



Market Regulation Services Inc.

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marché inc.

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Canadian Trading and Quotation System Inc.,
Suite 3850, P.O. Box 207,
BCE Place,
161 Bay Street,
TORONTO, Ontario.
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Attention: Timothy S. Baikie,
General Counsel & Corporate Secretary

- and -

Ontario Securities Commission,
Suite 1903, Box 55,
20 Queen Street West,
TORONTO, Ontario.
M5H 3S8

Attention: John Stevenson, Secretary

Dear Sirs and Mesdames:

**Re: Request for Comments
- Application to Vary Recognition Order of Canadian Trading and Quotation
System Inc.**

Further to the Request for Comments on the application to vary the recognition order of Canadian Trading and Quotation Systems Inc. ("CNQ") as published in the OSC Bulletin at (2005) 28 OSCB 8287, Market Regulation Services Inc. ("RS") would offer the

following comments on the proposed amendments to the rules and policies of CNQ. These comments have been restricted to the potential impact on the application of the provisions of the Universal Market Integrity Rules (“UMIR”). The variation of the recognition order of CNQ would also necessitate a number of significant changes to the Regulation Services Agreement between CNQ and RS and the manner in which RS is able to provide those services. The changes to the Regulation Services Agreement, including provisions related to the costs to be borne by CNQ in respect of the changes in services, need to be negotiated and agreed to between RS and CNQ and will be subject to approval by the Ontario Securities Commission. RS has written directly to CNQ regarding these possible changes.

Access to Order Information

The application by CNQ does not indicate whether CNQ proposes to make any changes to its practice and procedures regarding the availability of order information to marketplace participants that are not members of CNQ. RS currently understands that CNQ does not make available depth of book information except through proprietary software available to members of CNQ. Information on the best bid and best ask on CNQ is generally available.

If CNQ commences the trading of securities listed on other exchanges, RS has taken the position that Participants and Access Persons who have access to CNQ have an obligation to monitor prices available on CNQ (for best execution and best price) and trades on CNQ (for short sales and market stabilization). It is the understanding of RS that the Canadian Securities Administrators are of the view that all Participants and Access Persons trading in those securities that may be traded on the Alternative Market may also have an obligation to consider order and trade information from the Alternative Market for the purposes of complying with their obligations under UMIR or applicable securities requirements. In the view of RS, it is imperative that the availability to non-CNQ members of order and trade data for the Alternative Market be addressed and publicly disclosed prior to the approval of changes to the recognition order.

Inter-listed Securities

The definitions which are proposed for “CNQ-listed security” and “Alternative Market security” are tautological and lead to confusion over whether a security that is inter-listed with another exchange is capable of trading in the Alternative Market. If a security is listed on CNQ in accordance with CNQ Listing Policies, the security should not be eligible for trading in the Alternative Market. If a CNQ-listed security is inter-listed with another market, it should trade in utilizing the unique symbol for trading purposes assigned in accordance with Rule 10.15 of UMIR. RS would therefore suggest that Rule 11-102 provide that CNQ may designate a security as an “Alternative Market security” if the security is listed on another recognized exchange. A security would cease to qualify if the listing of the security is suspended on the other recognized exchange. (This change would clarify that the “suspension” or halt of trading in a particular security in

accordance with the rules of the other exchange for a non-regulatory purpose would not affect the ability to trade the security in the Alternative Market provided the other exchange had not suspended or delisted the security.)

Given that CNQ Rule 3 will apply in its entirety, RS does not believe that it is necessary to include in CNQ Rule 11-102 reference to a “regulatory halt”. As structured in the proposal, a security that had been designated by CNQ as “eligible” would be automatically disqualified for trading upon the imposition of the regulatory halt. However, CNQ Rule 3-102(3) would preclude trading during the halt. Upon the lifting of the halt, under the current proposal it would appear to be necessary for CNQ to “redesignate” the security before it could start trading again in the Alternative Market.

Access by Eligible Clients

CNQ Rules 11-103 and 11-104 propose to set out the circumstances under which a CNQ Dealer would be able to grant direct access to the Alternative Market to an “eligible client” of that CNQ Dealer. The “eligible client” would not have direct access to the trading of CNQ-listed securities. As a result, it may be more appropriate to tie access to the “Alternative Market” to clients of the CNQ Dealer that have “direct access” to the recognized exchange on which the Alternative Market security is listed.

