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INDEPENDENT THINKING

October 18, 2005

Members of the Canadian Securities Administrators
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- and -

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- and-

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Dear Sirs/Mesdames:

RE: Request for Comment – CSA Discussion Paper 23-403
Market Structure Developments and Trade-Through Obligations

On behalf of Canaccord Capital, please accept our comments on CSA Discussion Paper 23-403. Canaccord Capital is pleased to be able to participate in these discussions, and is aware of the importance of this particular debate and its potential impact on the structure and evolution of Canada's capital markets.

As Canada's largest independent dealer, Canaccord Capital understands competition and innovation. We firmly support innovation in our marketplaces, but do not support a two tiered regulatory system where a loophole in trade-through obligations has fostered uneven competition.

Marketplaces, buy-side firms and sell-side firms should compete under a balanced regulatory framework, which will provide the foundation upon which we build a vibrant international marketplace through perspicacious endeavour and enterprise.

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

Canaccord Capital believes that balanced regulation is required to encourage a competitive Canadian financial marketplace amongst all markets and marketplace professionals, while taking into account external factors to ensure Canada remains competitive and relevant internationally.

Canaccord Capital feels strongly that retail investors, in particular, must be recognized and protected, and we concur that pre-trade and post-trade transparency mitigates pricing volatility, providing significant value to all.

While we applaud innovation in the marketplace we do not feel that investor protection should be compromised in any fashion whatsoever, and note that complications created through minimal structural change could create additional barriers to entry through increased costs.

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

Canaccord Capital strongly supports a trade-through obligation for visible orders in all markets. Pre-trade transparency is a valuable and significant cornerstone that must be supported, not devalued.

Since the ATS rules have been put in place there has been remarkably little in the way of competition or innovation in the Canadian markets. Canaccord Capital however does not believe that this is due to over constraining rules, such as trade-through, but is more a factor of a relatively efficient, centralized, electronic auction book, and a significantly smaller capital market structure than the USA. To try to compare the multiple changes in marketplace structure brought about in the USA to those of Canada makes little sense.

While there is a general belief that the innovation in the USA has generated choice for the investor, this is not necessarily the case. For the most part the choice is taken by the Dealer, who is frequently influenced by least cost / maximum income order routing and by their ownership in a particular ECN.

It should also be noted that the frenzy to create new ECNs has long since passed, and that intense competition has forced consolidation to the point where we are again faced with a duopoly in the USA.

We believe that any issuers trading on multiple exchanges or ATS must use common symbols, regardless of whether they have multiple listings. The current trade-through problems generated by inter-listed stocks on the TSX (with 3 character symbols) and CNQ (with 4 character symbols) is something that should not occur, and should be addressed immediately.

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

Canaccord Capital feels that it is important at this point to find a considered solution to the equities markets, before considering the vagaries of other marketplaces.

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

Canaccord Capital agrees with the RS proposal regarding trade-through obligations. Canaccord Capital feels that the trade-through obligation is a duty due from all market participants, whether they be buy-side, sell-side or retail investor.

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If the CSA feels that there should be an exemption available for trade-through under extremely exceptional circumstances (such as the somewhat recent BCE trade), it should be prescriptive in nature requiring implicit approval of RS.

We understand that the issue of "access to the marketplace" may not in fact be a physical connection or membership, but that access ability through a broker/jitney relationship may be sufficient. This particular statement in UMIR must be clarified by the regulators.

We believe that the current RS interpretation of price improvement upon a trade-through considers only price and time, not size. As such, a solitary bid for 100 shares at a superior price obligates participants to adjust price on possibly tens of thousands of shares traded on another marketplace. We would urge that recent trade through incidents between the TSX Venture and CNQ on Solex and United Reef are considered. Canaccord Capital believes that the obligation imposed by RS must take size into account.

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

Canaccord Capital feels that we can look at the US markets, and, for the most part, learn from their experiences. We believe there were and are no barriers to entry in Canada, and as such, the lack of innovation and competition in our markets is perhaps more symptomatic of a smaller, centralized, well-formed, electronic marketplace structure and a lack of competitive opportunities.

