



CIRCULAR
October 29, 2003

REQUEST FOR COMMENTS

IDENTIFICATION AND ENTRY OF ORDERS AND MAINTENANCE OF RELATED RECORDS

AMENDMENTS TO ARTICLES 6312, 6376, 6377 AND 6379 OF THE RULES OF BOURSE DE MONTRÉAL INC.

Summary

The Executive Committee of Bourse de Montréal Inc. (the "Bourse") has approved amendments to articles 6312, 6376, 6377 and 6379 of the Rules of the Bourse concerning the identification and entry of orders and the maintenance of related records. The objective of the proposed amendments is to incorporate into the Rules of the Bourse clear definitions of the terms "order for the account of a customer", "order for the account of a firm" and "order for the account of a professional". Their purpose is also to clearly set the requirements regarding the information that must appear on order tickets. Finally, the proposed amendments put in place an obligation for approved participants to identify orders coming from an insider or from a significant shareholder at the time of order entry and to arrange for such information to be retained in the records relating to such orders.

Process for Changes to the Rules

Bourse de Montréal Inc. is recognized as a self-regulatory organization (SRO) by the Commission des valeurs mobilières du Québec (the "Commission"). In accordance with this recognition, the Bourse carries on activities as an exchange and as a SRO in Québec. In its SRO capacity, the Bourse assumes market regulation and broker-dealer regulation responsibilities.

The Board of Directors of the Bourse has the power to approve the adoption or amendment of various Rules and Policies of the Bourse. The Board of Directors has delegated its powers of approval of Rules and Policies to the Executive Committee. The changes are submitted to the Commission for approval.

Circular no.: 148-2003

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Comments on the proposed amendments to articles 6312, 6376, 6377 and 6379 must be submitted within 30 days following the date of publication of the present notice in the bulletin of the Commission. Please submit your comments to:

*Ms. Joëlle Saint-Arnault
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A copy of these comments shall also be forwarded to the Commission to:

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Appendices

For your information, you will find in appendices an analysis document of the proposed rule amendments as well as the proposed regulatory text. The implementation date of the proposed amendments will be determined following approval by the Commission des valeurs mobilières du Québec.



IDENTIFICATION AND ENTRY OF ORDERS AND MAINTENANCE OF RELATED RECORDS

AMENDMENTS TO ARTICLES 6312, 6376, 6377 AND 6379 OF THE RULES OF BOURSE DE MONTRÉAL INC.

I GENERAL OVERVIEW

A – Current Rules

The current Rules of Bourse de Montréal Inc. (the “Bourse”) contain certain requirements regarding the identification of orders, their entry and the maintenance of records regarding orders. Thus, we find in Article 6312 a definition of an “order for the account of a customer”. Article 6376 identifies what information must be recorded in the various fields of the trading screen in order to have the trading system of the Bourse route the orders to the market. Article 6377 sets the requirements concerning the maintenance of order records. Finally, Article 6379 requires, among other things, that orders be identified as to their origin, either as being orders for the account of a firm, of a customer or of a professional.

B – The Problem

Current Rules contain many gaps concerning the identification of orders and their entry. The first gap is that Article 6312 defines only what is meant by the term “order for the account of a customer”. There is nowhere in the Rules of the Bourse a definition of the terms “order for the account of a firm” and “order for the account of a professional”. In addition, even the current definition of what

is an “order for the account of a customer” may be confusing.

Also, the current Rules are not clear regarding the information that must appear on order tickets when such tickets must be completed.

Finally, although some derivative instruments and more particularly equity options could be used by an insider or by a significant shareholder of an issuer as an indirect means of trading on the basis of privileged information, the Rules of the Bourse are silent as to the necessity to identify orders coming from such persons.

C -- Objective

The objective of the proposed amendments is to arrange for the concepts of order for the account of a customer, of a firm or of a professional to be clearly defined in the Rules of the Bourse. Their purpose is also to clearly set the requirements regarding the information that must appear on order tickets. Finally, the proposed amendments implement an obligation for approved participants to identify any order coming from an insider or from a significant shareholder and to arrange for such information to be retained in the records relating to orders, regardless of the fact that such orders have been executed or not. The identification of orders shall therefore be done not only at the time of entry in the trading system of the Bourse, but also on any document or in any record relating to such an order.

D – Effect of proposed Rules

The proposed amendments will permit not only to clarify some concepts relating to the identification of orders but also to facilitate the application of the regulations. In addition, by requiring from the approved participants that they clearly identify orders

coming from insiders and/or significant shareholders of an issuer, the proposed amendments will allow the Bourse to better discharge itself of its market surveillance responsibilities.