Currently, the Toronto Stock Exchange and the TSX Venture Exchange are the two other exchanges which provide for “direct access”. We would suggest that it would be appropriate to allow an “eligible client” of a CNQ Dealer that has direct access to the TSX to have direct access to the Alternative Market to trade in securities listed on the TSX. Similarly, a client with direct access to the TSX V should have direct access to the Alternative Market to trade in securities listed on the TSX V. Under this formulation it would not matter whether there were slight variations in the requirements of the TSX and the TSX V or any other recognized exchange and changes in direct access rules to a particular exchange would be “automatically” adopted by CNQ (and the rules of CNQ would not have to be updated to tract every change in the “direct access” rules of other exchanges).

CNQ Rule 11-101 proposes that CNQ Rule 4-101 apply (and that rule limits access to the CNQ System). Any rule to expand access beyond what is contemplated in CNQ Rule 4-101 to cover “direct access” clients should stipulate that the expanded rule applies “notwithstanding” CNQ Rule 4-101.

RS is concerned that each marketplace may adopt different criteria for direct access by an “eligible client”. Such a situation may become practically unworkable particularly if marketplaces are required to route orders to other marketplaces in order to comply with any trade-through obligations that may be imposed. From the perspective of UMIR, the Participant through which the order is entered on a marketplace has “full” responsibility for each order entered by an “eligible client” and UMIR sets out supervision and compliance requirements in respect of such orders. As such, there may not be any business reason to establish differing requirements for each marketplace.

Last year, RS established a working group on the obligations and supervision of Access Persons and direct access clients. The recommendations of that working group will be considered as part of the overall strategic review of UMIR that is currently underway. There may be merit in considering whether the requirements for a Participant to provide “direct access” by a client to any marketplace should be uniform (and possibly incorporated into UMIR and administered by RS. Ultimately, this may assist RS in monitoring trading in a particular security by a direct access client irrespective of the marketplace on which the order is entered or the trading occurs.)

Trading Hours

CNQ is proposing that its system be open for trading in a CNQ-listed security or an Alternative Market security between 8:00 a.m. and 6:00 p.m. In Market Integrity Notice 2005-019, RS proposed a number of amendments to UMIR to accommodate the introduction of multiple marketplaces, including marketplaces that had adopted trading hours other than those used by current marketplaces. In particular, RS proposed the introduction of a “Last Sale Price Order” to facilitate trades at the last sale price on a particular marketplace (such as the “Follow-on Auction” on BlockBook or the “Special Trading Session” on the TSX.) In the view of RS, adoption to the amendments to UMIR set out in Market Integrity Notice 2005-019 are desirable prior to or concurrent with the approval to the changes in the recognition order of CNQ.

Advantage Goes with Securities Sold

We believe that CNQ Rule 11-106 is unnecessary. Rule 6.1(2) of UMIR provides that the rules of the marketplace on which the security is listed or quoted will govern clearing, settlement and entitlement questions. As such, the application of Rule 6.1(2) of UMIR should limit the application of CNQ Rule 5 (as proposed to be incorporated by clause (e) of CNQ Rule 11-101) in circumstances where special rules or directions have been issued by the marketplace on which an Alternative Market security is listed or quoted.

Foreign Currency Trading

CNQ Rule 11-107 would conflict with the requirements for the recording of prices of trades agreed to in a foreign currency that has been proposed as Policy 7.5 under UMIR and included in the package of amendments published in Market Integrity Notice 2005-012 – *Provisions Respecting “Off-Marketplace” Trades* published on April 29, 2005. We would therefore suggest that CNQ Rule 11-107 be deleted.

If you have any questions regarding this matter, please do not hesitate to contact me at (416) 646-7277.

Yours truly,

“James E. Twiss”

James. E. Twiss,
Chief Policy Counsel.

cc. Tom Atkinson, Market Regulation Services Inc.
Rosemary Chan, Market Regulation Services Inc.
Gerry Halischuk, Market Regulation Services Inc.
Maureen Jensen, Market Regulation Services Inc.