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VIA E-MAIL

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Dear Sirs/Mesdames:

Re: CSA/CIRO Staff Notice 23-331 - Request for Feedback on December 2022 SEC Market Structure Proposals and Potential Impact on Canadian Capital Markets, dated October 19, 2023 (the "Request for Comment")

TMX Group Limited ("**TMX**" or "**we**"), welcomes the opportunity to comment on the Request for Comment. We commend the Canadian Securities Administrators ("**CSA**") and the Canadian Investment Regulatory Organization ("**CIRO**") for taking the time to seek industry feedback to help analyze the potential impacts that significant regulatory changes to the U.S. equity market structure may have on the Canadian equities markets.

All capitalized terms used but not defined in this letter have the meaning as set out in the Request for Comment.

TMX

TMX is an integrated, multi-asset class exchange group. TMX's key subsidiaries operate cash and derivatives markets for multiple asset classes, including equities and fixed income, and provide clearing facilities, data driven solutions and other services to domestic and global financial and energy markets. Toronto Stock Exchange, TSX Venture Exchange, Alpha Exchange, The Canadian Depository for Securities, Montreal Exchange, Canadian Derivatives Clearing Corporation, Shorcan Brokers Limited and other TMX Group companies provide securities listing markets, trading markets, clearing facilities, data products and other services to the global financial community and play a central role in Canadian capital and financial markets.

The Request for Comment

The CSA and CIRO are requesting comments on the possible potential impacts on the Canadian capital markets from, and appropriate policy responses to, recent proposals by the the United States Securities and Exchange Commission (the "**SEC**") to amend various SEC rules relating to market structure and practices in the U.S. securities market. The SEC proposals, which were published on December 14 2022, relate to (i) Minimum Pricing Increments, Access Fees and Transparency of Better Priced Orders; (ii) Regulation Best Execution; (iii) Disclosure of Order Execution Information; and (iv) Order Competition Rule.

Our comments address each of the SEC proposals.

(i) <u>Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders</u>

The SEC proposal seeks to amend certain Regulation NMS rules that would adopt minimum tick size and trading increments for quoting and trading NMS stocks, reduce access fee caps, and enhance the transparency of better priced orders. As explained below, TMX is of the view that tick sizes in the Canadian listed market should be harmonized with those prevailing in the U.S. markets. We concur with the initial view of the CSA that the SEC's proposals to enhance transparency of better priced orders in the U.S. markets are inapplicable or unnecessary to the Canadian market.

a) <u>Variable Minimum Pricing Increments</u>

The SEC is proposing to assign one of four minimum pricing increments (or "tick sizes"), ranging from USD$0.001 to USD$0.01, for the quoting and trading of NMS securities priced at or above USD$1.00 per share based on the time-weighted average quoted spread on U.S. marketplaces during an evaluation period, with the minimum pricing increment recalculated on a quarterly basis.

TMX strongly supports harmonizing tick sizes on the Canadian markets with those prevailing in the U.S. markets *for all securities* traded on Canadian securities markets.

Impact in Canada on Interlisted Securities

A change on tick sizes on U.S. markets will directly impact Canada, where interlisted securities will be most affected. As at October 31, 2023, there were a total of 183 issuers listed on TSX that were interlisted on New York Stock Exchange or NASDAQ, and 23 issuers listed on TSXV that were interlisted on New York Stock Exchange or NASDAQ. Should the SEC adopt the minimum pricing increment proposal, it is imperative that Canada respond with harmonized tick sizes to ensure continued fair competition between Canadian marketplaces and market participants and the U.S. markets, and among other U.S. trading venues that already offer sub-penny trading. TMX is of the view that tick sizes in Canada should be harmonized with the U.S. not only for interlisted securities, but for all securities. Securities listed on Canadian marketplaces but not in the U.S. often trade heavily on the over the counter markets in the U.S.[1], particularly with retail investors. Accordingly, harmonized tick sizes for trading in all securities listed on Canadian markets better enables Canadian markets to compete for liquidity with the U.S. markets, including the OTC markets.

If the Canadian and U.S. tick size requirements were not aligned, it is likely that market participants would favour U.S. trading venues, lessening order flow to Canadian markets for all Canadian securities. This is because liquidity providers would prefer a market with greater pricing optionality that the tick size proposal would bring, driving liquidity takers to the more liquid market.

TMX is of the view that Canada should adopt a methodology for adjusting tick sizes that ensures that the tick sizes of all securities are always aligned, regardless of whether a particular methodology might otherwise yield different results (i.e., where the time-weighted average quoted spreads in Canada and the U.S. are different for the same security). Maintaining alignment between the two markets is necessary to minimize the opportunities for arbitrage of interlisted securities and to maintain the competitiveness of Canadian markets for all securities.

Effect of Currency Exchange

Given the relative minor fluctuations between the foreign exchange rate between the American and Canadian dollar, TMX does not believe that the difference in value between the American and the Canadian dollar is a relevant factor that marketplace participants will consider in their order flow routing decisions.

Increased Message Traffic

The Request for Comment identified concerns over the increase in message traffic that will likely result from an increase in the number of pricing increments. TMX shares these concerns.

