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*via e-mail*

May 21, 2013

**Re: Lynx ATS – Notice of Initial Operations and Request For Comment**

Dear Sirs and Madams:

TD Securities welcomes the opportunity to comment on the Lynx ATS Notice of Initial Operations and Request For Comment.

TD Securities is a leading securities dealer in Canada and the number one ranked block trader in Canadian equities and options based on dollar value and shares traded. TD Securities also acts as the executing dealer for TD Waterhouse which is the largest discount brokerage firm in Canada.

We previously raised a number of market structure concerns in our comment letters on the launch of TMX Select Inc.<sup>1</sup> and CX2 Canada ATS<sup>2</sup>. We have similar concerns with the Omega Lynx ATS proposal.

We are disappointed these recent new marketplaces have brought no new innovation in terms of market efficiency and have primarily been created to add a new make/take fee level for the marketplace operator.

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<sup>1</sup> [http://www.osc.gov.on.ca/documents/en/Marketplaces/com\\_20110304\\_alpha-ats\\_td-securities.pdf](http://www.osc.gov.on.ca/documents/en/Marketplaces/com_20110304_alpha-ats_td-securities.pdf)

<sup>2</sup> [http://www.osc.gov.on.ca/documents/en/Marketplaces/com\\_20121207\\_cx2-pankod.pdf](http://www.osc.gov.on.ca/documents/en/Marketplaces/com_20121207_cx2-pankod.pdf)



We fully support market competition to drive innovation, but we feel the current market structure framework is encouraging the wrong type of competition among marketplace operators and is driving a behaviour which is ultimately harmful to market participants and market quality.

Marketplace operators have an incentive to create as many make/take fee levels as possible to span a range of sub-penny prices and to offer payment-for-orderflow to both active and passive participants. We see the make/take fee model as being inconsistent with Canadian fair market principles since it is equivalent to sub-penny pricing and payment-for-orderflow, both of which are prohibited under Canadian regulations.

The make/take model also creates a lack of transparency since the payments are not included in the displayed price and are not uniformly passed to the end client. In Canada we already have close to a half cent difference between the actual price on CX2 (with a 10 mil active rebate) and the TSX (35 mil active fee) despite both displaying the same nominal price.

The incentive to create multiple make/take price levels has led to an extreme level of market fragmentation, a problem which will only be deepened by the approval of Lynx ATS. Fragmentation is harmful to market quality as it creates an unnecessary level of intermediation based on rebate arbitrage and reduces the likelihood of passive orders to be filled, which ultimately discourages investors from participating in our markets and harms price discovery.

A high level of fragmentation also increases the operational and change management risks for participants, which we consider to be the most significant drivers of risk in electronic trading systems. The recent Electronic Trading Rule addresses risks associated with market access and system testing, but we feel it overlooks the greater risk of operational complexity resulting from a highly fragmented market structure.

Most participants have multiple connection points to marketplaces through a variety of vendors or in-house systems. As new marketplaces are added, connections must be established to each vendor and in-house system, which rapidly multiplies the number of connections that must be supported and makes vendor co-ordination, system testing and change deployment exceptionally complex.

For example, in a Disaster Recovery scenario all marketplace connections to all vendor and in-house routing systems must be simultaneously switched to a backup site with no loss of message sequence or order state for any marketplace. As the number of marketplaces increases this becomes exponentially more difficult to achieve.

Increasing the number of marketplaces also increases the rate of change for gateway upgrades, matching engine enhancements, additional order types, data centre migrations and infrastructure maintenance. Each one of these changes introduces significant risk to the market ecosystem as a whole, as evidenced by the Knight failure. We strongly feel this operational risk should be taken into account by regulators when approving new marketplaces with an appropriate balance struck between supporting competition and reducing market fragmentation and operational risk.

We recommend regulators place a moratorium on all new marketplaces until the fundamental market structure issues can be addressed. As Warren Buffet and Will Rogers insightfully advised, “The most important thing to do if you find yourself in a hole is to stop digging.”



We appreciate the opportunity to comment on the Lynx ATS Notice of Initial Operations and we would welcome a meeting with OSC Staff to further discuss our views.

Respectfully,



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