September 19, 2014

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority (Saskatchewan)
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Attention:
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Toronto, ON M5H 3S8
Fax: 416-593-2318
E-mail: comments@osc.gov.on.ca

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Dear Sirs/Mesdames:

CSA Notice and Request for Comment – Request for Comment Regarding Proposed Amendments to National Instrument 23-101 – *Trading Rules* ("Request for Comments")

A. About BlackRock

BlackRock, Inc. ("**BlackRock**" or "**we**") is one of the world's leading asset management firms, managing assets for clients in North America and South America, Europe, the Middle East, Africa, Asia and Australia. Our client base includes corporate, public, multi-employer pensions

plans, insurance companies, mutual funds and exchange-traded funds, endowments, foundations, charities, corporations, official institutions, banks and individuals around the world.

As of June 30, 2014, BlackRock's assets under management totalled US $4.594 trillion across equity, fixed income, cash management, alternative investment, real estate and advisory products.

BlackRock Asset Management Canada Limited is an indirect, wholly-owned subsidiary of BlackRock and is registered as a portfolio manager, investment fund manager and exempt market dealer in all the jurisdictions of Canada and as a commodity trading manager in Ontario.

B. General Observations

The Canadian market is a well-functioning and efficient market. It operated effectively and efficiently through the stress of the global financial crisis in 2007-2008, and has continued to improve along a number of dimensions, including through the narrowing of bid-ask spreads and a general increase in liquidity. In part, these market improvements have been the result of thoughtful regulation, which promotes competition, innovation and transparency.

We commend the CSA for their detailed and thoughtful proposal and agree that the market structure issues identified in the Request for Comments warrant further investigation and enhanced scrutiny. We encourage the CSA to take a holistic approach in assessing the potential benefits and impacts associated with the proposed measures, as there is a high degree of connectivity in the current ecosystem given that many market structure issues raised in the Request for Comments are interrelated.

C. BlackRock's Responses

As BlackRock is generally in agreement with the proposed amendments and initiatives contemplated by the Request for Comments, our response focuses on certain general principles and proposals which we believe warrant our comment.

1. OPR Proposal

The order protection rules ("**OPR**") have fostered competition among trading venues, which we believe has encouraged a variety of positive effects for investors including the reduction of explicit trading costs, tightening of bid-ask spreads, and the introduction of innovative trading platforms. While investors have benefitted from these improvements, we recognize that these rules may also act as a crutch for certain marketplaces, and may have also fostered a more complex and fragmented market where trade order flow increasingly navigates multiple marketplaces. As a registered adviser, we have an obligation to make reasonable efforts to achieve "best execution" for our clients, which drives our need to connect, directly or indirectly, with multiple trading venues so that our clients' orders can benefit from whichever venue has the best execution quality. The ability to place orders on all venues comes at a cost which may not be commensurate with the attendant benefits when the likelihood of execution on some venues is very small.

Given the concentration of ownership of the principal exchanges in the Canadian equity market, we would encourage regulators to consider whether all of these trading platforms provide uniquely different offerings for investors that justify the additional complexity introduced by an increasing number of trading venues. There are real costs associated with accessing an exchange, ranging from payment for direct market feeds to managing routing logic. These costs are borne by brokers but they are ultimately passed on to end-investors. Furthermore, the complexity added by each additional venue may increase the risk of technological or human errors.

As a result, we support reducing the scope of the OPR by requiring a minimum market share threshold in order to maintain OPR protection and the attendant benefits. We defer to policymakers in establishing an appropriate threshold, but encourage the CSA, in doing so, to be mindful of striking the appropriate balance between promoting competition and moderating the adverse effects of undue complexity and fragmentation. We agree with the CSA that information regarding the criteria and process for setting market share thresholds and identifying protected markets should be transparent and reviewed on a systematic basis to ensure it continues to be appropriate, to ensure access to equal information by all market participants and to allow market participants adequate time to respond to any changes.

2. Best Execution

Achieving best execution is of paramount importance to asset managers such as BlackRock, given that transaction costs directly impact our ability to deliver alpha performance and/or track a benchmark for our clients.

