

13.1.8 Alpha Exchange Inc. – Notice of Proposed Changes and Request for Feedback

**ALPHA EXCHANGE INC.
NOTICE OF PROPOSED CHANGES AND REQUEST FOR FEEDBACK**

The Board of Directors of Alpha Exchange Inc. (“Alpha”) has approved amendments (“Amendments”) to the Alpha Exchange Trading Policies (“Trading Policies”). The Amendments, shown as blacklined text, are attached as Appendix “A”.

Alpha is publishing this Notice of Proposed Changes (“Notice”) in accordance with the requirements set out in the rule protocol attached to its Recognition Order. Market participants are invited to provide the Commission with feedback on the amendments.

Feedback on the proposed amendments should be in writing and submitted by May 14, 2012 to:

Market Regulation Branch
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West
Toronto, Ontario M5H 3S8
Fax: (416) 595-8940
e-mail: marketregulation@osc.gov.on.ca

And to:

Randee Pavalow
Alpha Exchange Inc.
70 York Street, Suite 1501
Toronto, Ontario M5J 1S9
Fax: (416) 642-2120
e-mail: randee.pavalow@alpha-group.ca

Comments received will be made public on the OSC website. Upon completion of the review by OSC staff, and in the absence of any regulatory concerns, notice will be published to confirm the completion of Commission staff’s review and to outline the intended implementation date of the changes.

Terms not defined in this Notice are defined in the Alpha Exchange Inc. Trading Policies.

DESCRIPTION OF THE RULE AND ITS IMPACT¹

Changes to IntraSpread™

Alpha is proposing to amend the IntraSpread™ functionality to allow for matching among Dark orders at the mid-point of the NBBO.

The Amendments include two new attributes for Dark orders:

- (1) A Contra Order Type Matching Preference (COMP) attribute, which determines which of the types of orders the Dark order will trade against:
 - Trade only with incoming SDL™ orders
 - Trade only with other Dark orders, whether resting or incoming
 - Trade with both SDL™ and Dark orders

Dark orders with COMP attribute that supports matching with Dark orders can only be priced at 50 per cent of the spread.
- (2) A Minimum Acceptable Quantity (MAQ) attribute, which optionally limits the size that the Dark order will trade against, when trading with other Dark orders. The MAQ condition does not apply to trades against SDL orders.

Under the Amendments, a Dark order marked for Self Trade Management (STM) will not trade with a matching STM Dark order on the other side of the book. Two such orders will remain in the book, and continue to be eligible for trading with other orders, but will not trade with each other.

Changes to the Opening

Alpha is proposing to amend the Opening Auction functionality to provide additional validation of the Calculated Opening Price (COP) and to provide more flexibility for managing the delayed opening state of the CLOB.

(1) Validating the COP

Existing functionality validates the COP to ensure it falls within the Opening Deviation Price Band, which is determined as previous day's Adjusted Closing Price plus/minus the Opening Deviation parameter. The Amendments include an additional validation of the COP to ensure it falls within the Opening Market Conditions Price Band, which is determined as the highest/lowest of the NBB, NBO and NLSP plus/minus the Opening Market Conditions parameter. The NBB and NBO represent the best displayed prices of any market with the exception of Alpha and any halted or frozen markets.

COP Validation Example

Adjusted Closing Price is \$4.99
Opening Deviation parameter is 10% .
=> Opening Deviation Price Band= $\$4.99 \pm (0.1 * \$4.99) = [\$4.49, \$5.49]$

NLSP is \$4.99, NBB is \$5.01 and NBO is \$5.00.
Min (NLSP, NBB, NBO) = \$4.99
Max (NLSP, NBB, NBO) = \$5.01
Opening Market Conditions parameter is \$0.02.
=> The Opening Market Conditions Price Band = $[\$4.97, \$5.03]$

The symbol will open without delay if the COP falls within both price bands, which is between \$4.97 and \$5.03.

Opening Market Conditions Price Band validation is optional and is enabled on a security by security basis. Securities where the COP is validated against the Opening Market Conditions Price Band will open with a price which is in line with the current market conditions on other markets.

¹ For examples, please see IntraSpread™ Product Sheet and Opening Product Sheet at Alpha Exchange web site: www.alpha-group.ca

(2) Managing the Delayed Opening

When the COP is not within applicable price bands, the opening is delayed.

With current functionality, when the book is in the delayed opening state, Members can only cancel orders. With the Amendments, Members can also enter new and amend existing orders. With every order change in the book, the COP is recalculated and re-validated using updated market conditions. In the absence of user activity, the re-validation is performed periodically by the system.

