The Bank of Nova Scotia
Global Equity
Scotia Plaza
40 King Street West, 68th Floor
Toronto, ON M5H 1H1

November 16, 2020

Market Regulations Branch
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
marketregulation@osc.gov.on.ca

and

Denno Chen
Director, Regulatory Affairs
TMX Group
100 Adelaide Street West, Suite 300
Toronto, Ontario M5H 1S2
tsxrequestforcomments@tsx.com

Via Email

Re: Notice of Proposed Amendments and Request for Comments – MOC Modernization

Scotiabank appreciates the opportunity to comment on the proposal by TMX Group to substantially revamp the Market-on-Close facility of the TSX. We believe this is a very impactful initiative with significant implications on the health of Canada's equity markets.

General Comments

The closing auction run by the TSX is the most important price discovery event of the trading day. It is used to establish daily closing levels widely used by the investing community, factoring directly into investor confidence in the equity markets. The close is also a very significant liquidity event, with the mechanism's design playing a key role in the orderly matching of closing orders.

The TMX Group's efforts to update and modernize the existing MOC facility are to be commended. The consultation process on this topic was extensive, involving many key stakeholders representing diverse constituencies. The proposed amendments to the MOC incorporate significant industry feedback, resulting in a model which we believe will accommodate the unique needs of the Canadian market. Our detailed feedback on this model has already been

The Bank of Nova Scotia
Global Equity
Scotia Plaza
40 King Street West, 68th Floor
Toronto, ON M5H 1H1

presented to the TMX Group as part of earlier industry consultation and has been substantially incorporated into the proposal. We support the model as presented.

Implementation Timeline

We believe that TMX Group's proposed implementation timeline, of Q2 2021, is aggressive. We do not doubt that TMX Group is able to meet this timeline for its own systems deployment. However, we are concerned that the ultimate smooth roll-out of the MOC facility is contingent on a wide range of stakeholders being able to support these changes at each step of the chain. If a material part of the broader industry is unable to support the MOC revisions, participation in the MOC will drop. The result will be investor harm through worse price discovery and greater closing auction volatility.

Based on our assessment of readiness to date, we do not yet have confidence that a large enough part of the industry will be able to adapt to the proposed MOC changes on the schedule proposed. It is our understanding that vendors and service providers are at early stages of their planning for the coming changes, despite the magnitude of the work involved. We are therefore concerned that the Street will not be ready in time for Q2 2021 deployment.

We would encourage all industry stakeholders to mobilize towards the proposed timelines. We concurrently encourage TMX Group to pay close attention to the preparedness of data vendors, trading software providers and the dealer community to assess the feasibility of the Q2 2021 launch timeline. We firmly believe that the deployment of the modernized MOC, as a "big bang" event, must take place at a time when industry is substantially prepared.

Limit-on-Close Orders and Allocation Priority

The proposal as presented does not contemplate any change to the allocation priority of orders entered in the MOC facility. However, this consistency has certain side-effects which merit further consideration and should be revised prior to implementation. I our concern is specific to the handling of limit-on-close (LOC) orders entered on either side of the start of the freeze period.

Specifically:

- LOC orders prior to freeze will be tradable to their limits and may impact the closing price in the auction by triggering a "gap" towards their limit.

The Bank of Nova Scotia
Global Equity
Scotia Plaza
40 King Street West, 68th Floor
Toronto, ON M5H 1H1

- LOC orders entered after the freeze period will be constrained in price to the midpoint of the NBBO at close – resulting in an inability to trigger a price move towards their ultimate limit.

This difference in the treatment for orders all called "Limit-on-Close" will be confusing. We therefore respectfully suggest that the "closing offset" order name be retained to refer to LOC orders entered after the start of the freeze period. The implementation of the closing offset order should be identical to that proposed today: LOC orders entered after freeze are simply named differently.

More importantly, post-freeze LOC orders are designed to prevent a "flip" of a published imbalance even though these post-freeze LOC orders are ultimately tradable. The existing price-centric allocation priority will allow LOCs with very aggressive prices to have priority over orders which are less-aggressively priced but which are equally unable to impact the close and contribute to price discovery. We view this as unhelpful, and would prefer that the allocation model be revised to reduce the potential for "scooping" among LOC orders.

Our suggestion is therefore that:

- LOC orders entered in the freeze period be renamed "closing offset"
- These "closing offset" orders be ranked lower in priority than any LOCs entered prior to the start of the freeze period.
- Fill priority among "closing offset" orders be determined in a fashion which rewards their entry by the maximum number of participants. Specifically, we would suggest that a round-robin-style allocation (where a partial fill is offered to many individual offsetting orders) may be a more equitable approach to encouraging offsetting liquidity from a diverse range of participants near the close.

We note that the above changes do not represent a significant departure from the main thrust of the MOC Modernization initiative. We do not believe incorporating such changes should delay the implementation of the MOC Modernization, and do not believe that this suggestion reaches the threshold of materiality necessitating a further comment period.

Inclusion of ETFs in the Closing Auction

The eligibility of exchange traded funds in the closing auction has been discussed in industry in conjunction with the broader MOC Modernization intiative. While it is not specifically mentioned

The Bank of Nova Scotia
Global Equity
Scotia Plaza
40 King Street West, 68th Floor
Toronto, ON M5H 1H1

Scotiabank
GLOBAL BANKING AND MARKETS

or proposed, eligibility of securities for the MOC remains within the jurisdiction of the TMX Group and would not require public comment.

We recognize that certain constituencies would find it convenient and useful to have the MOC mechanism be extended to exchange traded funds. However, the needs of those constituencies must be balanced against the potential for market harm, including loss of investor confidence, if the MOC facility was to result in a closing price for an exchange traded fund that is substantially away from the intrinsic value of the fund's holdings at that time. This is not a purely theoretical concern; TMX Group's past foray into ETF eligibility to the MOC facility resulted in numerous cases where funds' closing deviated significantly from their theoretical values, resulting in the ultimate removal of ETFs from MOC eligibility.

We believe that the proposed model is more suited to ETF usage than the existing MOC. However, we do not believe that the issues which led to adverse closing prices in the existing MOC go away simply by transitioning to a continuous imbalance publication or any of the other features presented as part of MOC Modernization. The suitability of the MOC for clearing ETF flows depends largely on the ability of a wide range of participants to supply liquidity to closing order flow imbalances, with the mechanism itself being a contributing factor to that dynamic. We respectfully suggest that the MOC Modernization rollout is sufficiently complex without the added risks of introducing ETFs into the mechanism.

We believe that ETFs should not be considered for inclusion in the MOC facility until such a time that the Street and TMX Group can be confident that ETF market making into the MOC facility would be robust. Given the magnitude of changes proposed, we recommend that TMX Group limit the scope of changes – including eligible securities – to the greatest extent feasible, and not consider the inclusion of ETFs until at least six months of successful operation for the new MOC. We would also suggest that before any ETF inclusion is considered, TMX Group evaluate whether ETF-specific enhancements to the MOC would be appropriate or beneficial.

We appreciate the opportunity to comment on this matter.

Respectfully,

Alex Perel, CFA
Head of ETF Services
Scotiabank Global Banking and Markets
(416) 862-3158

The Bank of Nova Scotia
Global Equity
Scotia Plaza
40 King Street West, 68th Floor
Toronto, ON M5H 1H1

Scotiabank
GLOBAL BANKING AND MARKETS

alex.perel@scotiabank.com