II – DETAILED ANALYSIS

A – Current Rules and Proposed Rules

Article 6312-

Current Article 6312 contains a definition of what is an “order for the account of a customer”. This definition has been withdrawn from the article and pursuant to the proposed amendments, it will now be found in Article 6376 (see detailed analysis on this Article). The text of this definition has not been simply transferred. It was also subjected to a complete review because its interpretation could give way to some confusion.

Article 6376 – Identification of orders

First, the title of this Article has been modified to read “Identification of orders” instead of “Trade and Clearing Information”. This new title appears more appropriate to the Bourse since with the proposed amendments this Article will now contain various definitions which will allow approved participants to clearly identify the nature of orders received according to their origin.

In addition, the current text of Article 6376 will be entirely deleted. This text was in fact an enumeration of the information fields that must be completed in the trading system of the Bourse before an order can be transmitted to the market. However, the system is set in such a way that if either one of these fields is not completed, it is impossible for the trader to transmit his order. It is therefore more a procedure to follow than a rule.

In addition to the definition of “order for the account of a customer” transferred, with some changes, from Article 6312, the proposed amendments introduce the following new definitions in the regulations of the Bourse :

- order for the account of a professional;
- order for the account of a firm; and
- order for the account of an insider or of a significant shareholder.

Concerning the definition of what is an order for the account of a customer transferred from Article 6312, this definition has been amended by replacing in it the term “affiliated company” by “related firm”. The term “related firm” is already defined in Article 1102 of the Rules of the Bourse and in order to avoid any errors regarding of this term, a specific reference to its definition has been included at the end of Article 6376.

Article 1102 of the Rules of the Bourse defines what is a related firm as follows :

“Related Firm means a sole proprietorship, partnership or corporation which is related with an approved participant in that either of them, together with the partners and directors, officers, shareholders and employees of it, collectively have at least a 20% ownership interest in the other of them, including an interest as a partner or shareholder, directly or indirectly, and whether or not through holding companies; which carries on as a substantial part of its business that of a broker, dealer or adviser in securities or futures contracts; which deals with or has obligations to any person other than such approved participant or for obligations to any person incurred through such approved participant; and which is under the audit jurisdiction of a self-regulatory organization which is a

participant to the Canadian Investor Protection Fund.”

The use of this term appears much more appropriate to the Bourse than the term “affiliated company” which has a much broader meaning. In effect, many approved participants of the Bourse have affiliated corporations that do not carry any securities or futures contracts brokerage activities and that are not members of a self-regulatory organization participating to the Canadian Investor Protection Fund. The current definition of what is an order for the account of a customer could give way to an erroneous interpretation since it is provided therein that an order for the account of a customer does not include “...***an order entered for an account in which...an affiliated company of an approved participant...has a direct or indirect interest, other than an interest in a commission charged***”. The erroneous interpretation that could be given to this provision is that an affiliated company, whatever its field of business activity, is not, when it has a direct or indirect interest in the account for which an order is placed, a client of the approved participant and, as a consequence, the orders taken for the account of such an affiliated company could be entered and transmitted as being orders for the account of the firm. The Bourse is of the opinion that any company affiliated to an approved participant other than an entity qualifying as a “related firm”, as this term is defined in Article 1102 of the Rules of the Bourse, is a “client” and that orders coming from such an affiliated company must be identified as being orders for the account of a client.

The definition of “order for the account of a customer” has also been modified by including therein an exclusion regarding orders coming from restricted trading permit holders. Although these persons are technically “clients”, the fact that they hold a trading permit justifies the fact that, according to the Bourse, they must be considered as “professionals”. Orders coming from these persons must therefore be

identified as “orders for the account of a professional” and not as “orders for the account of a customer”.

In addition, as already mentioned, the Rules of the Bourse did not define what was meant by the terms “order for the account of a professional” and “order for the account of a firm”. The proposed amendments therefore define these terms. The addition of such definitions should allow to clarify for all approved participants the issue of order identification according to their origin and result in an easier application of the requirements related to the management of order priorities.

