	
	(1)	A dealer acting as agent for a client shall make reasonable efforts to ensure that the client receives the best execution price on a purchase or sale of securities by the client.
	(2)	Without limiting the generality of subsection (1), a dealer acting as agent for a client shall not execute a transaction on a marketplace that could be filled at a better price on another marketplace or with another dealer.
	(3)	In order to satisfy the requirements in subsections (1) and (2), a dealer shall make reasonable efforts to use facilities providing information regarding orders.

[4] Discussion Paper at 6335.
[5] See RS Market Policy Notice 2005-001 – Strategic Review of UMIR – Progress Report (July 29, 2005) ("RS Strategic Review Notice")
[6] OSC Recognition Order of RS dated January 29, 2002 ("OSC Recognition Order").
[7] OSC Recognition Order, Schedule A, para. 7.

The statutory concept of trade-through captured in this provision is noteworthy in three respects: First, it applies only to dealers. Second, it applies only when a dealer is acting as an agent not when the dealer is acting as principal. Third, the trade-through prohibition is to be addressed by a dealer making "reasonable efforts" to check available prices on "facilities providing information".

In light of specificity of the legislation and RS's acknowledgement of the need for UMIR and RS to be "marketplace neutral", RS's campaign[8] in favour of an expanded trade-through rule seems inappropriate and unwarranted.

Competitive marketplaces regulated by NI 21-101 have not emerged for equity securities until the last few months. There is a definite lack of experience with marketplaces whose business plans and mode of operation differ from those of a stock exchange, the marketplace best understood by RS.

RS recognizes that institutional and retail investors face different market risks[9]. Investment dealers buying and selling out of inventory face unique risks. Dealers risk their capital to add liquidity to the market. Institutional investors and investment dealers face different risks and perform different functions.

Differences in risk faced by different categories of investors translate into differences in expectations about the services marketplaces need to perform. Retail investors depend on agents to convey their orders to marketplaces because they cannot get direct access to those marketplaces in any other way. Retail investors looking to execute small buy and sell orders equate "best price" with "best execution". Trade-through obligations force dealers acting as agents to find the marketplace with the best price. Trade-through prohibitions really speak to the aspirations and expectations of the retail or institutional investor who engages a broker to act as the investor's agent in the search process. It is no accident that both UMIR and NI 23-101 express the trade-through prohibition in the context of trading by an agent.

Retail investors and other categories of investor who rely on agency services to execute trades are the only appropriate beneficiaries of a trade-through obligation. Their agents should be obliged to compare prices on markets in which the client's trading interest can be represented. When an institutional investor or an investment dealer trade, their needs and expectations are

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[8] See for example, MIN 2005-016 (May 12, 2005) which reflects a surprising level of tension between RS and its recognizing regulators on the question of Trade-Through.

[9] See RS Strategic Review Notice at p. 4.

quite different from a retail investor. Their concept of best execution may entail much more than achieving best price[10].

For investment dealers seeking to manage risk, a trade-through obligation creates the risk of satisfying a cross market displacement obligation that forces them to address better priced interest in all markets before they can return to risk management in a specialized dealer market. In an inter-dealer market where trade negotiation is telephonic, the ability to conduct "work-ups" through a series of successive trades leading to an ultimate desired position is of critical importance to the viability of the model. With a trade-through obligation, the extent of interference by these other marketplaces with any transaction effected to manage risk cannot be predicted in advance. Investment dealers seeking to use specialized services in an inter-dealer market would have a contingent liability to other marketplaces to satisfy better priced interest there. This would impair their ability to manage risk with some certainty of getting their transactions completed especially when done as part of a "work-up" at their desired price point, size and time. This outcome is a consequence of regulating principal trading and agency trading identically when applying trade-through rules.

Investors that trade as principal and do not rely on agents to achieve best price should not be subject to a trade-through obligation. That UMIR policy 5.2 envisages such an obligation on parties trading as principal is not by itself compelling. First, as a basic legal matter, a policy interpreting a rule should not go beyond the rule it interprets in any fundamental way. Second, RS's thinking about trade-through reflects only the goals of marketplaces that operate on a principle of price priority: stock exchanges. RS has very little experience of looking at trading issues from the perspective of marketplaces that do not operate as conventional equities marketplaces.