It should also be noted that Canada has less corporations making up more of the marketplace, less buy-side firms, with the majority of order flow conducted through bank-owned sell-side firms. Much of the recent debate on trade-through in the USA focused on the minimal value impact that trade-throughs had on the general quality of the marketplace. In Canada with more leverage in the hands of fewer corporations, Canaccord Capital believes the results could negatively skew from the statistics derived in the USA.

Canaccord Capital feels that Canada too frequently considers the regulatory changes in the USA as being a lead generator to the Canadian regulators, and would urge broad consideration of developments in other international markets, in particular the UK and Australia given their generally more appropriate size and historic linkages.

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

Canaccord Capital believes we should focus on equity marketplaces first.

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?

As a foundation item, and as stated earlier, it should be an absolute pre-requisite that any marketplaces trading the same security are mandated to use the same symbol, regardless of whether the issuer may have multiple market listings.

Trade-through protection should be afforded to all visible orders across all markets. Trade-through protection across markets can only feasibly be accorded to price, and cannot take into consideration the time of order entry across markets.

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

Canaccord Capital does not feel that Canada would be best served by two tiered trading rules; the affirmation of a two tier system will serve to break down a cornerstone of investor confidence. We firmly do not believe the inference that trade-through protection in itself removes innovation and competition. If trade-through were to be allowed, it should be for extremely large trades with prescriptive conditions that would require implicit approval by RS.

Innovations that have been brought to bear in the USA were not derived by the application of trade-through as a significant rationale. Not all changes in the US markets have been positive; some highlights are lowering trading costs; tape rebate schemes; regulatory arbitrage; broader order handling types; speed of order handling and execution; pre-open and post-close continuous execution facilities; brokerage consolidation; reduced liquidity; increased regulatory compliance. Last but not least, innovation created significant market fragmentation; however we note that markets in the USA are currently heading back to a virtual duopoly.

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?

Canaccord Capital believes that trade-through is an obligation owed by all participants, whether they are buy-side, sell-side or markets, to the Canadian capital markets. We do however ask that there be strong consideration given to restricted access, market access fees, attribution, order types that may not translate to different marketplaces, and ease of transaction settlement.

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

Canaccord Capital feels that there should be a requirement imposed on all markets to interact with each other, since there is no question that this will be the least overall cost to achieve total linkage. While some markets may complain that this requirement would prove to be a barrier to entry, we would balance that against the higher costs of many more brokerage firms and vendors having to create routing linkage to the new marketplace entrant. Additionally it should be noted that while innovation and competition must be welcomed, they do not necessarily bring sustainability or profitability, and as such the new marketplace should bear the additional costs to assist in ensuring that they have a sound business model and solid financial backing.

11. What technology solutions exist or need to be developed if a trade-through obligation is imposed on marketplaces? What solutions exist if the obligation is imposed, instead, on marketplace participants?

As stated in 10, Canaccord Capital feels that the most appropriate obligation and linkage is between marketplaces. Stated simply there are fewer marketplaces than participants and it should therefore cost less for the markets to create efficient linkages. It could be argued that it is natural for marketplaces to be in the linkage "game", and one more link to a centralized order routing system, or links to each marketplace entrant, should be extremely achievable and more cost effective.

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

As stated in 11, Canaccord Capital feels that it would be sensible for there to be a centralized order handling service between marketplaces to ensure best execution. This service could be provided by one of the marketplaces or an independent vendor. Canaccord Capital believes that a data consolidator may naturally fall out of a trade-through protection requirement.

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

Canaccord Capital believes that there is a requirement to address access fees. While some may feel that market forces will direct access fees to an appropriate level, we would rather err on the cautious side and ensure that there is sufficient oversight to ensure that individual marketplaces cannot impose onerous access fees.

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

We feel that there has to be clarity on the issue of "marketplace access", and ask if a jitney transaction counts as sufficient access to require a participant to trade on any particular marketplace. We would again like to state that Canaccord Capital feels centralized linkages should be required of the marketplaces themselves, and that the obligation should extend to all orders.

