13.2.2 TSX – Notice of Approval – Market on Close Facility and Amendments to Section 4-902 of the TSX Rule Book

TORONTO STOCK EXCHANGE

NOTICE OF APPROVAL

**MARKET ON CLOSE FACILITY
AND AMENDMENTS TO SECTION 4-902 OF THE TORONTO STOCK EXCHANGE RULE BOOK**

Introduction

In accordance with the Process for the Review and Approval of Rules and the Information contained in Form 21-101F1 and the Exhibits thereto (the "Protocol"), Toronto Stock Exchange ("TSX") has adopted, and the OSC has approved, amendments (the "Amendments") to Section 4-902 of the Toronto Stock Exchange Rule Book (the "TSX Rules"). The Amendments are public interest amendments to the TSX Rules. The Amendments were published for public comment in a request for comments on May 1, 2014 ("Request for Comments").

Reasons for the Amendments

In response to client requests to re-examine the structure of the Market-on-Close ("MOC") facility, TSX hosted a number of forum discussions and individual meetings with Buy Side institutions and Sell Side dealers. Those consulted were market professionals, well versed with both the rules of continuous trading and the closing auction offered on TSX and were also significant users of the MOC facility. They represented trading interests across Canada and the United States.

We learned that the board lot restriction for closing orders created an inconvenience for MOC users who would like a definitive closing price for a given basket of securities, but where the constituent composition may result in mixed or odd lot orders. In dealing with this restriction today, participants often place board lot volumes into the MOC facility, while placing remaining odd lot quantity into the continuous session just prior to the close, ultimately being filled by the registered trader at prices different than the closing price. These odd lot orders entered just before the close also increase registered trader's overnight risk as there is not enough time to off-load any accumulated positions.

We also discovered that the MOC facility works well for traders who are seeking the closing price but are less price sensitive. It was identified by the MOC users that there are traders with discretion over their orders whose goal is to achieve the closing price but with the additional objective of value preservation. Allowing price limits on orders entered prior to the imbalance dissemination would aid value preservation and enable traders to utilize the MOC facility for orders over which they have discretion.

Therefore we had proposed to remove the board lot volume restriction for MOC and Limit-on-Close ("LOC") order entries. MOC and LOC orders will be accepted into the MOC book with board lot, mixed lot and odd lot volumes and to allow LOC order entry prior to the imbalance dissemination.

Summary and Text of the Final Amendments

TSX received seven comment letters in response to the Request for Comments. A summary of the comments submitted, together with TSX's responses, is attached as **Appendix A**.

TSX respects the public comment process and appreciates the value such public input provides. TSX thanks the commenters for their submissions.

As a result of the comments received from the Request for Comments, TSX is proposing that:

- MOC Limit Orders that do not contribute to the MOC Imbalance at the time of broadcast will be able to be cancelled after the MOC Imbalance is broadcast;

- the definition of "MOC Imbalance" (as defined in the TSX Rule Book) will be replaced in order to reflect the fact that In addition to MOC orders, LOC orders that are priced equal to or more aggressive than the TSX BBO mid-point at the time of the calculation will be considered when determining the MOC imbalance; and

- certain housekeeping amendments to clarify that Rule 4-902(2)(d) is intended to refer to MOC Limit Orders that are not included as part of the MOC Imbalance broadcast.

A blackline to the Amendments showing changes made since the Request for Comments is attached as **Appendix B**.

The Amendments will be finalized in the form attached as Appendix C.

Effective Date

The Amendments will become effective on December 1, 2014.

APPENDIX A

SUMMARY OF COMMENTS AND RESPONSES

List of Commenters:

1. BMO Capital Markets (BMO)
2. Canadian Security Traders Association, Inc. (CSTA)
3. ITG Canada Corp. (ITG)
4. National Bank Financial (NBF)
5. RBC Capital Markets (RBC)
6. TD Asset Management (TDAM)
7. TD Securities, Inc. (TDSI)

Capitalized terms used and not otherwise defined shall have the meaning given in the Request for Comments published in the OSC Bulletin on May 1, 2014.