RS has recently organized "roundtables" of buy-side and sell-side representatives and solicited written comments on specific questions of whether trade-through should be permitted and reported the following result:[11]

> "Respondents at the roundtables expressed the consensus view that "best execution" may require trading in a market with an inferior price if that market is more liquid and offers greater speed and certainty of execution than a market with a better price."

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[10] See Discussion Paper, in 9 and Concept Paper 23-402 Best Execution and Soft Dollar Arrangements (2005), 28 OSCB 1362 at 1367 and following.

[11] RS Strategic Review Notice at 8

(b) Answers to Specific Questions

1. *What factors or criteria should be considered in identifying the appropriate structure and requirements for the Canadian market?*

As pointed out in our introductory comments, the factors and criteria most relevant to addressing market structure are those that are already enshrined in NI 21-101 which emphasize competition among marketplaces with no restrictions on the business model that is followed by a particular marketplace. Trading rules like the trade-through prohibition should never undermine these principles if the result is that new marketplaces are prevented from emerging. Empirical and theoretical studies[12] support the view that competition between marketplaces enhances market quality and benefits investors. Market quality is directly related to the ability of market participants to manage trading risks. The expansion of the trade-through obligation to the ability of dealers to trade as principal in marketplaces is not justified. A market structure that respects the goals of NI 21-101 and addresses the varying needs of different market participants to effectively manage market risk should be allowed. Such a market structure will encourage competition which will foster innovation and enable specialization. Specialization is important because marketplace participants have diverse needs and objectives. By promoting competition, suppliers of marketplace services will strive to create products and services that best serve the needs of their target consumer group. In the context of financial markets this will mean that investors and traders will be able to choose those trading centers that most effectively meet their specific needs.

2. What market structure issues should be considered as part of the discussion on the trade-through obligation?

The following market structure issues should be considered:

(i) How does the trade-through obligation satisfy the best execution expectations of different classes of investor such as retail, institutional and dealers trading their inventory accounts?;

(ii) Should trade-through obligations apply only to trading by dealers as agents or to principal trading?

For the average retail investor, the concept of "best price" is generally the same as "best execution". It is appropriate that a trade-through obligation be a priority for stock exchanges like TSX and other marketplaces that want to attract retail agency orders.

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[12] See Lee, Ruben, *Capital Markets that Benefit Investors-A Survey of the Evidence on Fragmentation, Internalisation and Market Transparency*, September 30 2002

On the other hand, marketplaces that do not emphasize price priority but rather emphasize factors such as order size, type of order, or other trading features unrelated to price priority should not be subject to "trade-through" obligations across marketplaces. The historical experience in the Canadian fixed income market strongly demonstrates that specialization will reduce market risk. An equity market structure that enables specialized marketplaces to develop to better serve the risk management needs of dealers and the liquidity needs of institutional investors will improve market quality.

3. *Should the discussion about trade-throughs consider trading of non-exchange traded securities on marketplaces other than exchanges (for example, fixed income trading on more than one ATS)? If so, please identify structure issues that need to be reviewed.*

The issue has been raised squarely in the context of exchange traded securities and should be confined to that. Fixed income trading markets currently do not have a trade-through obligation and the absence of one has not been controversial. In fact, the fixed income markets have greatly benefited from the existence of the IDB marketplace which does not recognize a concept of trade-through that enables dealers to effectively manage the trading risks they incur when supplying liquidity to institutions.

4. *Please provide comments on the RS proposal regarding trade-through obligations. Which elements do you agree or disagree with and why?*

We think for the reasons provided in our introductory comments that the trade-through prohibition should only apply to agency trading by retail and other investors.

Shorcan disagrees with the view that dealers trading as principal and that institutional investors should "owe an obligation to the market". Expanding the trade-through obligation beyond a dealer's existing fiduciary responsibility as agent to pursue best price for a client order is not justified in principle and represents an "exchange-centric" view of the world and of UMIR as being based on price priority.

5. *If a trade-through obligation is imposed, what differences between Canadian and U.S. markets should be considered?*

It must be understood that even though the SEC has approved the Order Protection Rule ("OPR") in the U.S., it may never be implemented given the ongoing political opposition to the contentious SEC decision. The vote in

favour of trade-through narrowly passed by a 3 to 2 margin. Commissioners Glassman and Atkins noted in their dissent that the Commission selectively "cherry-picked statistics .....that appear to justify the adoption of a trade-through rule, while ignoring data that call the need for the rule into question".[13] Between now and expected implementation of the OPR in the 2nd half of 2006, it is not inconceivable that the original decision might be overturned.