15. If a trade-through obligation is imposed, should the obligation use a full depth-of-book approach or only a top-of-book approach?

Full depth of book should be used. All visible order volume should be accorded trade-through protection.

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

Canaccord Capital does not believe that a sweep order request would be a requirement in Canada, but would certainly support that its function may be something that should be defined in advance of any particular usefulness.

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 available on other marketplaces? If so, how? Should this be restricted to visible orders?

Canaccord Capital does not believe that the non transparent marketplace should be able to put up the cross before trading through the better priced orders. If the CSA deems that the certainty of the non-transparent transaction overrides the interests of the visible orders, we feel that the visible orders should be satisfied after the initial transaction to the order volume visible. This obligation would have to be taken on in principal by the side of the trade generating the trade-through.

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?

Ideally we believe that the trade-through obligation should be imposed before the inferior price trade. We concede in the interests of different potential execution practices that this may not always be feasible and would ask to be assured that the disadvantaged orders would be satisfied to the volume visible.

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 feel it should be imposed on all better priced pre-existing orders at the time of execution.

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

There are a number of special terms orders, such as VWAP, that should be granted exemptions.

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 an exemption should be provided for orders for which the price or other material terms cannot be determined on order entry. This view does not flow over into trading on a blind marketplace where all material terms are known on the blind order.

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

While we are inclined to state that the trade-through obligation should be the same for all, we feel that there is some room for a very prescriptive exemption to be granted on a case by case basis for extremely large transactions that might occur infrequently in Canada.

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?

We do not believe that there should be general exemptions granted on block trades, however any extremely large transaction exemption should be harmonious across all marketplaces.

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

We do not believe sweep orders will likely be required in Canada.

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

Canaccord Capital does not feel that the undisclosed volume of an order contributes to pre-trade order book transparency, and to that end do not feel that they should be protected by the trade-through obligation.

26. Should we provide the ability to opt out of routing orders to marketplaces where the better-priced order is on a manual marketplace or should the rule be drafted to apply to protect only those orders that are immediate and automatically accessible?

While this may be something that should be considered and drafted, we do not feel that it is likely that there will be a manual marketplace that we will have to consider.

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

Canaccord Capital strongly feels that there is a requirement for a uniform set of rules for all professionals, and that there should be no loopholes supporting regulatory arbitrage. Canaccord Capital does not believe a two tiered rules environment is in the interests of the Canadian capital markets, and we are confused as to how this can be categorized as a potential for innovation rather than regulatory oversight.

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

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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?

Our obligation to our customer is best execution. As yet we do not have a prescriptive interpretation for best execution, other than a general acknowledgement that price, speed and certainty of execution are three important factors. Best price at an instant in time is however an important, determinable factor within best execution.

29. How should locked or crossed markets be treated? Should procedures be set up to limit the occurrence of locked or crossed markets? If so, upon whom should the obligation be placed?

If proper linkages are put in place between marketplaces Canaccord Capital does not believe that locked and crossed markets should occur.

30. Should the method of trade allocation (price priority or 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?

Canaccord Capital believes that the fairest allocation mechanism is pure price time priority within a particular marketplace. Currently it has been left to the marketplaces to set their allocation algorithms and to date the TSX have favoured "same house" price time priority trades to the general benefit of larger brokerage firms. If marketplaces are allowed to continue determining their trade allocation algorithm there is no doubt that they will show a bias towards algorithms to attract order flow. It should be noted that there are other incentives that will be used by markets to influence order flow such as tape charges/rebates, tape discount schemes, and ownership interests.

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?

Last sale price should be determined by the last trade on any market, and should be the common gauge across all markets to interpret short sale and market stabilization rules.

In closing, we would like to once again thank you for the opportunity to add our voice to these important discussions. If you have any further questions or would like clarification on a particular point please do not hesitate to contact me.

Yours truly,
Canaccord Capital

Andrew Jappy
Executive Vice President & CIO

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