CANADIAN® SECURITIES EXCHANGE
The Exchange For Entrepreneurs

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Market regulation Branch
Ontario Securities Commission
20 Queen Street West, 22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-595-8940
marketregulation@osc.gov.on.ca

Matt Thompson
Chief Compliance Officer
Nasdaq CXC Limited
25 York Street, Suite 900
Toronto, Ontario M5J 2V5
matthew.thompson@nasdaq.com

Re: **Notice of Proposed Changes and Request for Comment – New options for Trading Book – Minimum size exception for retail orders and preferred counterparties**

Dear Mr. Thompson:

The Canadian Securities Exchange ("CSE") appreciates the opportunity to comment on the Notice of Proposed Changes and Request for Comment published by the Ontario Securities Commission on April 23, 2020 on behalf of Nasdaq CXC Limited ("Nasdaq Canada").

Nasdaq Canada's proposal presents three new options on how participants will be able to match orders on the "CXD Trading Book" using limiting variants of the Minimum Acceptable Quantity and Minimum Quantity order types (collectively, "MQO's"). Depending on which of the three new options are used, and how the orders are characterized, participants will be able to limit interaction of their orders to a subset of market participants' contra orders.

CSE has three principal concerns with the proposal regarding: 1) fair access to marketplaces, 2) introduction of moral hazard, and 3) establishing an incorrect regulatory precedent supporting further fragmentation of the price discovery process. It is the CSE's view that the proposal should not receive regulatory approval.

1. Fair Access

Fair access is a fundamental basis for the proper functioning of marketplaces.[1] This is one of the areas of compliance focus for the Canadian Securities Administrators.[2]

The proposal blurs the lines between:

(i) a private dark pool for large market participants, ensuring internalization with their own flow (retail or otherwise) or matching with retail flow from preferred counterparties, and
(ii) a fair access dark trading venue where all participants have the potential to interact with contra orders, given the same circumstances.

Under the proposal many participants would be disenfranchised, unable to interact with passive liquidity.

[1] "A marketplace must **not unreasonably prohibit, condition or limit access** by a person or company to services offered by it." (emphasis added). S. 5.1(1) National Instrument 21-101 *Marketplace Operation*. https://www.osc.gov.on.ca/documents/en/Securities-Category2/ni_20170201_21-101_unofficial-consolidation-forms-cp.pdf.
[2] See, s. 11.5 of Companion Policy 21-101 CP *Marketplace Operation*.

2. Internalization Moral Hazard

Under the proposal, participants will be able to set high minimum quantity thresholds on their MQO's. There would be a very low probability of the MQO's interacting with incoming order flow (with most incoming orders being below the high minimum threshold). A participant's resting high threshold MQO's would ignore all orders other than their own retail flow or retail flow from their chosen counterparties; with these participants having the capacity to further internalize by sending their own orders (retail or otherwise) below the high threshold for matching.

Nasdaq Canada acknowledges there are inherent concerns with this order type. In order to prevent such "*potential unintended consequences*", Nasdaq Canada proposes that the maximum value (i.e. the highest minimum quantity) for the Minimum Quantity Order will be determined on a discretionary basis by the Nasdaq Canada.

Nasdaq Canada's discretionary capping is not an adequate safeguard. There would need to be a formal and transparent methodology on choosing cap size. In the absence of a clear and equitable basis on choosing a cap size, there is considerable risk that Nasdaq Canada would be incented to increase the maximum cap to the benefit of large participants who wish to internalize.

3. Fragmentation precedent

By approving more features that allow differentiated treatment of participants based on their trading categorization (i.e. "retail", "institutional", "HFT"), the regulators would be condoning further fragmentation of the markets. While participant category is an important differentiator in how a participant manages order flow, fundamentally this should not influence how marketplace systems treat their respective orders. Approval of the proposal sends a message that differentiated treatment of market participants is fair game, and there would inevitably be a surge in new order types excluding certain participants out of markets based on their category. This is not a path the CSE believes would improve the price discovery system, market fairness or integrity in Canada.

Long-term investors

In assessing the proposal, it is noted that the term "long term investor" is used without definition. Benefits are implied for long term investors but without clarity as to the specific classes of investors that fall within this category, it is not possible to comment on such suggested benefits.

Sincerely,

Jamie Anderson
General Counsel & Corporate Secretary