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Dear Sirs/Mesdames:

Proposed Rule Amendments to the TSX Alpha Exchange ("Alpha") Trading Policies ("Proposed Alpha Amendments")

As Aequitas NEO Exchange is a recently-approved exchange, whose application initiated the discussion around and approval of the concept of a speed bump in Canada, we feel we are in a unique position to comment.

We thank OSC staff for allowing us an extension to provide our letter; the standard 30 day period was difficult to meet in this case. The proposed changes have, as we will discuss below, far-reaching consequences and we fear that many stakeholders in the industry will not be commenting due to a lack of time and, possibly, the absence of any questions being raised in the accompanying notice.

Set out below are observations on the process, followed by some clarifications and, finally, our specific comments on the Proposed Alpha Amendments. We are also including questions regarding technical aspects of the Proposed Alpha Amendments in the hope of eliciting additional clarity.

Process

Issues around equitable treatment, fair access, what constitutes "segmentation" and the application of the Order Protection Rule ("OPR") were raised in the context of the Aequitas application for recognition over the summer. Specific comment was requested in respect of a number of these issues.

Despite significant differences in the application of the concepts, no issues have been raised and no questions asked in the OSC notice with respect to the Proposed Alpha Amendments. In particular, the fact that no question was asked about the impact of applying OPR to a marketplace where all orders, except one single type of passive order, are subject to a delay appears inconsistent.

The elements of the Proposed Alpha Amendments were labelled in such a way as to infer that Alpha is offering similar solutions to those the Aequitas NEO Exchange recently brought into the markets but, regardless of the similar terminology, they are of very different impact.

We strongly urge regulators to ensure that, in their treatment of marketplace proposals, they are demonstrably going beyond a general review of the mechanisms used and high level impact. Regardless of similar terminology and concepts, it is critical that they are, and are seen to be, carefully considering the ultimate impact of a marketplace proposal, whether novel or a variation of an existing product or service.

Clarification re: inaccurate information

To ensure the review of the Proposed Alpha Amendments is based on accurate information, we would like to take this opportunity to correct an erroneous statement in circulation that suggests that both Alpha and the Aequitas NEO exchange will slow down the orders emanating from smart order routers. This is not correct with respect to the Aequitas NEO Exchange, as the delay on our market, resulting from a speed bump, only applies to "Latency Sensitive Traders" trying to take liquidity. In other words institutional and retail flow, passing through a smart order router, is not subject to any delay. The opposite is true for Alpha where ALL smart order routers managing institutional and retail flow will be impacted by a delay and only HFT firms using Post Only orders will not be impacted.

Specific Comments

Purpose of Alpha's proposal to slow down all active order operations

Much discussion and debate followed the publication of the Aequitas NEO Exchange proposal to apply a speed bump to "Latency Sensitive Traders". After an extended comment period and a number of submissions, the OSC accepted the view that not all differential treatment leads to "fair access" issues. We had argued that slowing down the fastest participants was not unfair, as we were simply taking the speed advantage away with the intention of giving everyone a much more equitable chance to execute against orders in the book.

The speed bump in the NEO Book™ was developed to provide a more level playing field, speed-wise, for active orders not originating from accounts using latency sensitive strategies, which include most orders entered on behalf of retail and institutional clients. It was also aimed at providing some level of protection from predatory high frequency trading (HFT) strategies for orders posted in the book – whether those passive orders were placed by HFT or non-HFT market participants on a proprietary or agency basis. Such protection should provide some comfort for liquidity providers to post greater size, which in our model would benefit all liquidity seeking investors and, in particular, retail and institutional investors.

The delay described in the Proposed Alpha Amendments serves an entirely different purpose: to protect orders sent as Post Only or, in other words, to re-create the economics of dark trading without minimum price improvement so as to provide an alternative to sending orders to U.S. markets where such trading is currently allowed. A Post Only order is an order type that was created for HFT firms, and is only used by HFT firms, allowing them to enter numerous identical orders with an objective of maximizing the probability of resting one of them at the top of the book without the risk of being traded upon entry.

Furthermore, not only would the Proposed Alpha Amendments slow down all orders from natural investors, it would also slow down all order operations (inserts, CFOs, cancels) for everything except Post Only orders. This in combination with OPR would mean that the speed advantage for passive HFTs would be further magnified, placing the already speed-disadvantaged natural orders in an even worse position than in current markets.