OPR works best in a market of multiple competing stock exchanges. Canada is very different from the US in this respect. It has taken almost four years for the first highly specialised equity marketplaces to emerge in Canada. The relatively small size of the Canadian equity marketplace could not easily accommodate another conventional stock exchange to compete with the TSX. In Canada, opportunities to compete and innovate will be limited to specialised marketplaces that meet the unique needs of specific "marketplace participant" segments such as institutions, dealers or both. These are the most likely forms of future competition in Canada. If a trade-through obligation is imposed, the negative impact on competition would be fatal. Also, Shorcan believes that not enough consideration has been given to the significant technology costs which would be associated with a mandated trade-through obligation.

6. *Should trade-throughs be treated differently on derivatives markets than equity markets? Why or why not?*

Historically, derivatives marketplaces have developed separately from stock exchanges. Applying trade-through prohibitions across derivatives marketplaces does not make obvious good sense or address an obvious harm or defect in market structure.

7. *Should trade-through protection be imposed where there are multiple marketplaces trading the same securities? Why? Why not? What are the advantages and disadvantages?*

Not necessarily. The correct approach depends on the specific nature and role of the individual marketplaces trading the same securities. For example, if multiple similar marketplaces are targeting the full spectrum of retail and institutional public investors –– and also intermingling orders with dealers trading both as principal and agent (as is the case for NASDAQ, the NYSE and TSX), some form of mandated trade-through protection for customer orders may be appropriate. On the other hand, in the case of specialized marketplaces that serve a specific objective such as risk

[13] See Securities and Exchange Commission, *Dissent of Commissioners Cynthia A. Glassman and Paul S. Atkins to the Adoption of Regulation NMS*, dated June 9, 2005, pages 10 to 14.

management for dealers or block trading for institutions, factors such as trade size, market impact, anonymity, speed and certainty will be more important than price. It would be wrong to mandate trade-through protection across fundamentally different marketplaces.

8. *Will the trade-through obligation impact innovation and competition in the Canadian market? How?*

As our comments above suggest, the reach of the trade-through obligation will have a significant impact on innovation and competition in the Canadian market. The optimal outcome would be to have no mandated trade-through obligation for activity other than agency trading. Shorcan believes that the existing rules regarding a dealer's fiduciary obligations to client orders are sufficient to protect the retail investor's interest. A mandated trade-through obligation makes the arbitrary assumption that price by itself is the most important factor impacting investors' trading decisions. This does not reflect the reality of the marketplace. If the trade-through obligation is imposed on marketplaces then each marketplace will need to electronically connect to every other marketplace that trades the same underlying stock and displays pre-trade information. This would impose enormous and unnecessary technology costs which will reduce competition and innovation.

9. *Should the trade-through obligation remain an obligation owed by dealers to their clients or should all marketplace participants owe a general duty to the market?*

For reasons elaborated in our opening commentary, Shorcan's answer is YES to the former and NO to the latter. By continuing to treat any trade-through obligation as a fiduciary duty owed by dealers handling client orders, there is no need to change current UMIR. There is no evidence to substantiate that any market structure problem will emerge if the trade-through obligation is not expanded now to include all market participants.

10. *If a trade-through obligation is imposed, should the obligation be imposed on the marketplace participant or the marketplace? Why?*

NI 23-101 currently is explicit about this point and imposes the obligation on the participant and not on the marketplace.

12. *Does the absence of a data consolidator affect whether and how the trade-through obligation should be imposed?*

Yes. If the trade-through obligation is imposed indiscriminately on market participants then a data consolidator (or a consolidated market display that

shows best "bid-ask" for each marketplace) will be necessary for participants to be able to assess which marketplace they need to direct their order to avoid a trade-through. An important point that seems to be continually overlooked, in addition to the technology costs associated with imposing a trade-through obligation, is the fact that it should not be assumed that all marketplaces will be electronic only. Shorcan strongly believes that verbal trade negotiation will continue to be an integral element of servicing specialized trading needs associated with institutional block trading and inter-dealer trading for risk management purposes.

13. *Does a regime imposing a trade-through obligation need to address access fees?*

Yes. Otherwise, there is no way for market participants to quickly and easily make best "net price" assessments as to whether the trade-through obligation has been violated.

