NATIONAL BANK FINANCIAL

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October 25th, 2005

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Subject: **CSA DISCUSSION PAPER 23-403**

In our letter dated September 16th,2005 we answered the first two questions contained in discussion paper and promised to answer the balance in due course Enclosed you will find the remaining answers,. We apologize for being late, however we hope you will still consider our comments.

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

   We agree with the RS proposal, especially the position taken that trade-through prohibitions **should apply to all participants and access persons**. Given that the **obligation is to the market place as a whole**, one should not care where the order came from. We should also remember that the RS proposal deals only with equities and does not attempt to impose its position on all market types or products.

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

   The US market is extremely fractured and difficult for participants to trade in. Traders want a fair and accessible alternative and that is why the ECNs, which resemble our markets, have had such success. They have been moving towards a system which resembles ours, not away from it. We should continue the course for now and see how their evolution progresses. If we need to alter our markets for theirs, we could consider that in the future.

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

   Trade-through protection should be applied to derivative markets of securities where the underlying, or cash market, has trade-through protection. Derivatives are often used as a substitute for the underlying security and could therefore allow someone to do indirectly what they would otherwise be prohibited from doing directly. That said, it may not be as easy to incorporate a consolidated trade-through rule across multiple security types. We believe that further study is needed, and if upon examination we discover that traders are in fact deliberately using derivatives just to get around the rule, some form of trade-through protection would need to be imposed.

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?*

   We view a "marketplace" as the collection of all markets where on could buy or sell a given security. For this reason, all "markets" must be subject to the same rules; otherwise trade-through protection would not work at all. While this idea should apply to US inter-listed stocks as well, we are not in a position to impose our market structure upon them.

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

   Ensuring that trade-trough obligations apply to all markets for equity products will only deter innovation aimed at getting around the rules. Assuming we agree with the rules, the loss of this kind of innovation will have no negative impact on our markets.

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?*

    Technology needs to be developed to satisfy the obligation. One could argue that the market to market link would be the most cost effective as it would necessitate the fewest number of physical and logical connections. On the other hand, new market places may be dissuaded from starting up as the cost to connect would be too high. Conversely, if the obligation were placed upon the trade vendors, it would mean that might have to hook up to all markets, even if there was no liquidity on the new market.

    The first alternative may be seen as hindering new competition while the second forces the industry to support all initiatives whether they make sense or not. We must first establish a rule including whatever restrictions might apply before finding a technological solution.

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

Access fess and rebates are, for the most part, a cost borne by the brokerage community. These fees are passed on to their clients via a commission which is intended to compensate for a variety of costs. There is rarely, if ever, a direct link between the two, and the cost structure varies by broker. Just as brokers pays different fees based upon volumes, clients pay different commissions based on volumes. For this reason it would not make sense to include fees on the trade-through restriction as it would be a moving target. Protecting prices across multiple markets will be a difficult task by itself. Adding fees to the mix would render the system unworkable.

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?

The trade through rule should apply to all orders, including the depth-of-book provided that the quotes/orders shown are **visible, accessible, and immediately executable**. That said, it should not apply to orders which do not meet these criteria.

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?

We are not sure what the difference is between "at" and "simultaneously"; however we believe that trade-through protection must be afforded to the orders that appeared in the consolidated book at the time of the first execution. We say this so as to prevent systems from entering new orders immediately after the first of a series of trades is executed before all trades which would have otherwise been protected are executed.

19 through 26

We have stated before that orders which are **visible, accessible, and immediately executable** should be afforded trade-through protection. Some special terms orders are not truly visible as the cost of the special term would not be apparent. These should be taken on a case by case basis, reviewed by RS. At the same time, block trades should take out all better priced orders which meet these criteria. What they should not do is give any kind of priority to hidden orders such as "Iceberg Orders".

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

As we have stated before, the trade-through obligation is owed to the market and therefore must be applied to all participants. Therefore the impact on non-dealers will be the same as that of dealers. They will not be able to trade through orders on the consolidated book; however their displayed limit orders will be protected.

28. Best price versus best execution

Best price is part of best execution, and while important, it is by no means the only part. But while a dealer has a best execution responsibility to its client, trade-through protection is more about protecting the orders and prices already in the book than it is about the best execution obligation vis-à-vis the incoming order.

29. How should locked or crossed markets be treated?

The systems should be set up in such a way so as to avoid locked or crossed markets. The ability to lock a market can be used by some as a means of getting around trade throughs. The rule should be clear in its intent which could prohibit locked or crossed markets, after which a technological solution could be found preventing them from occurring.

30. Should the method of trade allocation be the same for all markets?

Trade-through protection could mean many different things, two of which, price and time, were referred to in your document. While it could easily be argued that both factors should be considered in applying a trade-through rule, we believe that price is the principal factor and the only one which should be considered. If the commissions were to include every variable in determining which order was protected ahead of the next, all markets would end up, by default, being identical. This would not encourage competition or innovation. We believe that markets can compete with one and other, offering different trading systems and features while still respecting price priority. We believe that this is the appropriate place to balance the competing interests.

31. Should the last sale price reflect trading on all market places or should each market place have a separate last sale price?

Multiple last sale prices would be very confusing for the market place and confusion tends to be costly in this business. One of the benefits of trade-through protection is that you can have a single last sale price for all markets. The operative word here is price, as the price could have been set on one market and yet the actual last sale took place on a different market, but at the same price. What is important is the price, not the market on which it traded.

That said, we believe strongly that only markets which are afforded trade-through protection, that is to say, that their orders are **visible, accessible, and immediately executable,** should be allowed to set the last sale price.

Those summarize our answers to your questions. We would be pleased to answer any specific questions which you may have or provide clarification on any of the comments contained herein. Respectfully submitted;

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