Under proposed Amendments, the book will automatically transition into Continuous Trading session once the COP falls within the applicable price bands. In addition, as with the current functionality, Alpha Trading Services can manually force the opening at the COP if deemed necessary.

NATURE, PURPOSE AND INTENDED EFFECT OF THE RULE

Changes to IntraSpread™

The proposed changes to IntraSpread™ functionality are intended to promote block trading, and attract more natural institutional flow in IntraSpread™ to achieve additional benefits for participants.

Changes to the Opening

With the Amendments, the price of the opening trades will better reflect the current environment of a multi-marketplace environment and be more in line with the market conditions at the time of the opening.

The new mechanism will also allow for a speedy resolution of a delayed opening state through natural market activity, as opposed to the current, manual intervention by Alpha Trading Services, thus reducing the market risk for Members and end investors.

POSSIBLE EFFECTS OF THE RULE ON MARKETPLACE PARTICIPANTS, COMPETITION AND COSTS OF COMPLIANCE

Changes to IntraSpread™

Access to proposed additional IntraSpread™ functionality by Members is optional, there are no compliance requirements. Marketplace participants interested in matching larger sized orders in IntraSpread™ will need to adjust their trading strategies to properly account for the new features.

Changes to the Opening

The new rule should improve the quality of the opening at Alpha as well as price discovery among all marketplaces at this key time in the day.

DESCRIPTION OF HOW RULE WAS DEVELOPED

Changes to IntraSpread™

The IntraSpread™ functionality was developed based on requests and comments from Alpha clients to allow institutional order flow to participate on the active side in IntraSpread™.

Changes to the Opening

The proposed changes were developed after observing the problems of the current, traditional Opening Auction mechanism in the context of multiple marketplaces. Multiple solutions were analyzed internally and discussed with clients, including the options to re-price trades executed outside of a price band, as well as to re-route orders that violate the opening price band to other markets for execution. The final proposal was elected as an efficient solution to a complex issue and reduces the risks associated with multiple opening auctions on separate marketplaces.

TECHNOLOGY IMPACT AND IMPLEMENTATION:

Changes to IntraSpread™

The Amendments include low-risk changes for the Alpha Exchange trading system.

Members and vendors interested in accessing the new functionality will need to include the new attributes in the interface with Alpha Exchange and adjust their trading strategies to incorporate new Dark order types. The default behavior corresponds to the existing functionality; therefore Members accessing IntraSpread™ today that are not interested in the new functionality will not need to make any changes.

Changes to the Opening

The change to the opening mechanism is transparent to the Members. All technology changes are to be done by Alpha Exchange, and there are no changes to the data protocols. The proposed changes are low-risk technology changes for the Alpha trading system.

EXISTENCE OF COMPARABLE RULES IN CANADA OR OUTSIDE OF CANADA

Changes to IntraSpread™

Numerous dark pool examples focused on block-trading exist today in and outside of Canada.

The MAQ condition is a standard order attribute applicable to non-transparent orders, supported in Canada by MatchNow, TMX, Goldman Sachs, BATS, Turquoise and others.

COMP attribute as proposed is tailored to IntraSpread™ implementation, but similar concepts are implemented by BIDS and Credit Suisse liquidity pools.

Changes to the Opening

No directly comparable models were found in or outside of Canada. The Nasdaq Options Market Opening Auction market is one example of an opening model that takes into account NBBO conditions when determining the COP.

The Canadian market still dominantly depends on the listing market for the opening price regardless of where the majority of trading occurs. In the US, the rules allow for an environment where dealers can internalize retail orders and guarantee the opening price of any given marketplace, and therefore few models were developed to harmonize opening prices across multiple marketplaces.

CATEGORIZATION AS PUBLIC INTEREST RULE

Alpha believes the proposed changes not only add trading choices but also are not contrary to the public interest.