Another important addition to the regulations of the Bourse is the obligation for all approved participants of the Bourse to identify orders coming from insiders or from significant shareholders. Until now the Rules of the Bourse were totally silent regarding the identification of orders coming from insiders or from significant shareholders of an issuer. The transactions done by these persons are currently the subject of many discussions and consultations between the various Canadian exchanges and the principal securities commissions. These discussions and consultations aim at putting in place various mechanisms as well as an appropriate regulatory framework ensuring a quick detection of transactions done by the relevant persons and identification of situations that could justify initiating an investigation and, eventually, the assessment of sanctions by the competent authorities. The powers to impose sanctions for what concerns insider trading lies mostly in the hands of provincial securities commissions. However, Canadian exchanges have a major role to play in the prevention and the detection of such transactions because it is very often their markets that are used to commit such infractions. The Bourse, notwithstanding the fact that it is exclusively

a derivative instruments market, has also a role to play in the implementation of the necessary mechanisms. This is because derivative instruments that are traded on the Bourse and more particularly equity options can possibly be used by insiders or by significant shareholders as a diverted means to profit from privileged information to the detriment of the small investors.

The regulatory amendments proposed by the Bourse will therefore require from approved participants, when entering an order, to indicate if such an order is for the account of an insider or of a significant shareholder. This identification will be in addition to the one regarding the identification of the order as originating from a customer, a professional or a firm.

Article 6376 has therefore been drafted in order to include therein the definition of what is an “order for the account of an insider or a significant shareholder”. Accessory definitions of the terms “insider” and “significant shareholder” have also been added to Article 6376. For the purpose of these two definitions, the Bourse used a wording identical to the one that can be found in the Universal Market Integrity Rules.

Article 6377 – Keeping Records of orders

In addition to some format modifications, the amendments proposed to this Article are as follows.

First, a mention has been added to paragraphs 2 (executed orders) and 4 (unexecuted orders) to provide that records must contain the information relating to the classification of orders pursuant to the provisions of Article 6376. The purpose of this precision is to ensure that the identification of orders is made not only at the time of their entry into the trading system but also that an audit trail

of such identification is maintained in the records of approved participants.

Paragraph 4 has also been modified to set the records retention period to seven (7) years instead of five (5). This amendment allows to harmonize the retention period with those that prevail on most of the North American markets. The increase in the retention period should not result in significant additional cost for approved participants when considering the fact that most records and files are now kept in electronic format.

Secondly, a new paragraph 6 has been added regarding the information that must appear on order tickets. The Rules of the Bourse did not specify this requirement anywhere. Furthermore, rather than proceeding with an enumeration of all the required information, the Bourse deemed preferable, after analysis, to rather refer to Section 11.2 of National Instrument 23-101 entitled “Trading Rules”. This Section lists, in paragraph c), what is all the information that must appear in records of orders. The Bourse is of the opinion that order tickets must be considered as being part of order records and that consequently they are subjected to the same requirements. In addition, referring to this Instrument has two significant advantages, the first being that it is a national standard that should not cause any application and interpretation problem and the second being that if Canadian Securities Authorities decide, through this Instrument, to amend some requirements regarding the information required, the approved participants of the Bourse will be obligated to comply accordingly without the necessity for the Bourse to proceed with corresponding regulatory amendments. Finally, the Bourse has not identified in the relevant Section of the National Instrument any requirement that would be impossible to comply with because of the fact that the Bourse is a derivative instruments market. It is also important to mention that nothing

prohibits approved participants to enter any additional information considered relevant if circumstances justify it.

The last amendment made to Article 6377 concerns paragraph 7 in which a precision has been added to the effect that the exemption power of the Bourse does apply only to paragraphs 1) to 5) of the Article, the Bourse not having the power to exempt an approved participant of the requirements imposed by a National Instrument implemented by the Canadian Securities Authorities.

Article 6379 – Input of Orders

This Article has been amended to clearly specify that in the case of an order received for the account of an insider or a significant shareholder, the approved participant has the obligation to identify the order as such when entering it in the trading system.

It is important to mention that the Bourse, at the time of drafting the present analysis is currently in the process of creating the tests relating to the markers that will be used in its trading system to identify these types of orders. The fields related to such markers being optional fields, it is necessary that the Rules clearly provide that approved participants have the obligation to input the necessary information in these fields when orders coming from insiders or significant shareholders are entered.

B – Other Alternatives Considered

No other alternative was considered.

C -- Comparison with Similar Provision

The amendments proposed above will allow to further harmonize the Rules of the Bourse with the Universal Market Integrity Rules (UMIR). For that matter the Bourse referred

to UMIR to develop its amendment proposal. For example, although the terminology used is not entirely identical, the definitions proposed by the Bourse regarding the orders for the account of a customer, a professional or a firm have essentially the same meaning as the definitions appearing at the beginning of the UMIR. As far as the definitions of the terms “insider” and “significant shareholder” are concerned, the Bourse has adopted definitions identical to those that are found in UMIR. Finally, regarding the identification of orders for the accounts of insider or significant shareholders, the Bourse used a wording similar to the one that can be found in Section 6.2 of UMIR making changes necessary to reflect the fact that it is not the securities issued by the issuer itself that are traded on the market of the Bourse but rather derivative instruments having those securities as an underlying instrument.