14. *If a trade-through obligation is placed on marketplace participants, what other access issues need to be addressed?*

The stated goal of NI 21-101 has always been to encourage competition between marketplaces and market participants and to allow access restrictions that are not unreasonable. The CSA understands that marketplace participants represent a diverse number of investor and trader classes with differing needs and objectives. If Canada wants a marketplace that meets the specialized needs of different marketplace participants, it will be critical to continue to recognize, as NI 21-101 does today, that universal "access" to all marketplaces by all market participants is not appropriate or in the best interests of the marketplace as a whole. For example, in the fixed income market the inter-dealer market (IDB) services dealers' need to manage trading risk and adds liquidity and efficiency to the bond markets as a whole. A trade-through obligation would be in conflict with the IDB model. In equity markets, there are several examples of specialized marketplaces that focus on the block trading needs of institutional investors such as Liquidnet, Pipeline Trading and Instinet CBX in the U.S. and BlockBook in Canada. There are sound public policy arguments to support access restrictions to specialized markets serving unique customer segments.

16. Should the solution developed to deal with trade-throughs include the ability to route sweep orders?

Shorcan believes that mandated regulation of trade-throughs that force competing marketplaces to establish connectivity with other marketplaces or write programs to enable "sweep orders" is contrary to the intent of NI 21-

101 and NI 23-101 which envisage that marketplaces not be subject to "best execution" obligations. See NI 21-101, s. 6.11 and NI 23-101, Part 4.

17. Where marketplace participants are trading on a marketplace where they do not know if their orders will match and the order book is not transparent, upon execution of an order outside the bid/ask spread of another marketplace, should the participant have to satisfy better-priced orders on other marketplaces? If so, how? Should this be restricted to visible orders?

As discussed in our introduction, if a marketplace participant is faced with a "contingent liability" to satisfy better priced interest in multiple marketplaces, they will not trade or support new marketplaces since it will always be uncertain whether their transactions can be accomplished. The result will be to limit trader/investor choice, reduce liquidity, discourage competition, and impede specialization. This is not what NI 21-101 is designed to achieve.

18. If a trade-through obligation is imposed, should it occur at, simultaneously to or immediately after execution of the inferior–priced trade? Should the model accommodate all three solutions?

If a trade-through obligation is imposed, Shorcan argues that it should be limited to agency trading. Where a trade-through obligation applies, it must accommodate all three solutions.

19. If a trade-through obligation is imposed, should it apply to all better-priced orders existing when the obligation is discharged, all better-priced pre-existing orders (at the time of execution) or should it be limited to amount of the trade at the inferior price?

We have previously discussed the dampening impact on trading that may be expected when traders are faced with uncertainty pertaining to an unknown "contingent liability" to better priced interest in other market places that may preclude execution of a block trade. The options listed above attempt to create certainty regarding the size of the "contingent liability" but none of them eliminates it completely.

20. If a trade-through obligation is imposed, should exemptions be provided for special terms orders? Which ones and why?

The answer is yes. The current list of special terms orders that already have been granted exemption from best price and trade-through obligations on TSX should be expanded to include orders where there is a minimum size requirement on another competing marketplace. That would be consistent

with the principle behind the "wide-distribution" exemption. Market participants in such marketplaces will then be free to trade on the basis of "best execution" principles without any "contingent liability" to orders on TSX. This will enable specialized marketplaces to evolve to meet the risk management and block trading needs of dealers and institutional investors. When one looks at the case of a specialized marketplace for risk management or block trading, it is critical to understand that the negotiation process, particularly pertaining to "work-ups" (known as "trade expansion protocol"("TEP") in the IDB model) requires that there be no "contingent liability" to another marketplace.

21. If a trade-through obligation is imposed, should an exemption be provided for orders for which the price or other material terms cannot be determined on order entry?

Yes because it is difficult for a trade through obligation to operate meaningfully in the context of orders that are not priced in a way that permits dealers to do the comparison they are required to make when policing trade-through.

22. If a trade-through obligation is imposed, should it include an exemption for large block trades?

Yes. Moreover, any trade-through obligation that is owed by a block trade should only be specific to the marketplace on which the block trade is being negotiated. This will eliminate the "contingent liability" problem that arises if the trade-through obligation was to apply to participants' across marketplaces (as previously discussed). The nature of a trade-through obligation should be left to individual marketplaces to decide based on how each defines its value proposition and target customer base.

23. Should the size threshold for a block trade exemption for the same security traded on multiple marketplaces be the same across marketplaces? If not, what would the impact be?

