13.1.3 RS Market Integrity Notice – Notice of Amendment Approval – Provisions Respecting Manipulative and Deceptive Activities

April 1, 2005

NOTICE OF AMENDMENT APPROVAL

PROVISIONS RESPECTING MANIPULATIVE AND DECEPTIVE ACTIVITIES

Summary

Effective April 1, 2005, the Alberta Securities Commission, British Columbia Securities Commission, Manitoba Securities Commission, Ontario Securities Commission and, in Quebec, the Autorité des marchés financiers (the "Recognizing Regulators") approved a series of revised amendments to the Universal Market Integrity Rules ("UMIR") and the Policies to vary the requirements related to manipulative and deceptive activities by:

- modifying the language to achieve greater clarity and consistency;
- providing for consistency with the requirements related to manipulative and deceptive activities under National Instrument 23-101 ("Trading Rules") and applicable securities legislation;
- confirming the "gatekeeper" obligations of Participants and Access Persons;
- introducing a specific requirement to report to RS significant violations of UMIR; and
- eliminating potential gaps that may be caused by the current rule which combines both manipulative "effects" and "methods" in a single requirement.

RS published the initial version of the proposed amendments in Market Integrity Notice 2004-003 issued on January 30, 2004. On August 13, 2004, RS republished a revised version of the proposed amendments in Market Integrity Notice 2004-017 (the "Revised Proposal")

Summary of Changes to the Revised Proposal

Based on comments received in response to the Request for Comments contained in Market Integrity Notice 2004-017 and based on comments received from the Recognizing Regulators, RS made a number of changes to the Revised Proposal. The changes to the Revised Proposal are set out in Appendix "B". The following is a summary of the significant changes to the Revised Proposal:

- ***"Ought Reasonably to Know"***

  RS initially included reference to "generally accepted industry practice" to indicate that a particular Participant would not be held to a standard which exceeded the normal practice of the industry. A number of commentators noted that there was not a readily acceptable reference point for the industry standard. RS therefore deleted this portion of the interpretation and will rely instead on a formulation based on the common law which has been adopted as a standard in most corporate statutes.

- ***Trading Between Accounts Under Common Direction or Control***

  The proposed provision prohibiting a trade between accounts under the direction or control of the same person (other than an internal cross) has been moved from Part 1 of Policy 2.2 to Part 2. With this change, such a trade would only be prohibited if the trade creates or could reasonably be expected to create a false or misleading appearance of trading activity or interest or an artificial price.

- ***Reliance on Information***

  Part 5 of Policy 7.1 has been expanded to confirm that a Participant will be able to rely on information contained on a "New Client Application Form" or similar know-your-client record provided the information has been reviewed periodically in accordance with requirements of securities legislation or a self-regulatory entity and any additional practices of the Participant.

- ***"Gatekeeper" Obligations***

  The amendments changed the Revised Proposal by deleting a number of the rules for which a report of a violation of UMIR would be required. As a result of the changes, a report is not required if there is a violation of Rule 3.1 (respecting short sales), Rule 6.3 (respecting order exposure), Rules 7.7 and 7.8 (respecting market stabilization and market balancing) and Rule 8.1 (respecting client-principal trading). RS deleted these rules based, in part, on the existence of monitoring tools available to RS to detect violations of these rules.

  The amendments also clarified that a report was not required to be made to RS at the stage of a "review" undertaken as part of the ordinary supervision and compliance function. However, any possible violation detected as part of such review is expected to become the subject of a more formal investigation by the Participant or Access Person. The amendments also clarified that RS did not expect a report unless an investigation by the Participant or Access Person concludes that, after diligent investigation, a violation of one of the enumerated rules of UMIR has occurred. Nonetheless, RS would encourage a Participant or Access Person to report "possible violations".

  The amendments added a provision to the Policies which confirms that a Participant or Access Person must conduct further investigation or review if the Participant or Access Person has reason to believe that there may have been a violation of one of the enumerated Rules. A Participant or Access Person can not ignore "red flags" which may be indicative of improper behaviour by a client, director, officer, partner or employee of the Participant, Access Person or related entity.

Summary of the Amendments as Approved

The following is a summary of the most significant aspects of the amendments to UMIR related to the provisions on manipulative and deceptive trading:

- ***Changes to Rule 1.1 - Definition of "Requirement"***

  The definition of "Requirement" has been expanded to include "securities legislation". In accordance with the Marketplace Operation Instrument, Marketplace Rules must contain a provision that requires compliance with securities legislation. Since an ATS can not have rules, the expansion of the definition under UMIR ensures that trades undertaken through an ATS are subject to the same requirements as a trade through an Exchange or QTRS. While RS investigates possible breaches of securities legislation, RS refers these matters to the applicable securities regulatory authority for disciplinary or enforcement action.

- ***Changes to Rule 2.2 and Policies 2.2 – Manipulative and Deceptive Activities***

  Previously, Rule 2.2 prohibited a Participant or Access Person from using any manipulative or deceptive method of trading which created or could reasonably be expected to create a false or misleading appearance of trading activity or an artificial price. The amendments separated these prohibitions into two separate provisions. The first is a prohibition on the use of a manipulative or deceptive method of trading (irrespective of whether the use of the method creates a false or misleading appearance of trading activity or an artificial price). The second prohibits the entry of an order or the execution of a trade if the person knows or ought reasonably to know that the result would be to create a false or misleading appearance of trading activity or an artificial price.

  The amendment also clarifies that the entry of an order could be prohibited even though the order does not trade as the entry of the order could create a false or misleading appearance of interest in the purchase or sale of the security or an artificial ask price or bid price.

  The amendments also confirm that orders entered or trades made by a person in accordance with Market Maker Obligations imposed by Marketplace Rules will not be considered to be a violation of manipulative or deceptive trading restrictions. In this way, trades or orders which are automatically generated by the trading system of a marketplace will not be prohibited. However, the entry of orders or the execution of trades which are not required to fulfill Market Maker Obligations may violate the prohibitions on manipulative or deceptive trading.

  The amendments move the specific examples of prohibited activities from the Rules to the Policies to be consistent with the structure of other rules in UMIR. The amendments also expand the list of specific examples to include a prohibition on entering orders without the reasonable expectation of making settlement of the resulting trade. (The provision does not require that the dealer make a "positive affirmation" that it has

the ability to settle the trade but merely have a "reasonable expectation".) The Trading Rules contain comparable prohibitions for trading which is not subject to UMIR.

- ***Introduction of Rule 2.3 – Improper Orders and Trades***

  The changes introduce a new provision that prohibits the entry of an order or the execution of a trade if the Participant or Access Person knew or ought to have known that the order or trade would not be in compliance with various regulatory requirements. For example, if a Participant knows or ought to know that a client is entering an order for a security based on undisclosed material information related to that security (which action by the client would be contrary to securities legislation), the Participant would itself be violating the requirements of UMIR.

  If the Participant or Access Person did not have any reason to believe that there would be a failure to comply with any of the requirements of securities legislation, requirements of a self-regulatory entity, Marketplace Rules or UMIR there would not be a violation of Rule 2.3. As a self-regulatory entity, part of the mandate of RS is to ensure that the persons who are subject to its jurisdiction conduct trading openly and fairly in accordance with just and equitable principles of trade. This standard is incorporated directly into UMIR in Rule 2.1. Any person who knowingly breaches requirements of various entities regarding the trading of securities could not be said to be conducting transacting business "openly and fairly". Rule 2.3 is simply a specific statement of this general requirement.

- ***Changes to Rule 7.1 and Policy 7.1 – Trading Supervision Obligation***

  One of the amendments to Policy 7.1 clarifies that the supervision obligation imposed on a Participant by Rule 7.1 exists irrespective of the source of the order or the means by which the order is transmitted to a marketplace. The amendment specifically requires the supervision policies and compliance procedures to take into account the additional difficulties faced by Participants if there is direct order entry by clients.

  An additional change to Policy 7.1 requires a Participant that has detected a violation or possible violation of a Requirement to address whether additional supervision is appropriate or whether their policies and procedures should be amended to reduce the possibility of a similar future violation.

  The amendments require the supervisory system adopted by a Participant to specifically address several matters related to manipulative and deceptive activities. In particular, a Participant would be expected to have procedures to:

  - determine whether orders are being entered by insiders or other persons with an "interest" in affecting the price of a security;
  - monitor trading activity by persons with multiple accounts;
  - implement additional compliance procedures in circumstances when the Participant is unable to verify certain information regarding an account (e.g. the ultimate beneficial ownership of the account unless that information was otherwise required by applicable regulatory requirements); and
  - address the additional risks resulting from the fact that efforts to manipulate a security are more likely to:
    - occur at the end of a calendar month or on the expiry of derivatives; or
    - be centred on illiquid securities.

- ***Changes to Rule 10.4 – Extension of Restrictions***

  The amendment to Rule 10.4 is consequential on the changes in terminology used in Rule 2.2 and the introduction of Rule 2.3. As such, various persons including directors, officers and employees of a Participant or an Access Person are prohibited from the entry of an order or the execution of a trade which such person knows or ought to know does not comply with regulatory requirements.

- ***Introduction of Rule 10.16 and Policy 10.16 – Gatekeeper Obligations of Directors, Officers and Employees of Participants and Access Persons***

  The amendment introduces a specific rule related to the "gatekeeper" obligations imposed on a Participant or Access Person and their respective directors, officers and employees. These persons would be expected to act on "red flags" which may be indicative of possible improper behaviour and to report activity which may be a violation of enumerated integrity rules to their respective supervisor or compliance department. In turn, the supervisor or compliance department would be expected to make a written record of the report and to investigate the report and record the relevant findings, and where appropriate, inform the Market Regulator.

  While RS would encourage a Participant or Access Person to report "possible violations", RS will require a report only if the Participant or Access Person concludes after due investigation that a violation of one of the enumerated Rules has occurred. The report by a Participant or Access Person to RS of a violation of one of the enumerated Rules:

  - should be made a soon a practicable, and in any event, not later than the 15th day of the month following the month in which the Participant or Access Person make the findings of its investigation; and

  - should be in the form of an e-mail addressed to reports@rs.ca and a copy of the written record of the findings of the investigation by the Participant or Access Person is attached to the e-mail.