D – Effect of proposed regulatory amendments on systems

The proposed regulatory amendments will have a certain impact on the systems of some approved participants in the sense that they will require that some supplemental fields be put in place in their files and records regarding the identification of orders coming from insiders or significant shareholders and of transactions resulting from such orders. In any event, approved participants would not have had a choice to put in place such fields since pursuant to amendments to National Instrument 23-101 that will become effective on December 31, 2003, all Canadian Brokers will be required to maintain in their records and files information relating to transactions made by insiders.

E. – Interests of Capital Markets

The Bourse is of the opinion that the proposed regulatory amendments are not

prejudicial to the public interest neither to the interest of capital markets.

On the contrary, they will allow the implementation of clear and precise criteria regarding the identification of orders. In addition, they will allow the Bourse to identify immediately upon their entry any order coming from insiders or significant shareholders and to initiate more rapidly any investigation deemed necessary when there seems to have been an inappropriate use of privileged information. Furthermore, the fact that the orders and the operations resulting therefrom are immediately identified as coming from insiders or significant shareholders should have a certain deterrence effect and contribute to minimize the possibilities that inappropriate insider trading occurs.

F – Public Interest Objective

The proposed amendments are clearly of public interest because they will not only allow to eliminate the ambiguities that existed regarding the identification of orders but they will also have a deterrent effect on insider transactions. Furthermore, the order identification criteria being clearly set, it should result in a better capacity for the approved participants of the Bourse to manage order priority and thus ensure a stricter application of the rule which concerns the priority that must be given to clients' orders.

The proposed Rule will not create discrimination between clients, issuers, brokers, dealers, approved participants or other persons. It will not impose a useless or inappropriate burden on competition.

III -- COMMENTS

A – Filing in Other Jurisdictions

The proposed amendments will be filed with the Commission des valeurs mobilières du Québec for approval and to the Ontario Securities Commission for information.

C -- Process

The first step of the approval process for the regulatory amendments discussed in this document consists in having these amendments approved by the Executive Committee of the Bourse. Such approval was given by the Committee on October 27, 2003. Once such approval obtained, the proposed amendments are simultaneously published for a thirty (30) day comment period and submitted to the Commission des valeurs mobilières du Québec for approval.

IV -- SOURCES

- Articles 1102 and 1103 of the Rules of Bourse de Montréal Inc.
- Articles 6312, 6376, 6377 and 6379 of the Rules of Bourse de Montréal Inc.
- Universal Market Integrity Rules – Section 1.1 “Definitions” and Section 6.2 “Designations and identifier”
- National Instrument 23-101 – “Trading Rules”, Section 11.2 on the recording or creation of an order.

6312 ~~Members' Customers' Orders Have Priority~~
(10.10.91, 16.12.93, 00.00.03)

An ~~member~~ approved participant must ~~shall~~ give priority to orders for the accounts of its customers ~~of the member~~ over all other orders that the ~~member~~ approved participant holds for the same security or derivative instrument at the same price.

~~—————"Order for the account of a customer" means an order for a security entered for the account of a customer of any member or of an affiliated company of a member, but shall not include an order entered for an account in which a member, an affiliated company of a member, or an approved person has a direct or indirect interest, other than an interest in a commission charged.~~

6376 Order Identification
~~Trade and Clearing Information~~
(25.09.00, 24.09.01, 29.10.01, 00.00.03)

~~The input of an order in the system shall include the fields described below :~~

- ~~—— date~~
- ~~—— contract symbol~~
- ~~—— quantity~~

- ~~—— price~~
- ~~—— according to the derivative instrument type, delivery or expiry month and year~~
- ~~—— nature of transaction (buyer, seller)~~
- ~~—— account type (client, firm, pro)~~
- ~~—— transaction type (Hedger, Speculator) if applicable to the derivative instrument~~
- ~~—— opening/closing~~

Approved participants must ensure the proper identification of orders when entered into the trading system in order to ensure compliance with the provisions of article 6374 regarding management of priorities.

