

October 12, 2006

Alberta Securities Commission  
British Columbia Securities Commission  
Manitoba Securities Commission  
New Brunswick Securities Commission  
Securities Commission of Newfoundland and Labrador  
Registrar of Securities, Department of Justice, Government of the Northwest Territories  
Nova Scotia Securities Commission  
Registrar of Securities, Legal Registries Division, Department of Justice,  
Government of Nunavut  
Ontario Securities Commission  
Prince Edward Island Securities Office  
Saskatchewan Financial Services Commission  
Registrar of Securities, Government of Yukon

c/o John Stevenson, Secretary  
Ontario Securities Commission  
20 Queen Street West  
Suite 1900, Box 55  
Toronto, ON M5H 3S8

Madame Ann-Marie Beaudoin  
Directrice du secrétariat  
Autorité des marchés financiers  
800, square Victoria, 22<sup>e</sup> étage  
C.P. 246, tour de la Bourse  
Montréal, Québec H4Z 1G3

Dear Sir and Madam:

**Re: Notice of Proposed Amendments to National Instruments 21-101  
Marketplace Operation, Companion Policy 21-101CP, NI 23-101 Trading  
Rules and Companion Policy 23-101CP**

The Bank of Canada and the Department of Finance welcome the opportunity to comment on the CSA's proposal (the Proposal) to amend the ATS rules. Given our broad interest in the economic and financial welfare of Canada, and our interest in well-functioning Government of Canada securities markets in particular, we support the CSA's efforts in enhancing the efficiency and integrity of Canadian debt securities markets.

The Bank of Canada and the Department of Finance have actively supported enhanced transparency in Canadian fixed-income markets for many years. Transparency is an important component of well-functioning and efficient financial markets, supporting participation and the competitive allocation of capital. We recognize that the ongoing regulatory interest in promoting transparency has played an important role in the evolution of transparency initiatives. In Canada, private sector initiatives including the development of fixed-income ATSS have enabled further advances in transparency, engendered greater competition across liquidity providers, and led to operational efficiencies in debt securities markets.

We are pleased to see that these initiatives in Canada in recent years have enabled progress in the provision of much greater transparency to market participants. Through competition and technological innovations, the fixed income industry in Canada has seen a substantial growth in market-led transparency, delivered via alternative (electronic) trading systems (ATSS) since the initial exemption for government securities was granted in 2003. Several ATSS have been established and are now well supported by wholesale buy-side and sell-side market participants. For non-ATS users, there are several commercial data services companies, with a few recent entrants targeting small to medium size investors, offering innovative consolidation services at relatively low prices. In addition, real-time, benchmark government securities prices are available, in some cases for free, via several internet sites. These trading systems and information providers, in tandem with the dissemination of trading-related information by interdealer brokers (IDBs) to information vendors, have enabled investors and other market participants to obtain a much-improved level of transparency. Overall, the wholesale government securities market is functioning well and the majority of institutional investors see existing pricing sources as serving the market well.

Based on other jurisdictions' experiences with electronic trading and market-led data dissemination, we fully expect further gains in transparency for Canadian debt securities markets. The Bank of Canada and the Department of Finance would view a lack of future progress in market-led transparency innovations as increasing the necessity for mandated transparency standards.

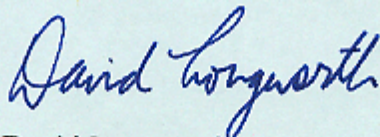
At the same time, the Bank of Canada and the Department of Finance are cognizant of the fact that the quality and attractiveness of these markets depends on the maintenance of liquidity, particularly for the government securities market. As there is only limited experience and data in Canada and in other jurisdictions, there is still an insufficient level of understanding of the trade-off between enhanced transparency and liquidity. We are concerned that tightening public dissemination standards applied broadly to all market places, even if these are phased-in, could negatively impact the current level of liquidity in the government securities market. Specifically, although we are confident that order-driven ATSS and IDBs could support a higher level of transparency than is currently required without unduly affecting market liquidity, there is insufficient evidence that this is the case for other ATSS particularly those marketplaces where trades are negotiated such as Request for Quote (RFQ) trading systems. We strongly believe that systems with

different trading structures need to have different levels of transparency in order to mitigate negative impacts on liquidity.

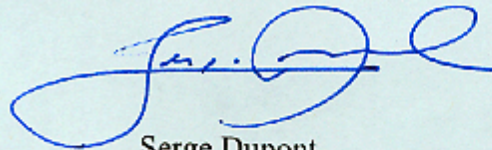
The Bank of Canada and the Department of Finance share the CSA's concerns regarding pricing and fairness of retail customer transactions in fixed-income markets. Mandatory transparency requirements alone will not resolve retail concerns and may have unintended consequences on the efficiency of wholesale debt securities markets. It is interesting to note that no other jurisdiction has extensive rules for transparency of government debt markets, but several have relied on other forms of regulation to deal with particular needs of retail investors for information and best execution.<sup>1</sup> We support the development of best execution standards and greater disclosure of the size of mark-ups and commissions related to retail debt security transactions, as these, in turn, would support greater retail participation in the debt markets. We are of the view that regulatory trade reporting obligations can be strengthened without mandating the public dissemination of trading in all wholesale debt marketplaces.

To conclude, the Bank of Canada and the Department of Finance want to see continued enhancement of transparency in the government securities market. In this regard, we would support the ongoing monitoring of transparency by regulators to ensure that there is continued progress. Given the analysis of the situation, we do not support any regulation that would apply to marketplaces (ATs or otherwise) where trades are negotiated. We support measures that would promote retail participation in the fixed income market, including the implementation of transparent mark-up and best execution policies.

Sincerely,



David Longworth  
Deputy Governor  
Bank of Canada



Serge Dupont  
Assistant Deputy Minister  
Department of Finance

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<sup>1</sup> See U.K. Financial Services Authority: *Trading Transparency in the UK Secondary Bond Markets. Feedback Statement*, July 2006, for arguments in favour of a greater reliance on stronger best-execution obligations in order to resolve retail investor protection concerns in debt markets.