Summarized Comments Received	***TSX Response***
Comments were received that were supportive of adding the ability to allow mixed/odd-lots to the MOC facility so to bring the TSX MOC facility in-line with international standards. (BMO, ITG, NBF, RBC, TDAM)	TSX acknowledges and appreciates the support from the commenters with respect to the inclusion of mixed/odd lots to the MOC facility.
Comments were received that agreed (in principle) with the proposal to allow LOC orders prior to 3:40 pm but suggested certain variations to how such orders would be implemented or commented that certain functionality issues should be addressed (BMO, CSTA, ITG, NBF, RBC, TDAM).	TSX acknowledges this comment and addresses the particulars of implementation and further functionality below.
Commenters indicated that the National Best Bid/Offer should be used to calculate the mid-point (which is used as a reference to determine whether an order is marketable) rather than the TSX Best Bid/Offer. (BMO, CSTA, ITG, RBC)	TSX acknowledges the comments received. The TSX MOC facility derives the official closing price for all securities admitted to it from the liquidity in the MOC book and the TSX central limit order book. In deriving the closing price for each symbol, transaction volumes and prices from trading activity in the last 20 minutes of the TSX CLOB are used to verify if the calculated closing price is within acceptable parameters to be set or if additional liquidity must be solicited. Only orders within the TSX books are eligible to derive the official closing price. When selecting a reference point from which it would be determined that LOC orders will contribute to the imbalance calculation it was important that the orders and prices that would derive the closing price provide the basis from which LOC orders should be included. If at some point in time additional marketplace liquidity is eligible to set the closing price it may be considered to include this liquidity in arriving at an imbalance reference price.
A number of comments were received addressing the handling of LOC orders that did not contribute to the 3:40 imbalance calculation (non-marketable LOC orders). Some commenters indicated that these orders should remain in the MOC facility as they help reduce volatility, but that participants should have the option to cancel these orders. (BMO, CSTA - some, TDAM) Other commenters felt that these orders should be cancelled by the marketplace. (RBC, TDSI, TDAM, CSTA-some)	TSX recognizes that introduction of pre-imbalance LOC orders reduces the participants' ability to estimate the closing price range. It is our view that this will occur regardless of how the imbalance is calculated at 3:40pm and how the pre-imbalance orders are handled, when compared to the current MOC facility model where the imbalance is based only on market orders. However, we believe (and as confirmed by some commenters) that the proposed model incentivises all players to put their best price forward, and therefore improves price discovery, increases liquidity in the facility and minimizes opportunities to influence the price.

Summarized Comments Received	TSX Response
	In our view, non-marketable LOC orders on the imbalance offsetting side have largely the same impact on the price formation as the offsetting LOC orders entered after 3:40pm and should not in any way increase uncertainty or add to information asymmetry, but may increase available offsetting liquidity at 4:00pm and contribute to price discovery. On the other hand, non-marketable LOC orders on the imbalance side have the potential to dampen the price volatility in case of imbalance flipping. With this in mind, TMX believes that automatically cancelling non-marketable LOC orders only serves to remove liquidity from the MOC book which in turn reduces the facility's' ability to dampen price volatility while weakening the price formation process of the auction. Furthermore, non-contributing orders at 3:40pm may become tradable at 4:00pm and should be executed if offsetting liquidity exists. We therefore believe that non-marketable LOC orders should be allowed to stay in the facility.
	However, TSX accepts that participants may wish to revise their non-marketable LOC orders if the market has moved away from their limit in the last 20 minutes of trading, which is not possible under the original proposal where all pre-imbalance LOC orders are locked. In response, TSX is proposing to revise the proposal and permit LOC orders that did not contribute to the imbalance publication to be cancelled.
Commenters highlighted that LOC orders that remain the in the book without contributing to the imbalance may become marketable between the 3:40 PM imbalance dissemination and the 4:00 PM closing call, resulting in an on-close imbalance that is not disseminated, thus offering no opportunity for participants to provide offsetting liquidity.(CSTA, TDSI)	The MOC model publishes only one imbalance and offsetting liquidity is solicited to address this imbalance at this time. Within the last 20 minutes the market may remain static, move in the direction of the imbalance or in the opposite direction of the imbalance. Unless the facility moves to a continuous imbalance publication (which was discussed with the MOC user community prior to the Request for Comment and did not receive support) as a viable option the imbalance can only reflect the supply/demand dislocation at 3:40pm.
Comments indicated that any participants entering LOC orders which are not part of the imbalance will be aware of the existence of such an order in the book and of the resulting impact on the end-of-day clearing price; such participants would therefore be at an information advantage over the rest of the market. (CSTA, TDSI)	When offsetting LOCs are entered today they remain undisclosed in the MOC book only known to the person that submitted the order. Given the number of competing orders in the MOC facility with varying volumes and price levels and the use of undisplayed liquidity in the CLOB through the use of iceberg orders, we do not believe a participant will have a greater chance of anticipating the end of day closing price under the Amendments than today.
A comment was received which suggested that a material standard of aggressiveness be included in the imbalance indication, because, in the commenter's opinion, a lack of a requirement for material aggressiveness will be dilutive to the risk transfer capacity of the facility. The inclusion of orders that are at or barely through the 3:40 pm reference price will allow new possibilities to game, and introduce new uncertainty to the community of users of the MOC facility and discourage overall participation. The commenter indicated that a minimum standard of aggressiveness relative to the 3:40 pm mid-point reference price should strike a balance between offering reasonable limit control and genuine intent and urgent need to transact at the closing price and	As noted above, accepting LOC orders prior to the imbalance message has the potential to reduce the participants' ability to estimate the 4:00pm closing price range, but at the same time incentivises all players to participate with their best price put forward thereby contributing to price discovery, and reduces the opportunities to influence the price. However, we disagree that orders that are at or barely through the 3:40 pm reference price will allow new possibilities to game the facility or further increase uncertainty.

