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Market Regulation Branch
Ontario Securities Commission
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Paul Romain
Head of Market Structure, and
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Omega Securities Inc.
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Dear Sirs / Mesdames:

Re: Lynx ATS Notice of Proposed Changes and Request for Comment

TMX Group Limited ("TMX Group" or "we") welcomes the opportunity to comment on the Notice and Request for Comment (the "Notice") as published by the Ontario Securities Commission (the "OSC") on March 5, 2020 on behalf of Omega Securities Inc. ("OSI") outlining certain proposed functional changes to the OSI's Lynx trading platform ("Lynx 2.0"). The first two proposed changes set out in the Notice relate to:

(i) the implementation of broker preferencing for attributed visible orders, and all hidden orders; and

(ii) the addition of a Minimum Price Improvement ("MPI") peg order.

Neither of these proposed changes are novel to the Canadian capital markets, and we therefore have no comments on these proposed changes.

The third proposed change in the Notice (the "LST Access Ban") relates to a proposal to restrict access to a registered, visible marketplace, Lynx 2.0, to an arbitrary and independently defined type of participant who is labelled as a latency sensitive trader ("LST"). While TMX Group is fundamentally supportive of innovations designed to improve the liquidity and execution environment for the investment community within Canada, there are material concerns about the proposed LST Access Ban that the OSC should consider and address. As a result, we are not supportive of the OSC approving the implementation of the LST Access Ban as it is described in the Notice. TMX Group cites the following concerns:

1. Access Concerns

TMX Group recognizes the merit in attempting to improve the liquidity environment through innovations that optimize counter-party interactions while adhering to the existing regulatory principles and framework that ensures no participant is unfairly restricted from accessing marketplace liquidity. While TSX Alpha, as a speedbump marketplace, subjects all orders to a short delay in an effort to dissuade low latency arbitrage trading behaviour, it adheres to the fair access requirements and principles by ensuring all active orders are subject to the same delay regardless of a participant's designation. In addition, size restrictions are imposed on post-only orders which have shown to have a positive effect on some liquidity metrics. We are of the view that TSX Alpha is able to offer substantially similar benefits as the LST Access Ban through its speedbump without imposing definitive access restrictions on a class of participants as the LST Access Ban clearly does.

The distinction between the TSX Alpha speedbump and access restrictions have been previously assessed by the OSC when Aequitas NEO ("NEO") proposed a similar access ban in an August 13, 2013 filing. Thirty eight comments were received in response to this NEO filing, many of which expressed concerns over fair access. Ultimately, the OSC provided guidance that restricting access to a participant was not in keeping with national instrument law:

> *"The OSC reviewed the Aequitas pre-filing within the context of the current regulatory framework and more broadly, the OSC's statutory mandate to provide protection to investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets and confidence in capital markets. After a thorough review of the proposal and related comments, the OSC informed Aequitas that it could not support the proposal as published. In particular, the proposal included restrictions on access to visible orders which do not conform to existing requirements of the regulatory framework, including fair access."*[1]

Following this guidance, NEO amended their proposal to include a speedbump mechanic as opposed to an access ban.

Based on this precedent, and the existing National Instrument, we would expect the OSC to question whether the LST Access Ban unreasonably prohibits, conditions or limits access to Lynx 2.0, and whether the LST Access Ban is contrary to the principles of fair access set out in section 5.1 of National Instrument 21-101 - *Market Operations* and its companion policy.

If the OSC were to consider approving the LST Access Ban, this would represent a significant departure from the current interpretation and application of the fair access provisions within the National Instrument that we believe would require the appropriate level of industry consultation and debate independent of and in addition to the LST Access Ban proposal. In addition, to the extent that other marketplaces choose to consider similar restrictions on access if the LST Access Ban were to be approved, the result could be a systematically segregated Canadian marketplace which the OSC and the investment community has historically viewed as highly undesirable

[1] OSC Bulletin, Volume 37, Issue 3 (January 16, 2014), Section 13.2.1, Page 96.

2. Subjective Definition of LST

OSI defines LST as a Trader ID that:

a. are entered by proprietary traders of dealers or direct electronic access (DEA) clients of dealers using automated, co-location trading strategies.

b. Co-location is defined as the participant having a server located in the same data center as any Canadian exchange or ATS and using it for automated trading strategies.

The OSC should question whether the definition is unsuitably vague and subjective, and could be interpreted to include participants who are incapable of engaging in high speed latency arbitrage trading activity, contrary to its intent. For example, we understand that several major trading vendors offer co-located execution as well as automated trading strategies in the form of smart order routing or participation schedule algorithms. These vendors service a very broad group of traders, many of which can be viewed as proprietary. These proprietary traders, while clearly not in a position to profit from latency inefficiencies, could be interpreted as qualifying for inclusion according to the LST definition set forth in the Notice. Could approving the LST Access Ban provide OSI the discretion to impose restrictions on participants as it sees fit?