  If an electronic submission can not be provided, the report may be faxed to RS: Market Regulation Eastern Region – 416.646.7261; or Market Regulation Western Region – 604.602.6986.

  While this type of "gatekeeper" obligation may have been implied in the conduct of the affairs of market participants, the amendment specifically sets out the standard in the form of a rule and identifies the rules to which this obligation applies.

Summary of the Impact of the Amendments

As a result of the approval of the amendments:

- Participants are required to review and revise their policies and procedures to specifically address:
  - the introduction of the gatekeeper obligation with its attendant obligation to conduct internal reviews and investigations into possible violations of UMIR, to maintain records of all reviews and investigations and to report findings of potential violations; and
  - certain identified fact situations where manipulative and deceptive activities are most likely to occur.
- Access Persons are required to adopt policies and procedures to accommodate the introduction of a more limited gatekeeper obligation applicable to an Access Person.
- Trades between accounts under the direction or control of the same person may not be completed on a marketplace if the purpose of the trade is to create a false or misleading appearance of investor interest or trading activity or to create an artificial price.
- A new rule specifically prohibits the entry of an order or the execution of a trade in circumstances where the Participant or Access Person knew or ought to have known that the order or trade would not be in compliance with various regulatory requirements. The application of this new rule is extended to directors, officers and employees of the Participant or Access Person and other related persons by the amendments to Rule 10.4.

Text of the Amendment

The amendments to the Rules and Policies respecting manipulative and deceptive activities are effective as of April 1, 2005. The text of the amendments is set out in Appendix "A".

Responses to the Request for Comments

RS received seven comment letters in response to the Request for Comments on the proposed amendments set out in Market Integrity Notice 2004-017. RS also conducted a consultation meeting regarding the Revised Proposal on September 29, 2004. The comments and the response of RS are summarized in Appendix "B". Appendix "B" also contains the text of the relevant

provisions of the Rules and Policies as the provisions read following the adoption of the amendments. This text has been marked to indicate changes from the Revised Proposal set out in Market Integrity Notice 2004-017.

Questions

Questions concerning this notice may be directed to:

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Appendix "A"

Universal Market Integrity Rules

Amendments to the Rules and Policies
Related to Manipulative and Deceptive Activities

The Universal Market Integrity Rules are amended as follows:

1. Rule 1.1 is amended by adding the following as clause (f) of the definition of "Requirements":

   (f) securities legislation.

2. Part 2 of the Rules is amended by deleting the phrase "Manipulative or Deceptive Method of Trading" in the heading and substituting the phrase "Abusive Trading".

3. Rule 2.2 is deleted and the following substituted:

   Manipulative and Deceptive Activities

   (1) A Participant or Access Person shall not, directly or indirectly, engage in or participate in the use of any manipulative or deceptive method, act or practice in connection with any order or trade on a marketplace if the Participant or Access Person knows or ought reasonably to know the nature of the method, act or practice.

   (2) A Participant or Access Person shall not, directly or indirectly, enter an order or execute a trade on a marketplace if the Participant or Access Person knows or ought reasonably to know that the entry of the order or the execution of the trade will create or could reasonably be expected to create:

      (a) a false or misleading appearance of trading activity in or interest in the purchase or sale of the security; or

      (b) an artificial ask price, bid price or sale price for the security or a related security.

   (3) For greater certainty, the entry of an order or the execution of a trade on a marketplace by a person in accordance with the Market Maker Obligations shall not be considered a violation of subsection (1) or (2) provided such order or trade complies with applicable Marketplace Rules and the order or trade was required to fulfill applicable Market Maker Obligations.

4. Part 2 of the Rules is amended by adding the following as Rule 2.3:

   Improper Orders and Trades

   A Participant or Access Person shall not enter an order on a marketplace or execute a trade if the Participant or Access Person knows or ought reasonably to know that that the entry of the order or the execution of the trade would not comply with or would result in the violation of:

   (a) applicable securities legislation;

   (b) applicable requirements of any self-regulatory entity of which the Participant or Access Person is a member;

   (c) the Marketplace Rules of the marketplace on which the order is entered;

   (d) the Marketplace Rules of the marketplace on which the trade is executed; and

   (e) the Rules and Policies.

5. Clause (2)(a) of Rule 7.1 is amended by inserting the phrase ", acceptance" after the word "review".

6. Rule 10.4 is amended:

(a) in clause (1)(a) by inserting the phrase "2.3," after "2.2" and by deleting the phrase "method of trading" and substituting the word "activities"; and

(b) in clause (2)(a) by inserting the phrase ", 2.3" after "2.2" and by deleting the phrase "method of trading" and substituting the word "activities".

7. Part 10 of the Rules is amended by inserting the following as Rule 10.16:

Gatekeeper Obligations of Directors, Officers and Employees of Participants and Access Persons

(1) An officer, director, partner or employee of a Participant shall forthwith report to their supervisor or the compliance department of the Participant upon becoming aware of activity in a principal, non-client or client account of the Participant or a related entity that the officer, director, partner or employee believes may be a violation of:

(a) Subsection (1) of Rule 2.1 respecting just and equitable principles of trade;

(b) Rule 2.2 respecting manipulative and deceptive activities;

(c) Rule 2.3 respecting improper orders and trades;

(d) Rule 4.1 respecting frontrunning;

(e) Rule 5.1 respecting best execution of client orders;

(f) Rule 5.2 respecting best price obligation;

(g) Rule 5.3 respecting client priority;

(h) Rule 6.4 respecting trades to be on a marketplace; and

(i) any Requirement that has been designated by the Market Regulator for the purposes of this subsection.

(2) An officer, director, partner or employee of an Access Person shall forthwith report to their supervisor or the compliance department of the Access Person upon becoming aware of activity by the Access Person or a related entity that the officer, director, partner or employee believes may be a violation of:

(a) Subsection (2) of Rule 2.1 respecting conduct of business openly and fairly;

(b) Rule 2.2 respecting manipulative and deceptive activities;

(c) Rules 2.3 respecting improper orders or trades; and

(d) any Requirement that has been designated by the Market Regulator for the purposes of this subsection.

(3) If a supervisor or compliance department of a Participant or Access Person receives a report pursuant to subsection (1) or (2), the supervisor or compliance department shall diligently conduct a review in accordance with the policies and procedures of the Participant adopted in accordance with Rule 7.1 or in accordance with the ordinary practices of the Access Person.

(4) If the review conducted by the supervisor or compliance department concluded that there may be a violation, the supervisor or compliance department shall:

(a) make a written record of the report by the officer, director, partner or employee and the review conducted in accordance with subsection (3);

(b) diligently investigate the activity that is the subject of the report and review;

(c) make a written record of the findings of the investigation; and

(d) report the findings of the investigation to the Market Regulator if the finding of the investigation is that a violation of an applicable Rule has occurred and such report shall be made not later than the 15th day of the month following the month in which the findings are made.

(5) Each Participant and Access Person shall with respect to the records of the report, the review and the findings required by subsection (4):

(a) retain the records for a period of not less than seven years from the creation of the record; and

(b) allow the Market Regulator to inspect and make copies of the records at any time during ordinary business hours during the period that such record is required to be retained in accordance with clause (a).

(6) The obligation of a Participant or an Access Person to report findings of an investigation under subsection (4) is in addition to any reporting obligation that may exist in accordance with applicable securities legislation, the requirements of any self-regulatory entity and any applicable Marketplace Rules.

The Policies under Universal Market Integrity Rules are amended as follows:

1. The following is added as Policy 1.2:

Part 1 – "Ought Reasonably to Know"

Rule 2.2 prohibits a Participant or Access Person from doing various acts if the Participant or Access Person "knows or ought reasonably to know" that a particular method, act or practice was manipulative or deceptive or that the effect of entering an order or executing a trade would create or could reasonably be expected to create a false or misleading appearance of trading activity or interest or an artificial price. Rule 2.3 prohibits a Participant or Access Person from entering an order on a marketplace or executing a trade if the Participant or Access Person "knows or ought reasonably to know" that the entry of the order or the execution of the trade would result in the violation of various securities or regulatory requirements.

In determining what a person "ought reasonably to know" reference would be made to what a Participant or Access Person would know, acting honestly and in good faith, and exercising the care, diligence and skill that a reasonably prudent Participant or Access Person would exercise in comparable circumstances. In essence, the test becomes what could a Participant or Access Person have been expected to know if the Participant or Access Person had:

- adopted various policies and procedures as required by applicable securities legislation, self-regulatory entities and the Rules and Policies; and
- conscientiously followed or observed the policies and procedures.

Part 2 Applicable Regulatory Standards

Rule 7.1 requires each Participant prior to the entry of an order on a marketplace to comply with applicable regulatory standards with respect to the review, acceptance and approval of orders. Each Participant that is a dealer must be a member of a self-regulatory entity. Each Participant will be subject to the by-laws, regulations and policies as adopted from time to time by the applicable self-regulatory entity. These requirements may include an obligation on the member to "use due diligence to learn and remain informed of the essential facts relative to every customer and to every order or account accepted." While knowledge by a Participant of "essential facts" of every customer and order is necessary to determine the suitability of any investment for a client, such requirement is not limited to that single application. The exercise of due diligence to learn essential facts "relative to every customer and to every order" is a central component of the "Gatekeeper Obligation" embodied within the trading supervision obligation under Rule 7.1 and 10.16. In addition, securities legislation applicable in a jurisdiction may impose review standards on Participants respecting orders and accounts. The regulatory standards that may apply to a particular order may vary depending upon a number of circumstances including:

- the requirements of any self-regulatory entity of which the Participant is a member;
- the type of account from which the order is received or originated; and

the securities legislation in the jurisdiction applicable to the order.