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[1] For example, as at October 31, 2023, 33% of our TSX and TSXV corporate issuers were trading on OTCQX or OTCQB.

Message traffic generally has been increasing over the last several years, and a significant reduction in tick sizes is likely to cause a further and sudden spike that will create increased costs across the U.S. and Canadian markets (if adopted). While the increase in message traffic is a concern that both the U.S. and Canadian regulators should consider, TMX maintains that Canada *must* harmonize tick sizes with the U.S. so that our markets remain competitive with the U.S. markets.

Operational Resiliency and Systems Readiness

TMX is of the view that, if adopted, the regulators should provide stakeholders with sufficient lead-time between establishing and implementing new minimum trading increments both initially and on an ongoing basis in order to adjust and build out any required infrastructure and systems changes. While adequate lead-in time is required, we are also of the view that any corresponding tick size amendments in Canada must be implemented *concurrently* with the implementation of the amendments in the U.S. We urge the CSA to have continued dialogue with the SEC to ensure concurrent implementation between Canada and the U.S. as any prolonged delay in implementation in Canada may hinder our ability to properly compete with our U.S. counterparts, and may cause disruptions to the Canadian markets.

Complexities in Managing Orders

Managing existing orders entered on marketplaces when tick sizes are changed presents certain challenges. Open orders existing at the time that the tick size changes will become invalid. On the other hand, in the event that a security becomes less liquid and tick sizes increase, it is likely that good-til-cancelled ("**GTC**") orders will need to be repriced to an appropriate tick size. This may be more of an issue for retail firms that have a larger number of open orders and make greater use of GTC order types. Any pricing changes that occur as a result will require client communication, raising the likelihood that resetting tick sizes should be afforded longer than the one day evaluation period currently proposed by the SEC.

Under the SEC's proposal, tick sizes would be reevaluated quarterly, which TMX agrees is reasonable. Although TMX would be prepared to perform the calculations set out in the SEC proposal (i.e. calculating the required evaluations a day after the month end based on data from the previous month), the SEC's proposal raises concerns. Under the SEC proposal, calculations, dissemination, and changes of tick sizes would all have to take place between one day's close and the next day's open. Such a compressed schedule may have an adverse effect on the markets' ability to ensure that data obtained during the evaluation period is subject to adequate quality control and testing and to deploy the change throughout applicable systems. Moreover, as discussed above, brokers may not have sufficient time to discuss and address order management issues with clients. Although the need to periodically reset tick sizes is clear, we encourage the CSA to engage with the SEC to address ensuring a more appropriate interval to implement tick size adjustments.

Determination of a "Better Price" under UMIR

TMX is of the view that modifying trading increments in Canada would not impact the determination of a "better price" under UMIR, and that participants would still be able to provide meaningful price improvement in circumstances where a "better price" is required. We believe that our existing rules work well for securities with different tick sizes and should continue to work well in a new tick size environment.

Expected Outcomes and Appropriate Evaluation Metrics

With respect to expected outcomes associated with any changes to minimum trading increments, TMX is of the view that:

- message traffic will increase (as discussed above);
- trading volume will likely increase due to traders engaging in proprietary trading having pricing options enabling them to get inside of other orders;
- bid-ask spreads for securities that generally trade at much wider spreads will narrow; and
- institutional trade execution costs may decline due to tighter bid-ask spreads, which may, in turn, lead to increased trading activity.

It may be challenging for the regulators to determine which metrics are appropriate when considering whether any new approach to minimum trading increments results in positive or negative outcomes, given there are many variables at play at any given time. These variables include market wide volatility, liquidity demand, and other regulatory or marketplace changes over a period of time. Perhaps the only way to address such complexity is an understanding that the metrics may need to evolve over time and should be periodically reassessed.

b) <u>Fee Tiers</u>

The SEC is proposing to require that all exchange fees and rebates be determinable at the time of execution rather than at the end of the month based on trading during the month of a participant. The trading venue would be required to set volume thresholds or "tiers" using past volume so that market participants are able to determine what fee or rebate level would be applicable to any submitted order at the time of execution.

Unlike the U.S., Canada has very limited fee tiering and its model is driven by raw volume, rather than by relative share of volume, as in the U.S. The trading volume percentages tend to remain fairly static over time, resulting in pricing tiers having minimal (if any) fluctuations and therefore, participants experiencing consistent pricing for extended periods of time. Although TMX would not be opposed to the implementation of the SEC's proposal on access fee caps, TMX sees little or no benefit to it in the context of the Canadian markets.

c) Enhance Transparency about Better Priced Orders Available in the Market

Rather than relying on exchange rules, the SEC is proposing to require the inclusion of a definition of “round lot”, and the addition of “odd-lot” quotes in market data feeds.