Summarized Comments Received	*TSX Response*
suggested, as a starting point, the greater of five ticks or 1% from the 3:40 pm reference price. (RBC)	Under the proposed model where the facility will not be automatically cancelling non-marketable LOC orders, only considering aggressive LOCs could lead to an under represented imbalance or even a wrong sided imbalance being broadcast given the liquidity in the MOC book at the time the imbalance was determined. Another consequence of only permitting aggressive priced LOC orders based on set parameters introduces an indicative closing price range based on the liquidity in the TSX CLOB at 3:40pm. During the MOC consultation sessions which preceded the Amendments, comments were received that additional transparency should not be included in the imbalance publication. Artificially constraining LOC orders would provide additional transparency into the imbalance.
A commenter indicated that the proposed deployment timeline (November 2014) is too aggressive because the proposal, in the view of the commenter, puts the onus on participants to ensure that orders that were previously represented in the market and then cancelled by the marketplace are re-entered which may introduce operational issues which did not previously exist. (TDSI)	The Amendments do not include the marketplace cancelling previously booked LOC orders. While we acknowledge the implementation timeline concern, we believe that TSX has provided ample time, in accordance with securities laws and guidance from securities regulator, for participants and vendors to modify their systems for the proposed changes. We also note that participants may continue to use the facility in the current manner until such time when they are ready to fully manage pre-imbalance LOC orders. The Amendments will be provided in an external test environment prior to the production implementation date for the period of time as required under Section 12,.3 of National Instrument 21-101 *Marketplace Operations*.
A number of commenters included proposals for additional improvements of the MOC facility: • Including Dark Orders in the closing auction • Preventing 'flipped imbalances' • Implementing Closing Offset orders • Amending Price Movement Extension functionality • Adjust MOC facility to handle a situation whereby a MOC-eligible stock is halted for a single stock circuit breaker (SSCB) near to the time of the close, if IIROC proceeds with the proposal to amend the SSCB model to 4:00pm • Reviewing eligibility of ETFs and structured products from the MOC facility • Adjusting the pricing structure to apply a fee cap at the parent order rather than the fill level	These proposed changes are outside of the scope of the Amendments, but TSX appreciates the input into how the facility could further be improved. We will take these comments into consideration as we continue to examine our trading facilities, including the MOC facility. We anticipate initiating an industry consultation process on these proposals later this year.

APPENDIX B

TSX Rule BOOK

Rule 1-101 Definitions (Amended)

"MOC Imbalance" means the difference between the aggregate eligible buy MOC Market Order and MOC Limit Order volume and aggregate eligible sell MOC Market Order and MOC Limit Order volume calculated in the manner determined by the Exchange.

[…]

4-902 MARKET-ON-CLOSE

(1) Eligible Securities

MOC Orders may only be entered for MOC Securities.

(2) MOC Order Entry

(a) MOC Market Orders and MOC Limit Orders may be entered, cancelled and modified in the MOC Book on each Trading Day from 7:00 a.m. until the time the MOC Imbalance is broadcast. MOC Market Orders and MOC Limit Orders that are included in the MOC Imbalance broadcast ~~submitted prior to the imbalance broadcast~~ may not be cancelled or modified after the MOC Imbalance is broadcast.

(b) The MOC Imbalance is calculated and broadcast on each Trading Day at twenty minutes before the closing time.

(c) Repealed (April 19, 2010)

(d) Following the broadcast of the MOC Imbalance, until the closing time on each Trading Day, MOC Limit Orders may be entered in the MOC Book on the contra side of the MOC Imbalance. MOC Limit Orders not included as part of the MOC Imbalance broadcast may be cancelled until the closing time.