2. Part 1 of Policy 2.2 is deleted and the following substituted:

Part 1 – Manipulative or Deceptive Method, Act or Practice

There are a number of activities which, by their very nature, will be considered to be a manipulative or deceptive method, act or practice. For the purpose of subsection (1) of Rule 2.2 and without limiting the generality that subsection, the following activities when undertaken on a marketplace constitute a manipulative or deceptive method, act or practice:

(a) making a fictitious trade;

(b) effecting a trade in a security which involves no change in the beneficial or economic ownership;

(c) effecting trades by a single interest or group with the intent of limiting the supply of a security for settlement of trades made by other persons except at prices and on terms arbitrarily dictated by such interest or group; and

(d) purchasing a security with the intention of making a sale of the same or a different number of units of the security or a related security on a marketplace at a price which is below the price of the last sale of a standard trading unit of such security displayed in a consolidated market display.

If persons know or ought reasonably to know that they are engaging or participating in these or similar types of activities those persons will be in breach of subsection (1) of Rule 2.2 irrespective of whether such method, act or practice results in a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security or a related security.

3. Policy 2.2 is amended by adding the following Parts:

Part 2 – False or Misleading Appearance of Trading Activity or Artificial Price

For the purposes of subsection (2) of Rule 2.2 and without limiting the generality of that subsection, if any of the following activities are undertaken on a marketplace and create or could reasonably be expected to create a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price, the entry of the order or the execution of the trade shall constitute a violation of subsection (2) of Rule 2.2:

(a) entering an order or orders for the purchase of a security with the knowledge that an order or orders of substantially the same size, at substantially the same time and at substantially the same price for the sale of that security, has been or will be entered by or for the same or different persons;

(b) entering an order or orders for the sale of a security with the knowledge that an order or orders of substantially the same size, at substantially the same time and at substantially the same price for the purchase of that security, has been or will be entered;

(c) making purchases of, or offers to purchase, a security at successively higher prices or in a pattern generally of successively higher prices;

(d) making sales of or offers to sell a security at successively lower prices or in a pattern generally of successively lower prices;

(e) entering an order or orders for the purchase or sale of a security to:

(i) establish a predetermined sale price, ask price or bid price,

(ii) effect a high or low closing sale price, ask price or bid price, or

(iii) maintain the sale price, ask price or bid price within a predetermined range;

(f) entering an order or a series of orders for a security that are not intended to be executed;

(g) entering an order for the purchase of a security without, at the time of entering the order, having the ability or the reasonable expectation to make the payment that would be required to settle any trade that would result from the execution of the order;

(h) entering an order for the sale of a security without, at the time of entering the order, having the reasonable expectation of settling any trade that would result from the execution of the order; and

(i) effecting a trade in a security, other than an internal cross, between accounts under the direction or control of the same person.

If persons know or ought reasonably to know that they are engaging or participating in these or similar types of activities those persons will be in breach of subsection (2) of Rule 2.2 irrespective of whether such activity results in a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security or a related security.

Part 3 – Artificial Pricing

For the purposes of subsection (2) of Rule 2.2, an ask price, bid price or sale price will be considered artificial if it is not justified by real demand or supply in a security. Whether or not a particular price is "artificial" depends on the particular circumstances.

Some of the relevant considerations in determining whether a price is artificial are:

(a) the prices of the preceding trades and succeeding trades;

(b) the change in the last sale price, best ask price or best bid price that results from the entry of the order on a marketplace;

(c) the recent liquidity of the security;

(d) the time the order is entered and any instructions relevant to the time of entry of the order; and

(e) whether any Participant, Access Person or account involved in the order:

(i) has any motivation to establish an artificial price, or

(ii) represents substantially all of the orders entered or executed for the purchase or sale of the security.

The absence of any one or more of these considerations is not determinative that a price is or is not artificial.

4. Part 1 of Policy 7.1 is amended by adding the following at the end:

The obligation to supervise applies whether the order is entered on a marketplace:

- by a trader employed by the Participant,
- by an employee of the Participant through an order routing system,
- directly by a client and routed to a marketplace through the trading system of the Participant, or

- by any other means.

In performing the trading supervision obligations, the Participant will act as a "gatekeeper" to help prevent and detect violations of applicable Requirements.

Where an order is entered on a marketplace without the involvement of a trader (for example by a client with a systems interconnect arrangement in accordance with Policy 2-501 of the Toronto Stock Exchange), the Participant retains responsibility for that order and the supervision policies and procedures should adequately address the additional risk exposure which the Participant may have for orders that are not directly handled by staff of the Participant. For example, it may be appropriate for the Participant to sample for compliance testing a higher percentage of orders that have been entered directly by clients than the percentage of orders sampled in other circumstances.

In addition, the "post order entry" compliance testing should recognize that the limited involvement of staff of the Participant in the entry of orders by a direct access client may restrict the ability of the Participant to detect orders that are not in compliance with specific rules. For example, "post order entry" compliance testing may be focused on whether an order entered by a direct access client:

- has created an artificial price contrary to Rule 2.2;
- is part of a "wash trade" (in circumstances where the client has more than one account with the Participant);
- is an unmarked short sale (if the trading system of the Participant does not automatically code as "short" any sale of a security not then held in the account of the client); and
- has complied with order marking requirements and in particular the requirement to mark an order as from an insider or significant shareholder (unless the trading system of the Participant restricts trading activities in affected securities).

5. Part 2 of Policy 7.1 is amended by deleting numbered paragraph 6 and substituting the following:

6. Identify the steps the Participant will take when a violation or possible violation of a Requirement or any regulatory requirement has been identified. These steps shall include the procedure for the reporting of the violation or possible violation to the Market Regulator if required by Rule 10.16. If there has been a violation or possible violation of a Requirement identify the steps that would be taken by the Participant to determine if:

   - additional supervision should be instituted for the employee, the account or the business line that may have been involved with the violation or possible violation of a Requirement; and
   - the written policies and procedures that have been adopted by the Participant should be amended to reduce the possibility of a future violation of the Requirement.

6. Policy 7.1 is amended by adding the following as Part 5:

Part 5 – Specific Procedures Respecting Manipulative and Deceptive Activities and Reporting and Gatekeeper Obligations

Each Participant must develop and implement compliance procedures that are reasonably well designed to ensure that orders entered on a marketplace by or through a Participant are not part of a manipulative or deceptive method, act or practice nor an attempt to create an artificial price or a false or misleading appearance of trading activity or interest in the purchase or sale of a security. The minimum compliance procedures for trading supervision in connection with Rule 2.2 and Policy 2.2 are set out in the table to Part 3 of this Policy.

In particular, the procedures must address:

- the steps to be undertaken to determine whether or not a person entering an order is:

- an insider,
- an associate of an insider, and
- part of or an associate of a promotional group or other group with an interest in effecting an artificial price, either for banking and margin purposes, for purposes of effecting a distribution of the securities of the issuer or for any other improper purpose;

- the steps to be taken to monitor the trading activity of any person who has multiple accounts with the Participant including other accounts in which the person has an interest or over which the person has direction or control;
- those circumstances when the Participant is unable to verify certain information (such as the beneficial ownership of the account on behalf of which the order is entered, unless that information is required by applicable regulatory requirements);
- the fact that orders which are intended to or which effect an artificial price are more likely to appear at the end of a month, quarter or year or on the date of the expiry of options where the underlying interest is a listed security; and
- the fact that orders which are intended to or which effect an artificial price or a false or misleading appearance of trading activity or investor interest are more likely to involve securities with limited liquidity.

A Participant will be able to rely on information contained on a "New Client Application Form" or similar know-your-client record maintained in accordance with requirements of securities legislation or a self-regulatory entity provided such information has been reviewed periodically in accordance with such requirements and any additional practices of the Participant.

While a Participant cannot be expected to know the details of trading activity conducted by a client through another dealer, nonetheless, a Participant that provides advice to a client on the suitability of investments should have an understanding of the financial position and assets of the client and this understanding would include general knowledge of the holdings by the client at other dealers or directly in the name of the client. The compliance procedures of the Participant should allow the Participant to take into consideration, as part of its compliance monitoring, information which the Participant has collected respecting accounts at other dealers as part of the completion and periodic updating of the "New Client Application Form".

7. The following is added a Part 1 of Policy 10.1:

Policy 10.1 Compliance Requirement

Part 1 – Monitoring for Compliance

Rule 10.1 requires each Participant and Access Person to comply with applicable Requirements. The term "Requirements" is defined as meaning:

- these Rules;
- the Policies;
- the Trading Rules;
- the Marketplace Rules;
- any direction, order or decision of the Market Regulator or a Market Integrity Official; and
- securities legislation,

as amended, supplemented and in effect from time to time.

The Market Regulator will monitor the activities of Regulated Persons for compliance with each aspect of the definition of Requirements and the Market Regulator will use the powers under Rule 10.2 to conduct any investigation into possible non-compliance. If the Regulated Person has not complied with:

- these Rules, the Policies or any direction, order or decision of the Market Regulator or a Market Integrity Official, the Market Regulator may undertake a disciplinary proceeding pursuant to Rule 10.5;

- the Trading Rules or securities legislation, the Market Regulator may, pursuant to the exchange of information provided for under Rule 10.13, refer the matter to the applicable securities regulatory authority to be dealt with in accordance with applicable securities legislation; and

- Marketplace Rules, the Market Regulator may undertake a disciplinary proceeding pursuant to Rule 10.5 if the marketplace has retained the Market Regulator to conduct disciplinary proceedings on behalf of the marketplace in accordance with an agreement with the Market Regulator contemplated by Part 7 of the Trading Rules, otherwise the Market Regulator may refer the matter to the marketplace to be dealt with in accordance with the Marketplaces Rules of that marketplace.

8. The following is added a Part 1 of Policy 10.16:

Policy 10.16 Gatekeeper Obligations of Directors, Officers and Employees of Participants and Access Persons

Part 1 – The Gatekeeper Obligation

Rule 10.16 requires a Participant or Access Person to conduct further investigation or review where the Participant or Access Person has reason to believe that there may have been a violation of one of the provisions enumerated in Rule 10.16. A Participant or Access Person can not ignore “red flags” which may be indicative of improper behaviour by a client, director, officer, partner or employee of the Participant, Access Person or related entity.