APPENDIX A

The following sets out the proposed black lined amendments to the Alpha Exchange Inc. Trading Policies. A complete version of the black lined Trading Policies can be found at www.alpha-group.ca

1.1 DEFINITIONS

<u>Contra Order Matching Preference (COMP)</u>	<u>Dark order designation identifying which orders in the IntraSpread™ facility the Dark order will trade against.</u>
<u>Minimum Acceptable Quantity (MAQ)</u>	<u>Optional minimum acceptable execution quantity condition attached to a Dark order.</u>
<u>Opening Market Condition Security (OMC Security)</u>	<u>A security identified by Alpha through a Trading Notice as subject to an Opening Market Conditions price band validation.</u>

5.16 SELF TRADE MANAGEMENT

- (1) Alpha Self Trade Management is a designation that suppresses trades that occur in the Continuous Trading Session in the CLOB from the public feed, and prevents trades between two Dark orders in the IntraSpread™ facility, where orders on both sides of the trade are from the same Member and contain the same “self trade key” set by the Member.
- (2) Self Trade Management applies only to unintentional trading (e.g. does not apply to intentional crosses).
- (3) The designation is only applicable in Continuous Trading in CLOB and IntraSpread™.
- (4) Self trades that occur in the CLOB Continuous Trading Session are not disseminated on the public trade messages and do not update the last sale price, daily volume and turnover, or other trading statistics.

5.23 ALPHA INTRASPREAD™ FACILITY

- (1) Scope
 - (a) Alpha IntraSpread™ facility allows Members to seek order matches without pre-trade transparency, with guaranteed price improvement for active orders.
 - (b) The IntraSpread™ facility is available to all Members and for all symbols traded on Alpha ATS.
 - (c) Order types in the Alpha IntraSpread™ facility include Dark orders and Seek Dark Liquidity™ (SDL™) orders.
- (2) Dark Orders
 - (a) The Dark order is a fully hidden order, ~~used to manage passive interest with no pre-trade transparency. It offers price improvement to tradable incoming orders. Dark orders trade only with incoming SDL™ orders that are tradable at the calculated price of the Dark order and do not trade with other Dark orders.~~

Commentary: Dark orders have no pre-trade transparency as information on Dark orders is not disseminated on any public feeds.

- (b) Based on the COMP attribute, the Dark order can trade as follows:
 - (i) Only with incoming SDL™ orders
 - (ii) only with other Dark orders, or
 - (iii) with both SDL™ and Dark orders.
- (c) The price of a Dark order is calculated as an offset of the NBBO by adding the price offset to the national best bid for a buy order and subtracting it from the national best offer for a sell order.
 - (i) The price offset is calculated as a percentage of the NBBO spread with one of two values: 10 % (capped to one standard price increment), or 50% (with no tick cap); however, Dark

orders with a COMP attribute that supports trading with other Dark orders can only have the 50% price offset value.

- (ii) The price of the Dark order can be optionally capped.
- (iii) If either side of the NBBO is not set, or the NBBO is locked or crossed, Dark orders will not trade.
- (d) Dark orders must be for a board lot quantity and are day only orders.
- (e) Dark orders cannot be Iceberg, On-Stop, Inside Match, FOK, FAK, MOO, LOO, MOC, Special Terms, Bypass, Passive Only, TTM or ROC.
- (f) Dark orders can be amended for quantity, price offset and price cap, in addition to other standard amendable order attributes.
- (g) Dark order marked with the MAQ attribute may specify the minimum acceptable number of shares that it will trade against when trading with another Dark order. The MAQ condition does not apply to trades against SDL orders.
- (h) Dark orders marked with the STM attribute will not trade with a matching STM marked Dark order from the same Member account.

All of the following examples have been removed.

Example of IntraSpread™ Matching

Alpha IntraSpread Book							
Order #	RR Priority	Time of Entry	Order Type	Bid Broker	Bid Size	NBBO Offset	Calculated Price
2	2	10:10am	Dark	A	200	50%	25.035
3	3	10:15am	Dark	A	800	50%	25.035
4	4	10:20am	Dark	B	600	50%	25.035
5	5	10:25am	Dark	A	1,000	50%	25.035
1	1	10:00am	Dark	A	500	10%	25.023

If dealer A enters SDL order #6 to sell 300 at 25.02, the following trade will occur:

- ~~300 @ 25.035 (order #6/order #3)~~

Priority:

- ~~Orders #2, #3, #4, and #5 have priority over #1 based on price~~
- ~~Orders #2, #3, and #5 have priority over #4 based on broker preferencing~~
- ~~Orders #3 and #5 have priority over #2 based on smart size~~
- ~~Order #3 has priority over #5 based on round robin~~

The state of the book is now as follows:

Alpha IntraSpread Book							
Order #	RR Priority	Time of Entry	Order Type	Bid Broker	Bid Size	NBBO Offset	Calculated Price
2	2	10:10am	Dark	A	200	50%	25.035
4	4	10:20am	Dark	B	600	50%	25.035
5	5	10:25am	Dark	A	1,000	50%	25.035
3	6	10:15am	Dark	A	500	50%	25.035
1	1	10:00am	Dark	A	500	10%	25.023

