RBC Global
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Via Email

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

Dear Sir or Madam:

Re: OSC Request for Comment – Proposed Structure of Trading Facilities for a New Exchange Proposed to be Established by Aequitas Innovations Inc.

We are writing on behalf of RBC Global Asset Management Inc. ("RBC GAM") in response to the request for comment issued by the Ontario Securities Commission ("OSC") concerning the proposed structure of trading facilities for a new exchange proposed to be established by Aequitas Innovations Inc. ("Aequitas") published on August 13, 2013 ("Notice"). RBC GAM is an indirect wholly-owned subsidiary of Royal Bank of Canada ("RBC"). While RBC holds an indirect economic interest in Aequitas, RBC GAM has developed the viewpoints expressed in this letter separately, which are a reflection of RBC GAM's perspective as an institutional shareholder.

We applaud the OSC's efforts to bring transparency to important market structure issues and appreciate the opportunity to provide our comments. As we are in favor of developments that bring innovation and benefits to the Canadian marketplace, especially for long-term investors such as RBC GAM, we welcome Aequitas' proposal as outlined in the Notice. The objectives of protecting long-term and retail investors, while considering innovations to reduce the detrimental impacts of high frequency trading ("HFT") and gaming, should be of the utmost importance to regulators, and the OSC should be commended for considering Aequitas' proposal.

We note, however, that for long-term investors it is equally important that the listing requirements of a new exchange protect shareholders' interests and meet corporate governance best practices. Thus we look forward to an opportunity to review and comment on Aequitas' proposed listing requirements prior to it being recognized as an exchange.

Outlined below are our comments on the specific questions raised in the Notice:

Question 1: Should OPR apply to all visible markets and to all orders displayed on those markets, or are there circumstances where the application of OPR should be limited?

The principles used as the basis for the OPR rule should not change. The main benefit of OPR was to enable the aggregation of liquidity across marketplaces. In practice, the OPR rule resulted in some unintended consequences, such as protecting small and inefficient marketplaces which do not add to overall market liquidity. It also resulted in increased costs for the sell side due to the cost of connectivity and market data. Indirectly, this affects the buy side as the costs are passed through to us. Therefore, regulators should be open to new ideas and allow for exceptions to the OPR in all visible markets as appropriate.

The structural issues that the Aequitas model seeks to address allow us to take a closer look at the role of the OPR in our marketplace. In our view, it seeks to resolve some of the unintended consequences that the OPR has played a role in generating, particularly technology-based intermediation through latency arbitrage-type strategies. Institutional buy side participants welcome efforts to address predatory trading practices. In this regard, we support Aequitas' position that Hybrid should not be subject to the OPR, or should otherwise be exempt from the OPR.

Question 2: Should OPR apply to Hybrid? Should it continue to apply at least with respect to active non-SME orders that are not restricted from accessing the best-priced displayed orders on Hybrid?

As indicated above, we support Aequitas' position that Hybrid should not be subject to the OPR, or should otherwise be exempt from the OPR, as it seeks to offer non-SME investors the potential for a better quality of fill. This exemption will allow non-SME participants to organically determine if the Aequitas Hybrid better serves the interests of natural investors. Given that executions on Hybrid would only occur at or within the NBBO, such that Hybrid trades cannot occur at an inferior price than protected marketplaces, orders executed on Hybrid cannot be traded through.

Question 3: If Hybrid is implemented as proposed, how should the best-priced displayed orders on Hybrid be treated for the purposes of consolidated display requirements, and why?

As an unprotected marketplace, the best-priced displayed orders from Aequitas' Hybrid book should not be included in the NBBO consolidated quote. As long as the Aequitas marketplace provides additional liquidity and improved price discovery to the Canadian market, we see this as an appropriate trade-off. Any meaningful demand-enhanced quote feeds by market participants could be independently built by data vendors such as Reuters if there is sufficient consumer demand.

Question 4: What should the appropriate reference price be for determining whether a dark order on any other market has provided minimum price improvement as required under the Dark Rules – the Away NBBO or the NBBO that includes a Hybrid best bid and/or Hybrid best offer? Does the answer to this question depend on whether or not OPR applies to Hybrid?

As indicated above, we support Aequitas' position that Hybrid should not be subject to the OPR, or should otherwise be exempt from the OPR. Therefore, the NBBO should not include the Hybrid best bid and/or Hybrid best offer, and should continue to be used as a reference price for this marketplace, as is the case with any dark pools.