Appendix "B"

Universal Market Integrity Rules

Comments Received on Proposed Amendments
Related to Manipulative and Deceptive Activities

On August 13, 2004, RS issued Market Integrity Notice 2004-017 requesting comments on revised proposed amendments to UMIR related to manipulative and deceptive activities. In response to that Market Integrity Notice, RS received comments from the following persons:

BMO Nesbitt Burns ("BMO")
Canaccord Capital Corporation ("Canaccord")
GMP Securities Ltd. ("GMP")
Raymond James Ltd. ("RJ")
Simon Romano ("Romano")
Scotia Capital Inc. ("Scotia")
TD Securities Inc. ("TD")

The following table presents a summary of the comments received together with the response of RS to those comments. Column 1 of the table is also marked to indicate the revisions to the amendments as published on August 13, 2004 made by RS in response to the comments. Additions are indicated in "red" font and the added text is underlined while deletions from the August 13, 2004 proposal are indicated in "blue" font and the deleted text is struck out.

Text of Provisions Following Adoption of Amendments As Revised	Commentator and Summary of Comment	Response to Comment
1.1 Definitions **"Requirements"** means, collectively: (a) these Rules; (b) the Policies; (c) the Trading Rules; (d) the Marketplace Rules; (e) any direction, order or decision of the Market Regulator or a Market Integrity Official; and (f) securities legislation, as amended, supplemented and in effect from time to time.	**Romano** - Notes that the commentary in MIN 2004-017 regarding the amendment to the definition of "Requirement" states that "an ATS can not have any rules". Notes that this is incorrect, as there is no prohibition in NI 21-101 on an ATS creating trading rules that will apply to its participants. States that the definition of an ATS in NI 21-101 allows for requirements to be set by an ATS in respect of trading conduct.	Under National Instrument 21-101 an alternative trading system can not "set requirements governing the conduct of subscribers, other than conduct in respect of trading by those subscribers on the marketplace". Reference should be made to Companion Policy 21-101CP with respect to the limitations on alternative trading systems.
	Scotia – Is of the view that inclusion of "securities legislation" in the definition exceeds RS's jurisdiction and authority as "securities legislation" may include foreign securities legislation. Recommends a definition of "securities legislation" such as "UMIR rules and policies and federal or provincial statutes, regulations, rulings or policies relating to trading or advising in respect of securities", which is consistent with IDA's enforcement jurisdiction. Is concerned with RS's stated intention to investigate breaches of any securities legislation and to refer matters to securities regulatory authorities, and is concerned that at the request of a foreign authority, RS may investigate and disclose information to a foreign authority for potential prosecution without due regard for Charter protections and privacy rights.	The term "securities legislation" is defined in National Instrument 14-101 and incorporated by reference into UMIR by virtue of Rule 1.2(1)(a). As such, securities legislation means the legislation of the thirteen provincial and territorial jurisdictions in Canada listed in Appendix B of National Instrument 14-101.

Text of Provisions Following Adoption of Amendments As Revised	Commentator and Summary of Comment	Response to Comment
Policy 1.2 Interpretation **Part 1 – "Ought Reasonably to Know"** Rule 2.2 prohibits a Participant or Access Person from doing various acts if the Participant or Access Person "knows or ought reasonably to know" that a particular method, act or practice was manipulative or deceptive or that the effect of entering an order or executing a trade would create or could reasonably be expected to create a false or misleading appearance of trading activity or interest or an artificial price. Rule 2.3 prohibits a Participant or Access Person from entering an order on a marketplace or executing a trade if the Participant or Access Person "knows or ought reasonably to know" that the entry of the order or the execution of the trade would result in the violation of various securities or regulatory requirements. In determining what a person "ought reasonably to know" reference would be made to what a Participant or Access Person would know, acting honestly and in good faith, and exercising the care, diligence and skill that a reasonably prudent Participant or Access Person would exercise in comparable circumstances. ~~generally accepted industry standards and practices applicable to a person of their size conducting the same types of business in the same jurisdiction.~~ In essence, the test becomes what could a Participant or Access Person have been expected to know if the Participant or Access Person had:	**BMO –** Concerned that standard of due diligence fails to address situations where a Participant acted in good faith and recommends amendment to exclude from liability those who do so. Also recommends that wording be amended such that there will be no liability in the absence of evidence of knowledge or intent to trade in a manipulative or deceptive manner, or in violation of securities laws or SRO requirements, or with reckless disregard for the consequences. Suggests that this standard is more appropriate as merely being publicly named in a disciplinary proceeding for a violation of UMIR may result in irreparable harm to reputation. States that proposed Rules fail to provide Participants with certainty as to compliance with the trading supervision requirements. As trading supervision cannot reasonably be expected to prevent all instances of violations of rules prohibiting manipulative and deceptive trading, securities legislation or SRO requirements, trading supervision systems should be expected to detect such trading where there is some reasonable indication of a violation that is reasonably detectable by a supervisory or monitoring system or procedure that can be administered by a Participant. Participants who have adopted these and observe them should not be subject to liability for failing to supervise. Concerned that the regulator has the advantage of hindsight with respect to assessment of what staff "ought to have known" or supervisory measures that ought to have been in place. Requests guidance as to what comprises "generally accepted industry standards" as there is currently no reference source for a Participant to consult.	RS initially included reference to "generally accepted industry practice" to indicate that a particular Participant would not be held to a standard which exceeded the normal practice of the industry. A number of commentators noted that there was not a readily acceptable reference point for the industry standard. RS is therefore proposing to delete this portion of the interpretation and to rely instead on a formulation based on the common law and which has been adopted as a standard in most corporate statutes.
	GMP – Suggests that references in the Rules to "ought to know" should always read "ought reasonably to know". Concerned that the reference to "generally accepted industry standards" which "may exceed minimum standards required by various regulatory requirements including any minimum elements of a supervisory system and minimum compliance procedures set out in Policy 7.1" means that reasonable means and standards may not be a defense against a violation for any Participant. Suggests that this section be left at "generally accepted industry standards and practices". Suggests that it be up to RS to establish a minimum for Participants to work from.	See response to BMO comment on Part 1 of Policy 2.2 above.
	Scotia – Concerned that the "ought reasonably to know" standard based on	See response to BMO comment on Part 1 of Policy 2.2 above.

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• adopted various policies and procedures as required by applicable securities legislation, self-regulatory entities and the Rules and Policies; and • conscientiously followed or observed the policies and procedures. ~~A Participant or Access Person must be aware that the generally accepted industry standard may exceed minimum standards required by various regulatory requirements including any minimum elements of a supervisory system and minimum compliance procedures set out in Policy 7.1.~~ ~~If there is no generally accepted industry standard, a Participant or Access Person, acting honestly and in good faith, must exercise the care, diligence and skill that a reasonably prudent Participant or Access Person would exercise in comparable circumstances.~~	undefined "generally accepted industry standards" is not clearly articulated and exposes Participants to indeterminate regulatory and civil liability including class actions. Suggests that the standard should be "A Participant or Access Person acting honestly and in good faith, must exercise the care, diligence and skill that a reasonably prudent Participant or Access Person would exercise in comparable circumstances". Suggests that RS develop a policy setting out the minimum standard for trading supervision in a manner similar to the IDA Policy 2- Minimum standard for retail account supervision.	
Policy 1.2 **Interpretation** **Part 2-- Applicable Regulatory Standards** Rule 7.1 requires each Participant prior to the entry of an order on a marketplace to comply with applicable regulatory standards with respect to the review, acceptance and approval of orders. ~~In addition, Rule 10.16 requires each officer, director, partner or employee of a Participant who receives or originates an order or who enter the order on a marketplace to comply with applicable regulatory standards with~~	**BMO** – Notes that proposed Part 2 of Policy 1.2 states that "Rule 10.16 requires each officer, director, partner or employee of a Participant who receives or originates an order or who enters the order on a marketplace to comply with applicable regulatory standards with respect to the review, acceptance and approval of orders." However, this provision has been deleted from Proposed Rule 10.16.	RS will make the additional consequential amendment as suggested.
	Scotia – States that the line, "[t]his requirement has been interpreted as requiring registrants in British Columbia to always know the beneficial owner of an account" is confusing and inconsistent with IDA 1300.1 (which sets out the regime for identification of (>10%) beneficial owners of non-individual accounts) and requests that it be deleted. Also see Scotia comments	The comment by Scotia illustrates the point which is made by RS. The standards which are in effect in each jurisdiction may vary. The requirements imposed by British Columbia with respect to the knowledge of the beneficial owner of an account may be different from that which is required by the Investment Dealers Association. Participants must comply with the higher

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~~respect to the review, acceptance and approval of orders.~~ Each Participant that is a dealer must be a member of a self-regulatory entity. Each Participant will be subject to the by-laws, regulations and policies as adopted from time to time by the applicable self-regulatory entity. These requirements may include an obligation on the member to "use due diligence to learn and remain informed of the essential facts relative to every customer and to every order or account accepted." While knowledge by a Participant of "essential facts" of every customer and order is necessary to determine the suitability of any investment for a client, such requirement is not limited to that single application. The exercise of due diligence to learn essential facts "relative to every customer and to every order" is a central component of the "Gatekeeper Obligation" embodied within the trading supervision obligation under Rule 7.1 and 10.16. In addition, securities legislation applicable in a jurisdiction may impose review standards on Participants respecting orders and accounts. ~~In British Columbia for example, Rule 48(1) made pursuant to the *Securities Act* (British Columbia) requires registrants, with certain exceptions, to make enquiries concerning each client to learn the essential facts relative to every client, including the identity and, if applicable, creditworthiness of the client and the reputation of the client if information known to the registrant causes doubt as to whether the client is of~~	under Rule 7.1 below.	standard in respect of accounts held in British Columbia.

