



**CANADIAN SECURITY TRADERS ASSOCIATION, INC.**  
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**Re: Process for the Review and Approval of Rules and the Information Contained in Form 21-101F1 and the Exhibits Thereto.**

The Canadian Security Traders Association, Inc. (CSTA), is a professional trade organization that works to improve the ethics, business standards and working environment for members who are engaged in the buying, selling and trading of securities (mainly equities). The CSTA represents over 850 members nationwide and is led by Governors from each of three distinct regions (Toronto, Montreal and Vancouver). The organization was founded in 2000 to serve as a national voice for our affiliate organizations. The CSTA is also affiliated with the Security Traders Association (STA) in the United States of America, which has approximately 4,200 members globally, making it the largest organization of its kind in the world.

This letter was prepared by the CSTA Trading Issues Committee (the "Committee"), a group of 20 appointed members from amongst the CSTA. This committee has an approximately equal proportional number of buy-side and sell-side representatives with various areas of market structure expertise. It is important to note that there was no survey sent to our members to determine popular opinion; the Committee was assigned the responsibility of presenting the opinion of the CSTA as a whole. The opinions and statements provided below do not reflect the opinions of *all* CSTA members nor the opinion of *all* members of the Trading Issues Committee.

The CSTA appreciates the opportunity to comment on the proposed change to the order matching priority of stocks priced  $\leq$  \$0.99 proposed by NASDAQ for its CX2 Trading Book (CX2).

As the proposal highlights, the CX2 market is attempting to encourage participants to post large orders (defined as 30,000 shares) in low price stocks by rewarding them with queue priority. With the proposed size-priority logic, participants that provide liquidity will be incented to post as large an order size as possible at the touch and to replenish (upsized) the order frequently to maintain queue priority. The CSTA TIC generally supports initiatives that encourage available, visible liquidity in lit venues, with an increase in size at the NBBO being considered a net positive to the Canadian public equity market ecosystem.

While more visible and available passive liquidity in the lit markets is generally positive, it is also important to consider the potential impact on price discovery and market quality as it refers here to bid-ask spreads. One of the benefits of a more traditional time priority approach in an order book is a reduced incentive for traders to hold back their orders from the market since they receive queue priority by being first at a price level. By allowing traders to compete for queue priority based on size, small orders that set a new price and tighten the bid-ask spread would lose their order priority if they are joined by larger orders at the newly established price levels. Size priority in order books can disincentivize the price setting behavior that we associate with better price discovery and potentially widen bid-ask spreads and affect market quality. In addition, size priority also allows larger traders to wait at wider spreads knowing that they can take queue priority when required, further impacting price discovery and bid-ask spreads.

The CSTA TIC generally thinks the CX2 proposal at hand is reasonably balanced. We believe that CX2 would succeed in improving liquidity available for low-priced stocks on CX2, with the benefits of the size priority outweighing the possibility of discouraging price discovery or widening spreads. For those smaller orders which are setting new price levels, there are many alternative venues that provide time priority and thus we do not believe that the overall market ecosystem would be affected. Additionally, in the context of low-priced stocks on an inverted venue, we do not see any unreasonable degree of discrimination, unfairness or preferencing of one participant over another while seeking to improve liquidity overall. We applaud the innovative priority mechanism proposed by Nasdaq.

Of concern to some of the CSTA TIC members are the potential unintended consequences that may result from setting a precedent of allowing lit, protected, order books to set queue priority based on size. At this time, there are other venues with aspects of size priority in their matching, but they have been limited to Dark or Hybrid venues. We acknowledge that the OSC will continue to evaluate the merits of proposals as they are presented. However, reversing past decisions based on unexpected or unintended consequences in the future is not as straightforward since it could materially impact business models that are based on previous approvals.

While contemplating approval of this proposal, we would suggest that the OSC consider the following questions that would refer to some of the broader implications the setting of a precedent:

- Why is this proposal being restricted to stocks below \$1? What are the issues of offering the same mechanism to stocks above \$1?
- If other marketplaces were concurrently proposing this methodology, would it be appropriate as a market-wide allocation scheme?
- Will market quality be harmed if smaller liquidity providers and market makers give up on providing liquidity and allow larger participants to prevail?

- A size priority mechanism may work in Dark/Hybrid markets, but is it appropriate for lit markets?
- Does an order book that uses size priority inordinately penalize small orders (including retail and institutional orders) and therefore cause harm to investors?
- Are there market integrity issues to consider with increasing the complexity of the Canadian public equity markets?

The CSTA TIC was unable to reach consensus on these questions; they are not simple! But we hope that providing these questions may assist in the decision-making process.

Notwithstanding the concerns we have expressed, we reiterate that it is likely that the available visible liquidity available on CX2 would increase under a size priority regime as proposed. This could present a benefit for both small sized and large sized orders that would cross the spread as routing could be simplified, certainty of execution improved, and potential price impact reduced.

We appreciate the opportunity to comment on this matter.

Respectfully,

*“Signed by the CSTA Trading Issues Committee”*