No. This decision is appropriately handled as a point of competition between marketplaces. The impact of allowing marketplaces to compete on this variable will be to increase competition and innovation and enable participants to choose the trading venue that most effectively meets their needs.

24. If a trade-through obligation is imposed, will sweep orders facilitate the execution of block orders? How?

It is important to be aware that the so-called "smart-router" technology that includes sweep order functionality that is available in the U.S. market has been developed in response to market need not mandated by regulators. For example, traditional dealers such as Goldman Sachs have developed systems to enable traders to enter an order that simultaneously clears prices on all markets that trade a stock without overtrading their order size. This technology is used by their proprietary traders and is made available to their institutional customers. Also, institutional agency brokers such as Instinet provide clients with "smart-router" technology that enables a client to disclose part of a larger order in its "electronic institutional upstairs marketplace" for block trading called CBX to try to find an institutional counterparty. The disclosed portion of the order will automatically spray out to any other marketplace where stock is offered at their limit price. This enables the client to simultaneously source liquidity across multiple marketplaces with built-in safeguards to avoid overtrading the order. These are just a few examples of the sophisticated technology platforms that dealers and software companies have developed to trade multiple markets.

25. If a trade-through obligation is imposed, should it apply to any non-visible portions of a trading book?

Proponents of trade-through often put forward the argument that an obligation encourages the placing of limit orders in the book. Although there is no hard data to support that argument, giving equal status to invisible orders on the same terms as visible orders certainly does not reward visible orders relative to "iceberg" orders. Furthermore, if a trade-through obligation is imposed, and it includes protection for "iceberg" or "reserve book" orders, it exacerbates the "contingent liability" problem previously discussed.

27. What is the impact of imposing a trade-through obligation on non-dealers?

First, it would create unnecessary and unrealistic regulatory burdens on non-dealer marketplace participants such as institutions and other "access persons". Trade-through obligations should only apply in respect of agency trading. Also, the additional regulatory cost of monitoring compliance would be imposed upon the market as a whole.

28. Does the introduction of multiple marketplaces trading the same security cause a conflict between what is needed to meet best price obligations and what is needed to meet best execution

obligations if the latter is defined as something different from best price only? How can this conflict be resolved? Is one obligation, best price or best execution more important than the other? Why? Why not?

If a trade-through obligation is imposed either across marketplaces or upon all marketplace participants, then conflict issues between best price and best execution obligations will become a serious problem. As we pointed out in previous comment letter responses,[14] best execution is a much broader, multi-dimensional concept than best price. Defining best execution in the narrow sense of best price fails to recognize the importance of other factors such as size, immediacy, market impact, certainty, risk management or dealer capital that may take precedence over price for certain types of market participants such as dealers trading as principal and institutional investors. For retail investors trading smaller orders best price and best execution likely mean the same thing. However, for participants trading blocks, the two concepts diverge and "best execution" obligations must supersede "best price" obligations.

If regulators focus too narrowly on best price, competition and specialization will suffer and the Canadian marketplace will be weaker with less innovation, diversity and investor choice. This will increase market risk and reduce market quality.

30. Should the method of trade allocation (price priority, price-time priority or some entirely different method) be the same for all marketplaces or should the marketplace be allowed to determine its own procedures for allocation of trades? Why or why not?

If the goal of regulation is to inspire competition, innovation and specialization between marketplaces to better service the varying needs of market participants, then trade allocation procedures have to be left up to each marketplace to decide. In a similar vein, marketplaces should be encouraged to compete on a full spectrum of variables such price, quality, access, anonymity, service, technology and trading hours.

31. Should the last sale price reflect trading on all marketplaces or should each marketplace have a separate last sale price? Why or why not?

Each marketplace should report details of the price, quantity and time of its last sale price. This will enable all marketplace participants, investors,

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[14] See *Shorcan's Response to OSC Concept Paper 23-402*, May 5,2005 at page 4 and see *Shorcan, Response to RS Market Integrity Notice-Request for Comments-Provisions Respecting "Off-Marketplace" Trades*, May 30, 2005 at pages 2, 3 and 4.

traders and other interested parties to assess the relevance of the various prices to their specific situation. Of course, the last sale price on the dominant marketplace (i.e. TSX) should be the standard for end of day portfolio evaluation for regulatory reporting purposes.

Should you have any questions please call the undersigned at (416) 360-2508 or James P. Magee at 416 360-2528.

Yours truly,

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