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~~good business or financial reputation. This requirement has been interpreted as requiring registrants in British Columbia to always know the beneficial owner of an account.~~ The regulatory standards that may apply to a particular order may vary depending upon a number of circumstances including: • the requirements of any self-regulatory entity of which the Participant is a member; • the type of account from which the order is received or originated; and • the securities legislation in the jurisdiction applicable to the order.		
2.2 Manipulative and Deceptive Activities (1) A Participant or Access Person shall not, directly or indirectly, engage in or participate in the use of any manipulative or deceptive method, act or practice in connection with any order or trade on a marketplace if the Participant or Access Person knows or ought reasonably to know the nature of the method, act or practice. (2) A Participant or Access Person shall not, directly or indirectly enter an order or execute a trade on a marketplace if the Participant or Access Person	**Scotia** – States that, in response to comments, RS has provided considerable guidance in Market Integrity Notice 2004-017 regarding the intended scope and focus of Rules 2.2 and 2.3, however such guidance must be reflected in these rules or Policy 1.2. Suggests the following "safe harbour": "For greater certainty, a Participant is not required to verify or make a positive affirmation of a client's intention regarding each order or trade activity. For a Participant to be liable for the conduct of the client in connection with manipulative or deceptive activities, the Participant must have either actual knowledge or "ought reasonably to know" that the client's conduct is unacceptable or that the entry of the order or the execution of the trade would result in a violation of a regulatory requirement."	RS accepts that a positive affirmation need not be obtained in respect of each order and the suggested amendments did not seek to impose such a standard.

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knows or ought reasonably to know that the entry of the order or the execution of the trade will create or could reasonably be expected to create: (a) a false or misleading appearance of trading activity or interest in the purchase or sale of the security; or (b) an artificial ask price, bid price or sale price for the security or a related security. (3) For greater certainty, the entry of an order or the execution of a trade on a marketplace by a person in accordance with the Market Maker Obligations shall not be considered a violation of subsection (1) or (2) provided such order or trade complies with applicable Marketplace Rules and the order or trade was required to fulfill applicable Market Maker Obligations.		
Policy 2.2 Manipulative and Deceptive Activities **Part 1 - Manipulative or Deceptive Method, Act or Practice** There are a number of activities which, by their very nature, will be considered to	**BMO** – Requests guidance as to the term "direction or control" as such phrase is used in proposed Policy 2.2, but not currently defined. States that Policy 2.2 Part 1 (c) is a change from the current requirement that all trades except those where there is no change of beneficial or economic ownership be carried out on a marketplace. Requests guidance for application to corporate accounts (e.g. does "direction and control" apply to signing officers, trading personnel	The concept of "direction or control" is used in applicable securities legislation. (For example, the definition of an "insider".) RS does not propose to adopt a definition distinct from the practice currently used in the administration of the securities legislation. On an operational level, RS would expect that this provision would cover any person that would be listed in response to question

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be a manipulative or deceptive method, act or practice. For the purpose of subsection (1) of Rule 2.2 and without limiting the generality of that subsection, the following activities when undertaken on a marketplace constitute a manipulative or deceptive method, act or practice: (a) making a fictitious trade; (b) effecting a trade in a security which involves no change in the beneficial or economic ownership; ~~(c) effecting a trade in a security, other than an internal cross, between accounts under the direction or control of the same person;~~ (~~d~~c) effecting trades by a single interest or group with the intent of limiting the supply of a security for settlement of trades made by other persons except at prices and on terms arbitrarily dictated by such interest or group; and (d~~e~~) purchasing a security with the intention of making a sale of the same or a different number of units of the security or a related security on a marketplace at a price which is below the price of the last sale of a standard trading unit of such security displayed in a consolidated market display. If persons know or ought reasonably to know that	or beneficial owners?). Asks that an expansion of the definition of "internal cross" be considered instead of the prohibition in Policy 2.2 Part 1 (c).	1 of section 6 of the standard New Client Application Form. RS would propose to move the prohibition of crossing with accounts under common direction and control to Part 2. RS acknowledges that, unlike a trade with no change in economic or beneficial ownership, a trade between controlled accounts may be a proper trade that should be reflected on a marketplace. By moving the provision to Part 2, the trade would only be considered to be manipulative or deceptive if undertaken when the person knows or ought reasonably to know that the trade would or could reasonably be expected to create a false or misleading appearance of trading activity or an artificial price.
	GMP – Notes that in Market Integrity Notice 2004-017, Policy 2.2 Part 1 (c) is summarized by RS as follows: "Trades between accounts under the direction or control of the same person would not be completed on a marketplace even in circumstances where the trade resulted in a change of beneficial or economic ownership." Notes that a husband with trading authority could journal to his wife and asks, could this not be an internal cross by definition? Asks whether this will affect volumes on the market where there is no clear posted market to show these changes occurring? Asks what are the tax implications for those who can no longer move securities between controlled accounts but not on the marketplace? Ask what is the need for this rule if there is a clear change in legal ownership behind the trade? Requests a clear definition of "Internal Cross" which allows for more than institutional crossing.	See response to BMO comment on Part 1 of Policy 2.2 above.
	Romano - Asks if trades between accounts under the direction or control of the same person would not be allowed to be completed on a marketplace under Policy 2.2 Part 1 (c), how will this affect UMIR 6.4 and how will it reflect "Chinese walls" in the context of dealers' pro or discretionary accounts held by different pro traders or registered representatives?	See response to BMO comment on Part 1 of Policy 2.2 above.
	Scotia – States that RS has acknowledged that Participants have no ability to monitor trades in a security between accounts under the direction or control of the same person where those accounts are not all held with the same Participant. States that Participants also have no ability to compel a client to disclose its accounts/account holdings held with other dealers, whether	The rule provides that a Participant is engaging in a manipulative and deceptive activity if the Participant knows or ought reasonably to know that the trade would be prohibited in accordance with the provisions of Rule 2.2. If the Participant has conscientiously completed the New Client Application Form and updated that form periodically in accordance with procedures

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they are engaging or participating in these or similar types of activities those persons will be in breach of subsection (1) of Rule 2.2 irrespective of whether such method, act or practice results in a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security or a related security.	the accounts are held in the name of the client or otherwise. Recommends that proposed Policy 2.2 Part 1(c) be amended to reflect this.	of the Participant, the Participant will have discharged its obligations and can rely on the information provided by the client unless the Participant has actual knowledge of "undisclosed" accounts.
Policy 2.2 Manipulative and Deceptive Activities **Part 2 – False or Misleading Appearance of Trading Activity or Artificial Price** For the purposes of subsection (2) of Rule 2.2 and without limiting the generality of that subsection, if any of the following activities are undertaken on a marketplace and create or could reasonably be expected to create a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price, the entry of the order or the execution of the trade shall constitute a violation of subsection (2) of Rule 2.2: (a) entering an order or orders for the purchase of a security with the knowledge that an order or orders of substantially the same size, at substantially the same time and at substantially the same price for the sale of that security, has been or will be entered by or for the	**GMP** – Regarding 2.2(a) and (b), queries whether, if one has an order to buy size in a name and is aware either from the client or from the historical trading record that another dealer is trading in the name, and if one calls that dealer and meets on the board for size, is this a violation? If one has reasonable knowledge of the client and this broker does not, to one's knowledge, represent them, and one trades, is this a violation? Suggests that the rule should read, "where this is no change in beneficial ownership or the trade was executed solely for the purpose of establishing fictitious volumes".	In response to the questions, RS would note that the trades are bona fide and are not being undertaken to create a false or misleading appearance of trading activity. The clauses do not limit the ability of a Participant to undertake a pre-arranged trade. In the view of RS, the structure of the provision makes all of the activities that are listed in clauses (a) to (i) dependent on the fact the order creates or could reasonably be expected to create a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price.

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same or different persons; (b) entering an order or orders for the sale of a security with the knowledge that an order or orders of substantially the same size, at substantially the same time and at substantially the same price for the purchase of that security, has been or will be entered; (c) making purchases of, or offers to purchase, a security at successively higher prices or in a pattern generally of successively higher prices; (d) making sales of or offers to sell a security at successively lower prices or in a pattern generally of successively lower prices; (e) entering an order or orders for the purchase or sale of a security to: (i) establish a predetermined sale price, ask price or bid price, (ii) effect a high or low closing sale price, ask price or bid price, or (iii) maintain the sale price, ask price or bid price within a predetermined range; (f) entering an order or series of orders for a		

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security that are not intended to be executed; (g) entering an order for the purchase of a security without, at the time of entering the order, having the ability or the reasonable expectation to make the payment that would be required to settle any trade that would result from the execution of the order; ~~and~~ (h) entering an order for the sale of a security without, at the time of entering the order, having the reasonable expectation to settle any trade that would result from the execution of the order; and (i) effecting a trade in a security, other than an internal cross, between accounts under the direction or control of the same person. If persons know or ought reasonably to know that they are engaging or participating in these or similar types of activities those persons will be in breach of subsection (2) of Rule 2.2 irrespective of whether such activity results in a false or misleading appearance of trading activity or interest in the purchase or sale of a security or an artificial ask price, bid price or sale price for a security or a related security.		
Policy 2.2 Manipulative and Deceptive Activities		

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Part 3 – Artificial Pricing For the purposes of subsection (2) of Rule 2.2, an ask price, bid price or sale price will be considered artificial if it is not justified by real demand or supply in a security. Whether or not a particular price is "artificial" depends on the particular circumstances. Some of the relevant considerations in determining whether a price is artificial are: (a) the prices of the preceding and succeeding trades; (b) the change in last sale price, best ask price or best bid price that results from the entry of the order; (c) the recent liquidity of the security; (d) the time the order is entered, or any instructions relevant to the time of entry of the order; and (e) whether any Participant, Access Person or account involved in the order: (i) has any motivation to establish an artificial price, or (ii) represents substantially all of the orders entered or executed for the purchase or sale of the security. The absence of any one or more of these considerations is not determinative that a price is or is not artificial.		