(e) In the event of a delay of the Closing Call for a MOC Security, MOC Limit Orders may be entered in the MOC Book for such security on the contra side of the MOC Imbalance for a period of ten minutes after the closing time. MOC Limit Orders may not be cancelled during this time period.

Amended (~~November 14~~, December 1, **2014)**

(3) Closing Call

(a) The Closing Call shall occur on each Trading Day at the closing time. The Closing Call in a MOC Security shall be delayed for a period of ten minutes in the event that the price that would be the calculated closing price for the MOC Security exceeds the volatility parameters determined by the Exchange. The Exchange will forthwith broadcast a message identifying the MOC Security that is subject to the delay.

(b) In the event that the price that would be the calculated closing price for a MOC Security exceeds the closing price acceptance parameters determined by the Exchange at the end of the delay period set out in Rule 4-902(~~4~~3)(a), the calculated closing price for the MOC Security will be the price at which most shares will trade, leaving the least imbalance, where the price does not exceed the closing price acceptance parameters determined by the Exchange for such security.

(c) Orders shall execute in the Closing Call in the following sequence:

(i) MOC Market Orders shall trade with offsetting MOC Market Orders entered by the same Participating Organization, according to time priority, provided that neither order is an unattributed order; then

(ii) MOC Market Orders shall trade with offsetting MOC Market Orders, according to time priority; then

(iii) MOC Market Orders shall trade with offsetting limit orders in the Closing Call entered by the same Participating Organization, according to time priority, provided that neither order is an unattributed order; then

(iv) MOC Market Orders shall trade with offsetting limit orders in the Closing Call, according to time priority; then

(v) limit orders in the Closing Call shall trade with offsetting limit orders in the Closing Call entered by the same Participating Organization, according to time priority, provided that neither order is an unattributed order; then

(vi) remaining orders in the Closing Call shall trade according to time priority.

(d) An order for a MOC Security shall not execute if, at the close:

(i) an automatic closing delay has been initiated in the MOC Security because the calculated closing price exceeds the volatility parameters determined by the Exchange; or

(ii) the participation of the MOC Security has been otherwise delayed by a Market Surveillance Official.

(4) Unfilled Orders

(a) Except as otherwise provided in this Rule, all MOC Orders that are not completely filled in the Closing Call shall expire at the end of the Closing Call and will be removed from the Book and the MOC Book.

(b) In the event that the closing price acceptance parameters are exceeded for a MOC security, MOC Market Orders shall trade with offsetting MOC Orders and any limit orders at the price at which most shares will trade, leaving the least imbalance, where the price does not exceed the closing price acceptance parameters determined by the Exchange for such security. All remaining MOC Orders will be removed from the Book and the MOC Book.

(c) All other orders, that are not marked as MOC, that are not completely filled in the Closing Call shall be eligible for trading in the Special Trading Session.

(5) Application of Exchange Requirements

Except as otherwise provided in this Rule, all Exchange Requirements shall apply to the entry and execution of MOC Orders.

APPENDIX C

TSX RULE BOOK

Rule 1-101 Definitions (Amended)

“MOC Imbalance” means the difference between the aggregate eligible buy MOC Market Order and MOC Limit Order volume and aggregate eligible sell MOC Market Order and MOC Limit Order volume calculated in the manner determined by the Exchange.

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(b) The MOC Imbalance is calculated and broadcast on each Trading Day at twenty minutes before the closing time.

(c) Repealed (April 19, 2010)

(d) Following the broadcast of the MOC Imbalance, until the closing time on each Trading Day, MOC Limit Orders may be entered in the MOC Book on the contra side of the MOC Imbalance. MOC Limit Orders not included as part of the MOC Imbalance broadcast may be cancelled until the closing time.

(e) In the event of a delay of the Closing Call for a MOC Security, MOC Limit Orders may be entered in the MOC Book for such security on the contra side of the MOC Imbalance for a period of ten minutes after the closing time. MOC Limit Orders may not be cancelled during this time period.

Amended (December 1, 2014)

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(b) In the event that the price that would be the calculated closing price for a MOC Security exceeds the closing price acceptance parameters determined by the Exchange at the end of the delay period set out in Rule 4-902(3)(a), the calculated closing price for the MOC Security will be the price at which most shares will trade, leaving the least imbalance, where the price does not exceed the closing price acceptance parameters determined by the Exchange for such security.

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