- a) “Order for the account of a customer” means an order for a security or a derivative instrument entered for the account of a customer of any approved participant or of a customer of a related firm of an approved participant, but does not include an order entered for an account in which an approved participant, a related firm of an approved participant, a person approved by the Bourse or a restricted trading permit holder has a direct or indirect interest, other than an interest in a commission charged;
- b) “Order for the account of a professional” means an order for a security or a derivative instrument for an account in which a director, officer, partner, employee or agent of an approved participant or of a related firm of the approved participant, a person approved by the Bourse or a restricted trading permit holder has a direct or indirect ownership interest. The Bourse may designate any order as being an order for the account of a professional if, in its opinion, circumstances justify it;
- c) “Order for the account of the firm” means an order for a security or a derivative instrument for an account in which the approved participant or a related firm of the approved participant has a direct or indirect ownership interest;

d) “Order for an insider or significant shareholder” means an order for a security or a derivative instrument for the account of a client, a professional or a firm who is an insider and/or significant shareholder of the issuer of the underlying security which is the subject of the order. If such client, professional or firm is both an insider and a significant shareholder, the significant shareholder designation must be used.

For the purposes of this article :

“insider” means a person who is an insider, pursuant to applicable securities legislation, of the issuer of the security underlying the security or the derivative instrument traded;

“significant shareholder” means any person holding separately, or jointly with other persons, more than 20 per cent of the outstanding voting securities of the issuer whose security is underlying the security or the derivative instrument traded.

“related firm” has the meaning given to that term in the definitions in article 1102 of the Rules of the Bourse.

6377 Keeping Records of Orders

(25.09.00, 24.09.01, 29.10.01, 00.00.03)

- 1) With the exception of ~~market-maker~~ orders transmitted by a market marker to comply with obligations required by his role and responsibilities, a record must be kept by each approved participant ~~and restricted permit holder, in its office,~~ of each order received for the purchase or sale of securities or derivatives instruments traded on the Bourse.
- 2) The record of each order filled must ~~show~~ indicate the person who ~~received~~ receiving the order, the time the order ~~was~~ is entered, the price, ~~paid or received, to the extent feasible~~ the time of execution of the order, its classification pursuant to the provisions of article 6376, the ~~broker~~ approved participant from or to or through whom the security or derivative instrument traded on the Bourse was ~~bought~~ purchased or sold and such record must be retained for ~~five~~ seven years.
- 3) No order can be executed on the trading system of the Bourse's ~~electronic trading system~~ until it has been identified as above ~~in the office of~~ by the approved participant who received the order.

All orders for securities or derivatives instruments traded on the Bourse must be time-stamped.

- 4) The record of each order, which remains unfilled, must ~~show~~ indicate the person ~~receiving~~ who received the order, ~~and its~~ and its time of receipt and its classification pursuant to the provisions of article 6376 and such record must be retained for ~~five~~ seven years.
- 5) All telephone conversations related to trading in derivative instruments listed on the Bourse must be recorded. The following conditions apply:
 - i) Recordings must be kept by Approved Participants for a period of one year.
 - ii) Authorization to consult the recordings of telephone conversations shall be granted in the case of an investigation by the Bourse, the Commission des valeurs mobilières du Québec or by any other regulatory body with which the Bourse has concluded an information sharing agreement;

- iii) In the case of litigation or in disciplinary matters, the recording may be filed as evidence;
- iv) Approved participants must advise their clients of the recording process of telephone conversations and abide by the provisions of article 7452 of Rule 7.

6) If an order ticket is completed, it must comply, for what concerns the information that must be entered on it, with the requirements of Section 11.2 of National Instrument 23-101 regarding Trading Rules.

7) Exceptionally, the Bourse may grant exemptions from all or any part of the ~~above~~ requirements set in paragraphs 1) to 5) above.

6379 Input of Orders
(25.09.00, 24.09.01, 29.10.01)

Except as provided in paragraph b) of article 6375 b), the market orders and limit orders are ~~input by~~ entered into the ~~electronic~~ trading system and presented to the market without delay in accordance with the chronology of their receipt. The other orders are presented to the market as soon as their time limit or triggering limit is reached.

Any order which is entered into the ~~electronic~~ trading system must indicate if the order is for the account of a ~~be identified by "firm," or "of a client" or "of a Professional", as these terms are defined in article 6376 for derivatives instruments.~~ In addition, if the order is for the account of an insider or of a significant shareholder, as these terms are defined in article 6376, it must be identified as such. ~~which will eventually be executed and by the identification of the final receiver of these derivatives instruments.~~ When these conditions are fulfilled, the input in the system triggers the recording of the order. Should the final receiver fail to be identified directly in the system, a time-stamped recording in accordance with article 6377 of the Rules must be completed.

If a chronological ranking of receipt cannot be established between many orders, the client priority rules of article 6374 of the Rules apply.