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2.3 Improper Orders and Trades A Participant or Access Person shall not enter an order on a marketplace or execute a trade if the Participant or Access Person knows or ought reasonably to know that the entry of the order or the execution of the trade would not comply with or would result in the violation of: (a) applicable securities legislation; (b) applicable requirements of any self-regulatory entity of which the Participant or Access Person is a member; (c) the Marketplace Rules of the marketplace on which the order is entered; (d) the Marketplace Rules of the marketplace on which the trade is executed; or (e) the Rules and Policies.	**BMO** – Suggests that Rule 2.3 should be amended to make it explicitly clear that RS does not require all orders to be reviewed prior to entry for order-execution accounts, as RS has made this clear in its responses to comments in Market Integrity Notice 2004-017.	RS does not believe that it is necessary to amend the proposed Rule. The interpretation which RS intends to take with respect to the provision has been set out in the Market Integrity Notice.
	GMP – Asks that the word "reasonably" be inserted in every case where "ought to have known" is used. Is concerned about the example used by RS in Market Integrity Notice 2004-017 to illustrate the meaning of this section. The example states that "if a Participant knows or ought to know that a client is entering an order for a security based on undisclosed material information related to that security (which action by the client would be contrary to securities legislation), the Participant would itself be in non-compliance with the requirements of UMIR." Concerned as to how a trader is to know that an institution received information that could be deemed to be material which the trader has no knowledge of. Asks what jurisdiction RS has regarding a Participant's responsibility to not violate rules in general. Asks why "securities legislation", SROs and "marketplace rules" are included when the RS jurisdiction is to the Canadian listed marketplaces? Requests clarification of what is meant by "(e) the Rules and Policies". Assumes UMIR should be referenced here.	In the revised proposal published on August 13, 2004, all references to "ought to know" where amended by the addition of the word "reasonably". The provision is premised on the Participant knowing or being in a position where they "ought reasonably to know" that an order does not comply with various requirements. If the Participant did not have any reason to believe that there would be a failure to comply with any of the requirements of securities legislation, requirements of an SRO, Marketplace Rules or UMIR there would not be a violation of the proposed Rule 2.3. As a self-regulatory entity, part of the mandate of RS is to ensure that the persons who are subject to its jurisdiction conduct trading openly and fairly in accordance with just and equitable principles of trade. This standard is incorporated directly into UMIR in Rule 2.1. Any person who knowingly breaches requirements of various entities regarding the trading of securities could not be said to be conducting transacting business "openly and fairly". Rule 2.3 is simply a specific statement of this general requirement. "Rules" and "Policies" are the defined terms which comprise UMIR.
	Scotia – See Scotia comment on: Rule 2.2 above.	See response to Scotia comment on Rule 2.2 above.
7.1 Trading Supervision Obligations (2) Prior to the entry of an order on a marketplace by a Participant, the Participant shall comply with: (a) applicable regulatory standards with respect to the review, acceptance and approval of orders;	**BMO** - States that Rule 7.1 and Policy 7.1 do not address the additional systems that will be required for additional supervisory requirements and resource needs nor the deadlines within which RS would expect Participants to have acted in order to address these required additional supervisory obligations. Proposes that RS delay the implementation of additional proposed supervisory obligations until after proposed electronic audit trail has been implemented pursuant to National Instrument 23-101. Adds that Rule and Policy 7.1 appear duplicative of requirements of the IDA by introducing a requirement for heightened supervision when client KYC information hasn't been obtained or verified. Suggests that RS	The revised proposal contained in Market Integrity Notice 2004-017 made a number of revisions to the original proposal made in Market Integrity Notice 2004-003 to clarify that the amendments were not introducing new supervision requirements. The amendments specifically will add a reporting requirement, but in the opinion of RS, this requirement will not necessarily involve additional systems work by a Participant. RS would note that many Participants already have voluntary reporting procedures. The provisions under UMIR do not augment the information which must be obtained in the completion of the New Client Application Form. However, the UMIR

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(b) the policies and procedures adopted in accordance with subsection (1); and (c) all requirements of these Rules and each Policy.	consider either removing this requirement, since there is an established system of IDA requirements in this area, or work more closely with IDA to coordinate impact of overlapping requirements.	requirement will require additional supervision and compliance procedures when certain of the information required on the New Client Application Form has not been provided by the client.
	GMP – In Market Integrity Notice 2004-017, RS stated the following as a response to comments to Rule 7.1: "Provided that the know your client form is reviewed periodically in accordance with the practice of the Participant, the Participant will be able to rely on this information". States that this phrase must be inserted in it's entirety into the rule. Queries whether this is a jurisdictional item and beyond a reasonable expectation.	RS would propose to expand Part 5 of Policy 7.1 to indicate the ability of a Participant to rely on information provided in accordance with "know-your-client" requirements. See response to GMP comment on Rule 2.3 above.
	Scotia – States that new "gatekeeper" provisions in Rule 7.1, Policy 7.1, Rule 10.16 and Policy 10.16 seek to shift the responsibility and cost of compliance from other market participants onto Participants. This is inappropriate and inefficient as Participants will have to individually create exhaustive monitoring systems, at considerable costs, to ensure that other market participants are complying with their regulatory requirements relating to their orders and will be exposed to potential regulatory and civil liability (including potential class actions) for non-complying orders, even where the order is entered directly by Access Persons or online retail clients without any participation by the Participants. Costs should be borne by market participant in the best position to ensure effective compliance.	UMIR has always imposed responsibility on each Participant for all orders entered on a marketplace by that Participant. The proposed provisions do not "shift the responsibility and cost of compliance from other market participants on Participants" but merely clarifies the steps which RS believes as reasonable for a Participant to discharge existing obligations. Where a Participant is acting in a transaction for another Participant or dealer, either Participant or the dealer may, if agreed upon, undertake certain of the supervision and compliance activities. However, neither Participant can absolve themselves of "responsibility" because of a delegation of these functions.
Policy 7.1 Trading Supervision Obligations **Part 1 – Responsibility for Supervision and Compliance** For the purposes of Rule 7.1, a Participant shall supervise its employees, directors and officers and, if applicable, partners to ensure that trading in securities on a marketplace (an Exchange, QTRS or ATS) is carried out in compliance with the applicable Requirements (which includes provisions of securities legislation, UMIR, the Trading Rules and the Marketplace Rules	**Scotia** – See Scotia comments under Rule 7.1 above.	See response to Scotia comment on Rule 7.1 above.

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of any applicable Exchange or QTRS). An effective supervision system requires a strong overall commitment on the part of the Participant, through its board of directors, to develop and implement a clearly defined set of policies and procedures that are reasonably designed to prevent and detect violations of Requirements. The board of directors of a Participant is responsible for the overall stewardship of the firm with a specific responsibility to supervise the management of the firm. On an ongoing basis, the board of directors must ensure that the principal risks for non-compliance with Requirements have been identified and that appropriate supervision and compliance procedures to manage those risks have been implemented. Management of the Participant is responsible for ensuring that the supervision system adopted by the Participant is effectively carried out. The head of trading and any other person to whom supervisory responsibility has been delegated must fully and properly supervise all employees under their supervision to ensure their compliance with Requirements. If a supervisor has not followed the supervision procedures adopted by the Participant, the supervisor will have failed to comply with their supervisory obligations under Rule 7.1(4). When the Market Regulator reviews the supervision system of a Participant (for example, when a violation occurs of Requirements), the Market Regulator will		

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consider whether the supervisory system is reasonably well designed to prevent and detect violations of Requirements and whether the system was followed. The compliance department is responsible for monitoring and reporting adherence to rules, regulations, requirements, policies and procedures. In doing so, the compliance department must have a compliance monitoring system in place that is reasonably designed to prevent and detect violations. The compliance department must report the results from its monitoring to the Participant's management and, where appropriate, the board of directors, or its equivalent. Management and the board of directors must ensure that the compliance department is adequately funded, staffed and empowered to fulfil these responsibilities. The obligation to supervise applies whether the order is entered on a marketplace: • by a trader employed by the Participant, • by an employee of the Participant through an order routing system, • directly by a client and routed to a marketplace through the trading system of the Participant, or • by any other means. In performing the trading supervision obligations, the Participant will act as a "gatekeeper" to help prevent and detect violations of applicable Requirements.		

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Where an order is entered on a marketplace without the involvement of a trader (for example by a client with a systems interconnect arrangement in accordance with Policy 2-501 of the Toronto Stock Exchange), the Participant retains responsibility for that order and the supervision policies and procedures should adequately address the additional risk exposure which the Participant may have for orders that are not directly handled by staff of the Participant. For example, it may be appropriate for the Participant to sample for compliance testing a higher percentage of orders that have been entered directly by clients than the percentage of orders sampled in other circumstances. In addition, the "post order entry" compliance testing should recognize that the limited involvement of staff of the Participant in the entry of orders by a direct access client may restrict the ability of the Participant to detect orders that are not in compliance with specific rules. For example, "post order entry" compliance testing may be focused on whether an order entered by a direct access client: • has created an artificial price contrary to Rule 2.2; • is part of a "wash trade" (in circumstances where the client has more than one account with the Participant); • is an unmarked short sale (if the trading system of the Participant does not		

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automatically code as "short" any sale of a security not then held in the account of the client); and • has complied with order marking requirements and in particular the requirement to mark an order as from an insider or significant shareholder (unless the trading system of the Participant restricts trading activities in affected securities).		
Policy 7.1 Trading Supervision Obligations **Part 2 – Minimum Elements of a Supervision System** Regardless of the circumstances of the Participant, however, every Participant must: 6. Identify the steps the Participant will take when a violation or possible violation of a Requirement or any regulatory requirement have been identified. These steps shall include the procedure for the reporting of the violation or possible violation to the Market Regulator <u>if</u> ~~as~~ required by Rule 10.16. If there has been a violation or possible violation of a Requirement identify the steps that would be taken by the Participant to determine if: • additional supervision should be instituted for the employee, the account or the	**GMP** – Suggests that "violations" or "patterns of potential violations" should be reportable rather than a potential violation in singular form. States that there is a lack of consistency in the wording used throughout the various references to this Rule.	RS expects a Participant to take action with respect to each violation which it detects. It would not be appropriate for the supervisors or compliance personnel of a Participant to bring violations to the attention of a trader only if a "pattern of potential violations" has been detected. The supervisor or compliance personnel should be determining whether the violation or potential violation was a mistake or a lack of understanding of the applicable Requirement. RS would propose to clarify that a report to the Market Regulator is not required in every instance (e.g. a report would only be made to the Market Regulator "if" required by Rule 10.16.)