<u>Effect of Alpha's proposed delay on natural investors' orders and dealers</u>

If, as is often the case, an order is broken up and one part must go to Alpha because of the Order Protection Rule, a delay would allow HFT firms to take in and take advantage of the information from the other marketplaces and adjust their orders before the delayed order trades in Alpha. This has the following consequences:

- *Client interests being at odds with those of their dealers*. Best execution would dictate that parts of orders should not be sent to a venue that facilitates information leakage and resulting technological front-running of these orders. However, the inverted fee structure provides a benefit to dealers who may or may not pass it on to their clients.
- *"Natural" investors whose orders get frequently broken up due to their size being incentivized to avoid the Canadian markets*. Such investors – typically institutional investors and wealth management clients – will seek, if they have the ability to, to avoid the Canadian markets where they are exposed to the risk of having to trade on a venue that facilitates information leakage.
- *The entire dealer community having to invest in new technology.* Dealers will need to invest in new smart order routing technology, compliance monitoring, etc., to adapt to the new Alpha model. This seems to have been completely disregarded in the analysis we have seen. The economic impact should not be underestimated.

Effect on Canadian equity markets of separating retail and institutional flow

Research has shown that markets operate more efficiently if the order flow of natural investors is able to interact as much as possible without intermediation. Many marketplaces offer different value propositions for different types of trading. However, a mechanism that sets up a perfect ecosystem for HFT firms to trade against retail orders while incentivizing institutions to protect themselves by going elsewhere, including the U.S. markets, raises significant concerns that appear to have been dismissed on the basis that at 30 thousand feet, the Alpha proposal seems to be a duplication of already-approved functionality.

Even from the perspective of stated intentions, questions arise about what the Proposed Alpha Amendments mean to the market as a whole:

- The Aequitas NEO Exchange provided extensive information to regulators and the industry about how the exchange's functionality is aimed at providing tools and opportunities for both retail and institutional investors – and aligning their interests with those of their dealers in an environment often driven by trading fee economics.
- The Alpha proposal is primarily focused on solving the problem of southbound trading volumes, solely by appealing to dealers trading retail orders. There has been no analysis provided on the impact on the market as a whole if the Proposed Alpha Amendments are approved and, in particular, how domestic and international institutional investors will adjust their order flows.

Questions

1. It is difficult to form a view on the extent of the impact (including the value of the Proposed Alpha Amendments) without knowing what is being considered for the minimum volume requirement for the liquidity providers. Does Alpha have a range under consideration that would assist in this analysis?
2. The Proposed Alpha Amendments state that Alpha will set the minimum volume requirement in its discretion; will there be a minimum notice period for setting and changing the minimum volume? Has there been consideration of where the balance is between the minimum volume required to post and the benefit of being protected by the delay imposed on active orders?
3. It is also difficult to assess the impact of the proposal without more clarity about the delay parameters. Some ranges were provided but it appears that they have not been finalized. As this is a key issue for institutional investors, will it be available for consideration prior to the decision about approval?
4. The Proposed Alpha Amendments appear to be based on the assumption that the only factor driving the southbound trend is regulatory arbitrage (including the pricing rules or payment for order flow); has there been analysis of the role that the comparative volumes and relative parity in foreign exchange rates between the Canadian and U.S. markets have played?

5. Concerns remain about the impact of high frequency trading in the markets – is it clear in the documentation that the passive counterparties will all or virtually all be HFT firms?
6. Has there been any assessment performed about how domestic and international institutional investors will adjust their flows based on the Proposed Alpha Amendments? Is there a risk that Canadian markets will on a net basis lose more volume than they would gain volume back?
7. Has there been any assessment of the economic impact on dealers having to fundamentally review and change their order routing and related technologies? How does this cost increase compare to any savings that may result from the Proposed Alpha Amendments?

One of the concerns voiced in response to the Aequitas NEO Exchange application was a "floodgates" argument – i.e., that even if the particulars of our model did not raise issues, it could lead to other, more troubling differential treatment. This is the case with the Proposed Alpha Amendments and we urge the regulators to carefully consider the differences and assess the consequences before approving it.

We appreciate the opportunity to provide our comments.

Yours truly

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