In Canada, odd lot data already is available and there are limited circumstances that permit off-exchange trading of listed securities. This obviates the need in Canada to adopt a proposal similar to the SEC’s for enhancing the transparency of better priced orders. Accordingly, TMX shares the preliminary views of the CSA and CIRO that transparency of order and trade data is already sufficient in Canada without regulatory intervention. Furthermore, Canada has relatively few stocks trading over $250 per share when compared to the U.S., and it appears that the proposal in the U.S. is aimed at improving retail price improvement metrics in the U.S. These metrics do not apply in Canada due to a lack of bilateral payment for order flow and internalizing.

While TMX is of the view that the proposed amendments would not benefit the Canadian markets, a more general discussion around the trading of odd lots and fractional shares in the Canadian market is warranted. For example, consideration should be given to aligning Canadian market practice with the U.S. and European markets, which have a trading increment of one share and where odd lots and fractional shares appear to trade more seamlessly when compared to the Canadian markets. TMX welcomes the opportunity to discuss with the CSA and CIRO whether any changes to the definition of a “standard trading unit” in UMIR are appropriate.

(ii) Regulation Best Execution

Pursuant to the SEC proposal, the SEC seeks to, among other things, (i) adopt a new rule requiring broker-dealers to obtain the best execution for their customers’ orders (in addition to the existing best execution requirements under the applicable FINRA and MSRB rules); (ii) adopt provisions to address potentially conflicted transactions with retail customers, including payment for order flow to retail brokers; (iii) establish, maintain and enforce policies and procedure designed to comply with the best execution standards; and (iv) require quarterly and annual review processes (the “**SEC Best Execution Requirements**”).

These proposals require no changes to the current Canadian regulatory framework. As noted in the Request for Comment, dealers and advisors in Canada are currently required to make reasonable efforts to achieve best execution when acting for a client (i.e. obtain the most advantageous execution terms for a client order reasonably available under the circumstances)[2], and similar to the SEC Best Execution Requirements, are required to adopt best execution policies and procedures, and annually review such policies and procedures[3] (the “**Canadian Best Execution Requirements**”).

[2] See IDPC Rule 3100 Part C – Best Execution of Client Orders and Part IV of NI 23-101.
[3] IDPC Rule section 3126 – Review of best execution policies and procedures.

Given that the SEC Best Execution Requirements are similar to, and do not conflict with, the Canadian Best Execution Requirements, TMX shares CIRO's and the CSA's preliminary view that the US Best Execution Requirements likely do not have any implications for the Canadian best execution regime and no impact on the Canadian capital markets, and as such, no amendments to the Canadian Best Execution Requirements are necessary or appropriate.

(iii) Disclosure of Order Execution Information

The SEC is also proposing to update and expand the "market quality" data required to be reported by various market venues under SEC Rule 605, expand the definition of "covered orders" as well as the scope of entities subject to Rule 605, and to amend certain reporting categories and information required to be reported under Rule 605.

TMX shares the preliminary view of the CSA and CIRO that the SEC proposal with respect to the disclosure of order execution information should not affect Canadian markets given there are no equivalent disclosure requirements in Canada.

The CSA determined in the past not to proceed with a similar proposal (previously published in 2007 and 2008[4]) which would have required (i) marketplaces to publish monthly reports on liquidity, trading statistics and speed and certainty of execution; and (ii) dealers to publish quarterly reports on routing of orders when acting as agent (similar to SEC Rule 605). TMX agrees with that determination based upon the view that the minimal benefits that would be experienced by the introduction of such a requirement would be outweighed by the undue burden on the capital markets. Such reporting would require significant staffing and technological effort by marketplaces and dealers, but would likely not be well used by market participants.

(iv) Order Competition Rule

The SEC is proposing to require certain orders from retail investors to be exposed to an auction mechanism before those orders could be executed internally by any trading center that restricts order-by-order competition. This proposal is not applicable to Canadian markets insofar that in Canada, orders are generally not permitted to be internalized by a trading venue or dealer that restricts order-by-order competition. TMX agrees with the CSA's and CIRO's preliminary view that the issues addressed by the SEC proposal regarding order competition do not exist in Canada, and therefore, changes to the applicable rules in National Instrument 21-101 *Marketplace Operation* or UMIR are not required in this regard.

Concurrent Implementation of Proposed Amendments in Canada and the U.S.

TMX understands that neither the CSA nor CIRO is proposing any changes to the regulatory framework in Canada based on the SEC proposal at this time, and that any proposed changes that may result from this consultation will be published in a separate request for comment.

[4] See Notice and Proposed Amendments here and here.

Implementation by the SEC of these proposals is uncertain. Nevertheless, given that the SEC is reportedly aiming to finalize its policies in April 2024, we strongly urge the CSA and CIRO to solicit feedback on any corresponding proposed amendments to the Canadian framework as soon as reasonably possible and to provide an adequate comment period to allow all stakeholders sufficient time to provide meaningful feedback on the proposals. We also urge the CSA and CIRO to continue dialogue with the SEC to ensure minimal impact for the Canadian market (especially as a result of changes to tick sizes) and to ensure an opportunity for congruent implementation in the two jurisdictions of any changes.

We appreciate the opportunity to respond to the Request for Comment. We would be pleased to discuss in more detail at your convenience.

Sincerely,

"Rizwan Awan"

Rizwan Awan
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TMX Group Limited