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business line that may have been involved with the violation or possible violation of a Requirement.; and • the written policies and procedures that have been adopted by the Participant should be amended to reduce the possibility of a future violation of the Requirement.		
Policy 7.1 Trading Supervision Obligations **Part 5 – Specific Procedures Respecting Manipulative and Deceptive Activities and Reporting and Gatekeeper Obligations** Each Participant must develop and implement compliance procedures that are reasonably well designed to ensure that orders entered on a marketplace by or through a Participant are not part of a manipulative or deceptive method, act or practice nor an attempt to create an artificial price or a false or misleading appearance of trading activity or interest in the purchase or sale of a security. The minimum compliance procedures for trading supervision in connection with Rule 2.2 and Policy 2.2 are set out in the table to Part 3 of this Policy. In particular, the procedures must address: • the steps to be undertaken to determine whether or	**GMP** – Concerned that the last portion of this section referring to the "New Client Application Form" treads into IDA Policies. Asks whether this RS requirement is going to be added to the IDA Rules for consistency amongst the regulators? Asks how dealers are meant to enforce this with clients, as there is no justifiable right to ask this question to a client other than this new rule. Queries the inclusion of "asset lists" and the application of privacy laws that may supercede this rule. States that it is unreasonable to expect a Compliance Department to monitor for this without development costs and time. Suggests that this should be the sole responsibility for the RR of a retail account and should not extend beyond that level where the knowledge MAY be required by this potential rule.	The text of Part 5 makes reference to the information which the Participant has in its possession as a result of the completion or updating of the "New Client Application Form". The provision merely requires that a Participant take into account information which is already within its possession. Reference should be made to the table in Part 3 of Policy 7.1 setting out Minimum Compliance Procedures for Trading on a Marketplace. With respect to testing for manipulative and deceptive trading, the "New Client Application Form" is already listed as one of the potential information sources. The paragraph which has been added to Part 5 merely illustrates how this information should be used.
	Scotia – States that RS has acknowledged that Participants have no ability to monitor trades in a security between accounts under the direction or control of the same person where those accounts are not all held with the same Participant. Suggests further that Participants have no ability to compel a client to disclose its accounts/account holdings held with other dealers, whether the accounts are held in the name of the client or otherwise. Recommends that Policy 7.1 Part 5 be amended and the proposed paragraph added to the end of Policy 7.1 Part 5 should be deleted in its entirety, in order to reflect this.	Question 3 of subsection (6) of the New Client Application Form requires the disclosure of accounts held at other firms by the client. See response to GMP comment on Part 5 of Policy 7.1 above.

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not a person entering an order is: o an insider, o an associate of an insider, and o part of or an associate of a promotional group or other group with an interest in effecting an artificial price, either for banking and margin purposes, for purposes of effecting a distribution of the securities of the issuer or for any other improper purpose; • the steps to be taken to monitor the trading activity of any person who has multiple accounts with the Participant including other accounts in which the person has an interest or over which the person has direction or control; • those circumstances when the Participant is unable to verify certain information (such as the beneficial ownership of the account on behalf of which the order is entered, unless that information is required by applicable regulatory requirements); • the fact that orders which are intended to or which effect an artificial price are more likely to appear at the end of a month, quarter or year or on the date of the expiry of options where the underlying interest is a listed security; and • the fact that orders which are intended to or		

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which effect an artificial price or a false or misleading appearance of trading activity or investor interest are more likely to involve securities with limited liquidity. A Participant will be able to rely on information contained on a "New Client Application Form" or similar know-your-client record maintained in accordance with requirements of securities legislation or a self-regulatory entity provided such information has been reviewed periodically in accordance with such requirements and any additional practices of the Participant. While a Participant cannot be expected to know the details of trading activity conducted by a client through another dealer, nonetheless, a Participant that provides advice to a client on the suitability of investments should have an understanding of the financial position and assets of the client and this understanding would include general knowledge of the holdings by the client at other dealers or directly in the name of the client. The compliance procedures of the Participant should allow the Participant to take into consideration, as part of its compliance monitoring, information which the Participant has collected respecting accounts at other dealers as part of the completion and periodic updating of the "New Client Application Form".		
Policy 10.1 Compliance Requirement	**Scotia** - Is concerned that Participants may be exposed to civil liability for disclosing	This is a matter which each Participant must address in its account agreement with

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Part 1 – Monitoring for Compliance Rule 10.1 requires each Participant and Access Person to comply with applicable Requirements. The term "Requirements" is defined as meaning: • these Rules; • the Policies; • the Trading Rules; • the Marketplace Rules; • any direction, order or decision of the Market Regulator or a Market Integrity Official; and • securities legislation, as amended, supplemented and in effect from time to time. The Market Regulator will monitor the activities of Regulated Persons for compliance with each aspect of the definition of Requirements and the Market Regulator will use the powers under Rule 10.2 to conduct any investigation into possible non-compliance. If the Regulated Person has not complied with: • these Rules, the Policies or any direction, order or decision of the Market Regulator or a Market Integrity Official, the Market Regulator may undertake a disciplinary proceeding pursuant to Rule 10.5; • the Trading Rules or securities legislation, the Market Regulator	clients' personal information to RS in the course of an RS investigation when RS may further disclose information to third parties without clients' consent. Recommends that a safe harbour be incorporated into Policy 10.1 Part 1 to protect Participants from liability arising from disclosure of information under an RS investigation.	its clients. The disclosure of the information is for regulatory purposes and Participants should have made it clear to clients that the Participant will provide information to comply with legal and regulatory requirements to which the Participant is subject. It is the responsibility of the Participant to ensure that it has all necessary consents to ensure compliance. See the "Joint Regulatory Notice on Federal and Provincial Privacy Legislation" issued by RS, the Investment Dealers Association, Mutual Fund Dealers Association, Montréal Exchange and Canadian Investor Protection Fund on December 3, 2003.

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may, pursuant to the exchange of information provided for under Rule 10.13, refer the matter to the applicable securities regulatory authority to be dealt with in accordance with applicable securities legislation; and • Marketplace Rules, the Market Regulator may undertake a disciplinary proceeding pursuant to Rule 10.5 if the marketplace has retained the Market Regulator to conduct disciplinary proceedings on behalf of the marketplace in accordance with an agreement with the Market Regulator contemplated by Part 7 of the Trading Rules, otherwise the Market Regulator may refer the matter to the marketplace to be dealt with in accordance with the Marketplaces Rules of that marketplace.		
10.4 Extension of Restrictions (1) A related entity of a Participant and a director, officer, partner or employee of the Participant or a related entity of the Participant shall: (a) comply with the provisions of these Rules and any Policies with respect to just and equitable principles of trade, manipulative and deceptive activities, short sales and	**Scotia** – States that, in response to comments, RS has provided considerable guidance regarding the intended scope and focus of Rules 10.3 and 10.4, however such guidance must be reflected in these rules. Suggests the following "safe harbour" for inclusion in Rule 10: "For greater certainty, a Participant will not be in breach of Rule 10.3 or 10.4 where an employee or a related entity breaches a Participant's policies without knowledge or authorization of the Participant, provided the Participant had adequate policies in place and the Participant and its supervisory personnel followed the procedures as adopted."	Neither Rule 10.3 nor 10.4 makes a Participant responsible for the behaviour of a "related entity" or the directors, officers, partners or employees of the related entity. In particular, Rule 10.4 brings the related entity and its directors, officers, partners and employee within the ambit of UMIR and the jurisdiction of RS with respect to certain key market integrity rules. Under UMIR, a "related entity" is an affiliate that is registered under securities legislation as a dealer.

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frontrunning as if references to "Participant" in Rules 2.1, 2.2, 2.3, 3.1 and 4.1 included reference to such person; and … (2) A related entity of an Access Person and a director, officer, partner or employee of the Access Person or a related entity of the Access Person shall in respect of trading on a marketplace on behalf of the Access Person or related entity of the Access Person: (a) comply with the provisions of these rules and any Policies with respect to just and equitable principles of trade, manipulative and deceptive activities and short sales as if references to "Access Person" in Rules 2.1, 2.2, 2.3 and 3.1 included reference to such person; and		
10.16 Gatekeeper Obligations of Directors, Officers and Employees of Participants and Access Persons (1) An officer, director, partner or employee of a	**BMO** – States that a requirement on officers, directors, partners and employees of a Participant to report account activity that "may be" a violation of applicable rules should be clarified as it would capture technical violations that have no impact on the marketplace and imposes a significant reporting, record keeping and administrative burden on Participants. Recommends that RS consider a requirement to report activity	Repeated "technical" violations may be an indication of either a lack of training of personnel or inadequate policies and procedures. RS recognizes that "technical rules" should be exempt from the reporting requirement (and RS would certainly include the requirements on order marking and records in the "technical" category"). RS would propose to delete a number of the Rules that were originally included in

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Participant shall forthwith report to their supervisor or the compliance department of the Participant upon becoming aware of activity in a principal, non-client or client account of the Participant or a related entity that the officer, director, partner or employee believes may be a violation of: (a) Subsection (1) of Rule 2.1 respecting just and equitable principles of trade; (b) Rule 2.2 respecting manipulative and deceptive activities; (c) Rule 2.3 respecting improper orders and trades; ~~(d) Rule 3.1 respecting short selling;~~ (d) Rule 4.1 respecting frontrunning; (e) Rule 5.1 respecting best execution of client orders; (f) Rule 5.2 respecting best price obligation; (g) Rule 5.3 respecting client priority;	where the officer, director, partner or employee has reasonable grounds to believe a violation of the specified Rules has occurred. Minor, technical violations with no effect on the market should be excluded. The proposed rule should be made as consistent as possible with reporting actual violations similar to IDA Policy 8. Notes that supervision and monitoring procedures already exist as regulatory requirements (e.g. UMIR 7.1, Rules of Bourse de Montreal Policy 6, IDA Policy 2 and proposed IDA Policy 4), and Participants are already subject to regular on-site reviews by multiple regulators, therefore the need for an additional reporting requirement to RS is mitigated by this well-established system. Notes that the Rule has been drafted to allow RS to designate Requirements from time to time that are subject to these reporting and investigation requirements. Submits that in order to ensure fairness, such power should be exercised only as the result of an amendment to UMIR following the rule-making process.	the reporting requirements (particularly Rule 3.1 respecting short selling, Rule 6.3 respecting exposure of client order, Rule 7.7 and 7.8 respecting market stabilization and market balancing and Rule 8.1 respecting client-principal trading. Breaches of these rules may be readily detectable through existing monitoring mechanisms of RS.) Policy 8 of the IDA requires the member to report "whenever an internal investigation, pursuant to Part II of this Policy, is commenced and the results of such internal investigation when completed". The IDA Policy requires the investigation "where it appears" that there has been a violation. (BMO has interpreted this phrase as requiring only "actual violations". The ordinary interpretation of the phrase is "to give certain indications" or "seem" which equates to the legal usage of "may be".) The RS proposal did not require a report on the commencement of the investigation nor a report on the outcome of the investigation unless there is a finding that a violation "may have" occurred. RS is proposing to require the report only where the Participant or Access Person concludes after diligent investigation that a violation has occurred. Nonetheless, RS would encourage reports where the Participant or Access Person has determined that a violation may have occurred. In any event, the Participant or Access Person will be under an obligation to retain a record on the investigation and this record may be reviewed by RS as part of any trade desk review. While RS has attempted to parallel the structure used by the IDA in Policy 8, RS is proposing to further revise the requirements to clarify that "ordinary reviews" conducted in accordance with the trading supervision and compliance procedures of a Participant do not constitute an "investigation". (In passing, RS would note that IDA Policy 8 does not provide a similar exemption for "inadvertent" or "technical" violations of the rules covered by its reporting requirements.) Any designation by RS of additional rules for which an investigation report could be required would only be made after agreement from the applicable securities regulatory authorities and appropriate notice to Participants and Access Persons by means of a Market Integrity Notice.