Institutional clients such as BlackRock typically employ fixed commission models with their dealers, who consequently bear the actual costs of trading in the form of exchange access fees or communications charges. This environment fosters an inherent conflict of interest for the dealers between balancing their best execution obligations to clients and routing orders in a manner that reduces their explicit trading costs. This inherent conflict is exacerbated in a multiple marketplace environment and by the costs of accessing trading venues compared to the magnitude of the rebates currently being paid by certain venues.

BlackRock strongly believes that in a complex trading environment, it is important that clients understand how their dealers are executing and routing their orders. As a result, BlackRock is supportive of the measures in the proposal that seek to provide greater transparency for investors. We particularly support the proposed new disclosure requirements that will require dealers to provide greater disclosure to their clients regarding their best execution policies and order handling and routing practices.[1] We believe that requiring dealers to disclose the identity of any marketplace and each type of intermediary to which the dealer might route orders and whether fees are paid or payments or other compensation is received by the dealer[2] will help clients understand

[1] Proposed requirements in section 4.4(c) of National Instrument 23 -101 – *Trading Rules* ("**NI 23-101**").
[2] Proposed requirements in section 4.4(c)(i) and 4.4(c)(v) of NI 23-101.

the impact of rebates on their dealers' routing decisions and may therefore limit trading behaviours that are driven by optimizing rebates.

We encourage the CSA to consider clarifying that the new disclosure requirements do not apply to dealers registered solely in the dealer category of "exempt market dealer" where they are distributing units of investment funds for which they act as investment fund manager. Since the price of these units will generally be referable to the funds' net asset value, concerns regarding best execution do not arise.

3. Prohibition on payment of rebates by marketplaces

BlackRock believes that competition among execution venues and incentives for providing liquidity have had a positive impact on market structure. Indeed, we believe that incentives to provide liquidity, including through the payment of rebates, have generally promoted price discovery in public markets and have helped foster tightened spreads as well as competition and choice among trading venues.

However, we agree with the CSA that the payment of rebates should not drive dealers' routing decisions nor distort the rationale for trading decisions. It is not the payment of rebates that are *per se* problematic, but rather the magnitude of such rebates relative to a dealers costs to access a venue and the misalignment of economic interests among market participants that raises concern. As such, BlackRock is supportive of measures that would help narrow this disparity and lessen the impact of cost in routing decisions.

In order to better balance the benefits to the marketplace of providing rebates with the potential conflicts of interest such payments may give rise to, BlackRock welcomes the proposed measures to enhance transparency discussed above under "Best Execution" and echoes some of the recent observations noted by the International Organization of Securities Commission on this issue:

> Where transparent, fees and fee models can help to ensure that information regarding the operation of the trading venue provides an understanding of the venue and the services it offers. Transparency also enables users to assess the costs associated with accessing these services. Further, the information about fees, including rebates, can help support investor confidence.[3]

Another policy option the CSA may want to consider would be to clarify a dealer's obligations to clients by identifying the circumstances when consideration of rebates and access fees are inconsistent with their best execution obligations. Achieving best execution for clients should be the sole objective in order handling and routing practices and BlackRock strongly encourages the CSA to consider initiatives which reinforce this objective.

Lastly, given that the value of liquidity – and therefore the rationale for providing rebates and other incentives – is not the same across all securities, BlackRock would also be

[3] *Trading Fee Models and their Impact on Trading Behaviour: Final Report* (December 2013) (http://www.iosco.org/library/pubdocs/pdf/IOSCOPD430.pdf)

supportive of regulatory inquiry into whether highly liquid stocks require any rebates or other volume-based incentives at all.

4. Pilot Study on the Prohibition of the Payment of Rebates

BlackRock is supportive of efforts to understand the effects of proposed market regulation such as through the pilot study contemplated in the Request for Comments regarding the prohibition on the payment on rebates. We share Staff's concerns, however, that such an examination should be conducted cautiously and judiciously so as to ensure any adverse unintended consequences, such as the widening of spreads, are minimized to the greatest extent possible.