In addition, trader IDs that could execute orders originating from co-located and automated trading strategies, could potentially trade both proprietary and client order volume. The LST Access Ban does not provide for an exemption in these scenarios to ensure that client orders are always able to access the best available prices.

The LST definition does not afford the level of specificity such that it could only apply to the intended participants.

Additionally, OSI states in the Notice that they will "... have a process in place to monitor ID's based on a variety of metrics such as numbers of orders per day, cancel to trade ratios, number of executions, etc. If we determine that a trader ID is not classified correctly, we will immediately notify the subscriber and ask for written clarification as to the status of that trader ID."

In the above statement, OSI is referencing metrics that it feels are consistent with LST trading. However, the OSC should consider whether there is a correlation between the stated metrics that are proposed to be monitored and the type of latency arbitrage behaviour that the LST Access Ban is intended to minimize. We do not believe that there is a clear correlation between "number of orders and executions" and latency arbitrage activity, as some retail trading IDs would lead the marketplace in this regard. In addition, we would argue that the proposed "cancel to trade ratio" metric is indicative of sophisticated market making activity and not of latency sensitive price arbitrage as set out in the Notice. A successful latency arbitrage strategy would, in fact, result in a lower "cancel to trade ratio". The LST Access Ban suggests that additional metrics will be monitored but does not provide them. It is important for these metrics to be made transparent.
These metrics are stated as justification for an investigation of a trader ID. Given the broad definition of LST, any investigations could lead to material restrictions on participants, we therefore believe that it is important to provide details as to what levels would constitute a breach and trigger an investigation of a Trader ID. Given the impact of a restriction on participants, full transparency into these metrics is essential.

TSX Group also feels that the relationship between the definition of LST and the monitored metrics is not clearly outlined. In this regard, a number of questions remain unanswered including whether an ID that is in breach of the monitored metrics can be labelled LST if their orders originate from a logical engine that is not strictly within the bounds of the physical building housing an exchange or ATS matching engine?

3. Justification

TMX Group is in favour of improving the Canadian capital markets, which includes marketplace changes designed to improve the investment experience and the liquidity environment for natural investors. We are supportive of initiatives that carefully address clearly defined issues and provide measured and quantitative solutions. TMX Group is strongly opposed to marketplace mechanics that seek to contravene regulatory principles and rules, such as fair access, and especially when they do not address a recognized issue and provide an effective and measured response. For example, in the Notice OSI states:

"Despite this, natural Canadian market participants continue to be frustrated by their inability to trade without the interference from latency sensitive traders, and they continue to experience quote fade, and smaller fill rates leading to increased back office and transaction costs. "

It is not clear how the LST Access Ban will address quote fade and poor fill rates. Even with the LST Access Ban implemented, post only participants would be just as capable of cancelling at opportune times on Lynx 2.0 as they are on any other venue, and LST's would continue to be able to contribute to quote fade and poor fill rates for natural investors on Lynx 2.0. We do not believe that there is correlation between active low-latency order flow and active retail execution rates.

4. Impact Analysis

OSI states that it expects minimal impact on subscribers because "our definition of an LST trader ID will apply to a very small subset of subscribers and those subscribers are already accustomed to similar restrictions on other Canadian marketplaces."

We question whether the number of affected subscribers is an appropriate or valid measurement of potential impact. We believe it would be more appropriate to measure the percentage of average daily volume that accounts for this subset of subscribers, as a small subset of subscribers can account for significant volume. We also do not believe it to be relevant or appropriate to suggest that these participants are already accustomed to similar restrictions, as no marketplace enforces access bans. As such, we suggest that the OSC consider whether the impact of operational segregation of order flow should extend beyond the number restricted trader IDs.

5. General Concern

In the Notice, OSI states that it "does not see any effect on the systemic risk in the Canadian financial system as Lynx is an unprotected lit marketplace where marketplace participants can avoid quotes or trade through quotes on Lynx if they do not see any improved trading opportunities for their clients". While the statement is accurate as it pertains to participants choosing to avoid quotes on Lynx, we believe that unprotected marketplaces are still expected to fully consider the impact and risk of their proposals, particularly when proposing fundamental changes that are contrary to existing regulatory rules and principles. We do not feel that the ability to avoid quotes fully captures the impact for participants who would potentially be unable to execute visible better priced Lynx 2.0 quotations.

Conclusion

We believe that the LST Access Ban is contrary to the established principle of fair access, which applies equally to all marketplaces including unprotected marketplaces such as OSI.

While TMX Group agrees that fair access does not necessarily equate to equal access, the OSC should question whether an outright ban on access is consistent with the principle of fair access enshrined in National Instrument 21-101 - *Market Operations*. The LST Access Ban, as defined within the Notice, could permit unreasonable discrimination among participants, and reflects a methodology that could restrict participants unnecessarily and inappropriately. We fail to see a clearly defined issue in the Notice that is solved by implementing an outright access ban on a class of participants.

TMX Group appreciates this opportunity to express our thoughts and views.

Yours truly,

"Kevin Sampson"

Kevin Sampson
President, Equities Trading
TMX Group Limited