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~~(h) (Rule 6.3 respecting exposure of client orders;~~ (h) Rule 6.4 respecting trades to be on a marketplace; and ~~(i) Rule 7.7 respecting trades during a distribution or Rule 7.8 respecting trades during a securities exchange take-over bid;~~ ~~(j) Rule 8.1 respecting client principal trading; and~~ (i) any Requirement that has been designated by the Market Regulator for the purposes of this subsection.	**Canaccord** – Recommends that Participants be allowed discretion to judge which rule violations (potential or actual) should be reported to the market regulator. Requiring Participants to report all rule violations, including those as a result of human error, is time consuming and impractical and demonstrates the market regulator's lack of faith in the compliance departments of Participants. Violations due to human error must be resolved internally. All parties should remain focused on significant rule infractions.	Repeated "human error" may be an indication of either a lack of training of personnel or inadequate policies and procedures. RS recognizes that "technical rules" should be exempt from the reporting requirement (and RS would certainly include the requirements on order marking and records in the "technical" category"). See response to BMO comment on Rule 10.16 above and the response to GMP comment on Rule 10.16 below.
(2) An officer, director, partner or employee of an Access Person shall forthwith report to their supervisor or the compliance department of the Access Person upon becoming aware of activity by the Access Person or a related entity that the officer, director, partner or employee believes may be a violation of: (a) Subsection (2) of Rule 2.1 respecting	**GMP** – Recommends that clarification of gatekeeper obligations found under the heading "Summary of Revisions to the Original Proposal" in Market Integrity Notice 2004-017 (stating that gatekeeper obligations do not set a new standard nor require Participants to "guarantee" compliance) be inserted into the gatekeeper rule itself. States that the RS summary of this section in Market Integrity Notice 2004-017 indicates that dealers are to "report findings of potential violations" and feels that dealers should not be required to inundate RS with every question, particularly where there is no evidence, on follow-up of an actual intentional violation or if there is no pattern. States that there needs to be allowance made for human and technical errors and suggests that it is more important for patterns to be reportable. Suggests that Rule 10.16(3)(d) should read as follows: ""report the findings of the investigation to the Market Regulator if the finding of the	RS would propose to clarify the ambit of Rule 10.16 by an addition to the Policies. See proposed Part 1 of Policy 10.16 below. While RS would encourage a Participant or Access Person to report "possible violations", RS would require a report only if the Participant or Access Person concludes after due investigation that a violation of one of the enumerated rules has occurred.

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conduct of business openly and fairly; (b) Rule 2.2 respecting manipulative and deceptive activities; (c) Rules 2.3 respecting improper orders or trades; and ~~(d) Rule 3.1 respecting short selling; and~~ (d~~e~~) any Requirement that has been designated by the Market Regulator for the purposes of this subsection. (3) If a supervisor or compliance department of a Participant or Access Person receives a report ~~in~~ pursuant to ~~accordance with~~ subsection (1) or (2), the supervisor or compliance department shall diligently conduct a review in accordance with the policies and procedures of the Participant adopted in accordance with Rule 7.1 or in accordance with the ordinary practices of the Access Person. (4) If the review conducted by the supervisor or	investigation is that a violation of an applicable Rule occurred or that a pattern of potential violations has appeared and such report shall be made not later that the 15th day of the month following the month in which the findings are made." States further that the RS response to comments in Market Integrity Notice 2004-017 that "It has been the intention of RS to limit the reporting requirement to the "non-technical" rules in which either the interest of the client or the market was in issue" must be incorporated into 10.16. States that the striking of a wrong key allowing a downtick on a short sale with no pattern of repetition or a best execution error where one trader does better than the other, must not be captured. Asks, in this example, if one of these traders is executing for INV and the trades are reviewed and corrected to the client, was there intent? Was it rectified therefore no longer a violation? Further, notes that the RS response to comments in Market Integrity Notice 2004-017 stating that "If there is any doubt as to whether a violation has occurred the Participant should report the event to the Market Regulator" is a clearer statement than other references to what is reportable under 10.16 and is a better option than what is currently proposed. Notes that the RS response to comments in Market Integrity Notice 2004-017 stated that "The proposed rule would require a report only when the internal investigation by the Participant came to the finding that "a violation of an applicable Rule may have occurred". Queries whether it is reportable when Participant feels that they have corrected any doubt, completed a review which found there to be a reasonable explanation for the potential violation and will monitor for any pattern.	
	RJ – Suggests that rather than requiring Participants to submit monthly gatekeeper reports for transactions that "may" be a violation, firms should be required only to submit reports for activity that is, in their determination, "clearly" a violation. This would allow the market regulator in hindsight to determine whether a Participant was deficient in not reporting gross violations of UMIR 2.2. Requests clarification of what accountability, if any, would be attached to the Chief Compliance Officer and Ultimate Designated Person where RS determines in hindsight that a	See response to BMO comment on Rule 10.16 above. Responsible officers of a Participant or Access Person would be liable for failing to make a report if the Participant had not diligently pursued the investigation or did not make a determination in good faith.

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compliance department concludes that there may be a violation, the supervisor or compliance department shall: (a) make a written record of the report by the officer, director, partner or employee and the review conducted in accordance with subsection (3); (b) diligently investigate the activity that is the subject of the report and review; (c) make a written record of the findings of the investigation; and (d) report the findings of the investigation to the Market Regulator if the finding of the investigation is that a violation of an applicable Rule has ~~may have~~ occurred and such report shall be made not later than the 15th day of the month following the month in which the findings are made. (5) Each Participant	gatekeeping report should have been submitted. A specific standard should be developed for reporting. Requests a thorough list of scenarios on which Participants may base their gatekeeping reporting requirements.	
	Scotia – See Scotia comments under Rule 7.1 above.	See response to BMO and GMP comments on Rule 10.16 above.
	TD – Concerned as to when the reporting requirements are triggered and what steps must be taken to advise the market regulator. States that the wording indicates that any violation (e.g. improper marking of a short sale) must be reported to the market regulator, though this is an unreasonable amount of administrative work for an immaterial violation that may be sufficiently dealt with internally. Concerned that this requires 100% compliance with all rules at all times and places unwarranted scrutiny on one-off errors rather than market integrity issues. Suggests instead a policy where a third violation within a set period would be subject to an internal investigation with the result being provided to the market regulator. Concerned that rule will create an unwanted adversarial relationship between compliance and trade desk staff.	The improper marking of a "short sale" was not a reportable violation under the draft of August 13, 2004. What would have been reportable in respect of a short sale was any a sale that occurred at less than the less sale price because the order was not marked as "short". However, under the revised proposal, reports will not be required with respect to violations of Rule 3.1. RS expects that there will be the highest possible compliance with requirements that affect the interest of clients or other market participants.

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and Access Person shall with respect to the records of the report, the review and the ~~record of the~~ findings required by subsection (43): (a) retain the records for a period of not less than seven years from the creation of the record; and (b) allow the Market Regulator to inspect and make copies of the records at any time during ordinary business hours during the period that such record is required to be retained in accordance with clause (a). (65) The obligation of a Participant or an Access Person to report findings of an investigation under subsection (43) is in addition to any reporting obligation that may exist in accordance with applicable securities legislation, the requirements of any self-regulatory entity and any applicable Marketplace Rules.		
Policy 10.16 Gatekeeper Obligations of Directors, Officers and Employees of Participants and Access Persons		

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Part 1 – The Gatekeeper Obligation Rule 10.16 requires a Participant or Access Person to conduct further investigation or review where the Participant or Access Person has reason to believe that there may have been a violation of one of the provisions enumerated in Rule 10.16. A Participant or Access Person can not ignore "red flags" which may be indicative of improper behaviour by a client, director, officer, partner or employee of the Participant, Access Person or related entity.		
General and Additional Comments	**Canaccord** – Suggests that the market regulator consider informing compliance area of Participants of potential or actual rule infractions discovered by the market regulator via internal systems or public complaints. Compliance area should be contacted first, rather than specific Approved Trader, as Approved Traders are busy during market opening hours and may make inadvertent mistakes in trading if communicating with market regulator at the same time. TSX is developing a product to provide Participants with alerts for compliance violations; market regulator should request that TSX publish specifications of this product along with a time-line for implementation. Market regulator and TSX should work together to develop products to reduce rule infractions that arise from unintentional human error (e.g. missing firm numbers on jitney orders).	The practice of RS is to move to "solve" any problem in real time with the applicable trader as any error or violation may impact of current market activity. RS believes that the internal policies and procedures of the Participant should govern the reporting of contacts by a regulator to the compliance department. RS offers a "Potential Violation Alert Notification" service to subscribing dealers as a mechanism or notifying dealers of actual rule violations. RS is aware of the initiative by the TSX and is co-operating in its development. However, it must be recognized that any TSX solution may only be applicable in respect of orders entered onto the TSX.