In considering both the timing and parameters of the study, BlackRock would encourage the CSA to minimize the number of variables present which may otherwise frustrate an accurate assessment of the observable effects. For example, the implementation of parallel initiatives noted in the Request for Comments (such as amendments to the OPR) may make it difficult to isolate the impact of a prohibition on rebates. While we recognize it will be difficult to completely silo the effects of each initiative, the timing and duration of the pilot study should be thoughtfully considered to ensure that other aspects of the Request for Comments, if implemented, don't unduly "taint" the data gleaned by the pilot study.

With respect to the proposed constituents in the study, we note that the Request for Comments contemplates the inclusion of up to one-half of all exchange-traded securities. The Request for Comments is not clear as to whether exchange-traded funds ("**ETFs**") would be included in the sample. Given the unique structure of ETFs, we strongly recommend that the CSA work closely with ETF providers in selecting any ETFs for inclusion in the study to ensure that prohibitions on rebates do not impair their functioning as financial instruments or give rise to competitive disadvantages amongst similarly-situated products. For example, as ETFs are typically used for different purposes than conventional equity securities (such as to express a short-term investment view) and given that they have structural features that are qualitatively and fundamentally different (such as NAV premiums/discounts which give rise to ETF arbitrage mechanisms), liquidity is of paramount importance. We respectfully submit, therefore, that the selection of any ETFs in the sample should be subject to rigorous scrutiny and consideration to ensure that the prohibition of rebates doesn't inadvertently undermine one of their salient benefits to investors, namely liquidity. To the extent both ETFs and their underlying constituent securities are included in the pilot study, it may be difficult to isolate the impact of the prohibition of rebates given that the ETF will be impacted on two levels (i.e., both at the ETF unit level as well as on its constituent securities). In addition, if ETFs are included in the study, we would strongly recommend that particular consideration be given to the underlying benchmarks and/or investment exposure of each in order to minimize the potential for product arbitrage risk. For example, an ETF included in the sample may be competitively disadvantaged vis à vis another ETF which tracks the same or a similar benchmark but which is not included in the pilot and is therefore insulated from rebate prohibitions. This risk is similar to that noted in the Request for Comments regarding inter-listed securities as, in both cases, prohibiting rebates may unintentionally create an un-level playing field between ETFs. To the extent

these concerns are not sufficiently addressed, BlackRock would not be supportive of the inclusion of ETFs in the pilot study.

Finally, with respect to the sample size and duration of the study, if the pilot uses a large sample size of one-third to one-half of all exchange-traded securities (as contemplated in the Request for Comments), we believe that a duration of 3-6 months is likely appropriate given the volume of data that would be generated during this period. If a smaller sample size is used, a longer duration for the study may be appropriate.

5. Credits for Market Makers

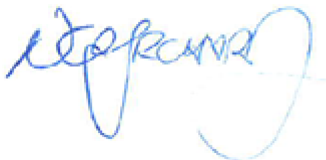
Market makers perform an essential function in capital markets by posting liquidity and creating effective two-way markets in a security. To the extent that market makers are contributing liquidity, maintaining narrow spreads and promoting price discovery, we share the CSA's view that it may be appropriate for market markets to be eligible for rebates or some other appropriate form of incentive. To ensure discount or credit programs such as these are made available only to *bona fide* liquidity providers, however, we would encourage the CSA to consider objective eligibility criteria or the use of tiers based on higher levels of trading activity. We understand, for example, that other global listing venues recently introduced incentive programs related to size, consistency, and quality of quotes.

D. Conclusion

The Canadian equity market is not broken or in need of large scale change. In our view, investors will be best served by targeted initiatives which enhance existing rules and practices to improve market structure, transparency and efficiency. We encourage the CSA to consult extensively with industry participants on the issues raised in the Request for Comments to ensure that any proposed measures foster fair and efficient capital markets and promote investor confidence. BlackRock would be pleased to make appropriate representatives available to discuss any of these comments with you.

Yours very truly,

BlackRock Asset Management Canada Limited



Noel Archard
Chief Executive Officer