If dealer A then enters SDL order #7 to sell 300 at 25.02, the following trade will occur:

- ~~300 @ 25.035 (order #5/order #7)~~

Priority:

- ~~Orders #2, #3, #4, and #5 have priority over #1 based on price~~
- ~~Orders #2, #3, and #5 have priority over #4 based on broker preferencing~~
- ~~Orders #3 and #5 have priority over #2 based on smart size~~

• ~~Order #5 has priority over #3 based on round robin~~
 The state of the book is now as follows:

Alpha IntraSpread Book							
Order #	RR Priority	Time of Entry	Order Type	Bid Broker	Bid Size	NBBO Offset	Calculated Price
2	2	10:10am	Dark	A	200	50%	25.035
4	4	10:20am	Dark	B	600	50%	25.035
3	6	10:15am	Dark	A	500	50%	25.035
5	7	10:25am	Dark	A	700	50%	25.035
1	1	10:00am	Dark	A	500	10%	25.023

If dealer A then enters ~~SDL order #8 to sell 900 at 25.02~~, the following trades will occur:

- ~~200 @ 25.035 (order #2/order #8)~~
- ~~500 @ 25.035 (order #3/order #8)~~
- ~~200 @ 25.035 (order #5/order #8)~~

Priority:

- ~~Orders #2, #3, #4, and #5 have priority over #1 based on price~~
- ~~Orders #2, #3, and #5 have priority over #4 based on broker preferencing. No orders have priority based on smart size~~
- ~~Order #2 has priority over #3, and #3 over #5 based on round robin~~

The state of the book is now as follows:

Alpha IntraSpread Book							
Order #	RR Priority	Time of Entry	Order Type	Bid Broker	Bid Size	NBBO Offset	Calculated Price
4	4	10:20am	Dark	B	600	50%	25.035
5	8	10:25am	Dark	A	500	50%	25.035
1	1	10:00am	Dark	A	500	10%	25.023

If dealer C then enters ~~SDL order #9 to sell 1,800 at 25.02~~, the following trades will occur:

- ~~600 @ 25.035 (order #4/order #9)~~
- ~~500 @ 25.035 (order #5/order #9)~~
- ~~500 @ 25.023 (order #1/order #9)~~

Priority:

- ~~Orders #4 and #5 have priority over #1 based on price~~
- ~~No orders have priority based on broker preferencing~~
- ~~No orders have priority based on smart size~~
- ~~Order #4 has priority over #5 based on round robin~~

The book is now empty.

5.25 OPENING CALL

- (3) The Opening Call for each security will occur at a random time between 9:30:00 a.m. and a time specified by Notice.
- (4) Each security will open at the COP.

Commentary: The COP is calculated to maximize the traded volume. If there are two prices at which the same volume will trade, the COP is the price that will leave the smallest imbalance. If there is more than one price that satisfies the second rule, then the price that does not leave the better priced order in the book will be the COP. If the imbalances are equal, and no price leaves better priced orders in the book, the price will be the one closest to the previous day's closing price. For the purposes of determining the COP, Market Orders are assigned the worst price on the opposite side of the book, or if that price is not available, the best price of its own side.

5.26 DELAYED OPENINGS

- (5) Alpha may delay the opening of a security for trading on Alpha ~~if~~for the following reasons:
- (a) Opening Deviation Price Band Validation. If ~~the~~ COP differs from the previous day's ACP (adjusted to the Closing price of the listing marketplace) by an amount greater than the price band parameters set by Alpha and provided to Members by way of a Member Notice, or
 - (b) Opening Markets Conditions Price Validation. If the COP of an OMC Security is
 - (i) Lower than the minimum of the NBB, NBO and NLSP by more than the market conditions price variation parameter, or
 - (ii) Higher than the maximum of the NBB, NBO and NLSP by more than the market conditions price variation parameter.
 - (c) Alpha determines that it is appropriate due to market conditions.

Commentary: If a security is listed on both Alpha and another Canadian exchange, the ACP will be based on the closing price of the initial listing marketplace.

- (6) During a delayed opening, a Member may place new orders and cancel or amend existing orders regarding the security that is subject to the delay.

Commentary: With every change in the book, the COP is recalculated and revalidated using the updated pricing band validation and can move out of the delayed state immediately.