Question 5: How should fair access requirements be applied with respect to access to visible marketplaces?

We fully support the fair access principle. However, we believe fair access in our marketplace is currently being compromised through the predatory use of technology and various structures of maker/taker schedules. Fair access requirements should be applied to the speed and type of access to liquidity. Where a predatory HFT strategy derives a speed advantage for the purpose of latency or rebate arbitrage, fair access to natural liquidity would be disrupted from the traditional long-term buy-side investor. In this regard, we conceptually welcome the use of the SME marker as a mechanism to level the playing field of fair access to liquidity.

One possible solution to preserving fair market access would be the application of a time enforcement mechanism or latency embargo which would discourage any HFT strategy looking to intermediate.

Question 6: Should visible markets be fully accessible or, like dark pools, should access restrictions be permitted? Why? What are the criteria that should be used to determine if the differences in access are reasonable? What impact, if any, could restricting access to the best displayed price have on confidence and market integrity?

If restricting access to certain market participants results in benefits to long-term investors and allows natural trade flow to interact with each other, that would be viewed as a positive change by the buy side. Today, the way marketplaces operate leads to increased data costs for dealers, and indirectly for retail and institutional money managers. Market makers on most markets have no obligation to provide this function. There is a lack of true competition between marketplaces. We are concerned about the overall reduction in market liquidity and welcome an innovation that could change these deficiencies.

Question 7: Are the access restrictions proposed for Hybrid consistent with the application of the fair access requirements?

Based on the information presented in the Notice, we believe that the proposed access restrictions for Hybrid are consistent with the application of the fair access requirements, provided long-term investors and natural order flow are allowed in the marketplace.

Question 8: Is the SME marker an appropriate proxy to identify the behaviours Aequitas seeks to restrict?

Yes. At this time, the SME marker is the most appropriate tool available to identify the behaviors that Aequitas seeks to restrict. However, regulators need to urgently address the participant use and compliance of SME markers. As SME markers are viewed and applied differently by different parties, regulators must provide clear guidance on the use of the SME marker. For this proxy to prove useful and successful, regulators should ensure that there is minimal room for interpretation.

That said, we are concerned that the SME marker alone may not be sufficient as HFT firms could potentially change their strategies in order to be barely non-SME compliant.

Question 9: What, if any, is the impact on market quality and market integrity if market makers are provided matching priority (after broker preferencing)?

With proper surveillance, the market maker role is essential to our markets and should be welcomed by all participants. A qualified market maker who has defined, controlled and monitored responsibilities is obligated to provide liquidity, balanced by the privilege of priority to protect the integrity of our markets. Providing market makers with matching priority appears to be an incentive for them to stay and provide liquidity at all times, not only when they see fit. However, such privilege should come with a clearly defined obligation and expectation to provide liquidity. By providing regular surveillance, oversight and measurement of the market makers' activities, marketplaces can ensure that market makers comply with their obligations or be excluded from the marketplace. Establishing a strong market maker program will improve price discovery and efficiency.

Question 10: In light of the details of Aequitas' proposed market maker program, is it reasonable to provide the benefit of priority to a market maker in the Dark and Hybrid books when the market maker's corresponding obligation is limited to the Lit book? If not, should there be market making obligations in Aequitas' Dark or Hybrid books?

If market makers receive priority in all Aequitas markets, then firm obligations should be applied to all markets as well. Please refer to our response to Question 9 for more details on how to keep track of market makers' adherence to this obligation.

Question 11: Should market making benefits accrue with respect to obligations for market making in non-Aequitas listed securities? If so, why and if not, why not?

Yes. Market making benefits should accrue across all listed securities in order to offer continuous incentive to market makers to provide liquidity to the marketplace.

Question 12: Should DEA clients that are not subject to the direct regulatory authority of the securities regulatory authorities, IIROC and/or the exchange be permitted to act as market makers? Why or why not? How would the following facts affect your response: (i) the DEA client market maker must be sponsored by an IIROC member and (ii) the DEA client market maker must be a member of a self regulatory organization such as FINRA or otherwise subject to appropriate regulatory oversight?

We are of the view that DEA client market makers must be members of a self regulatory organization such as FINRA, or otherwise subject to appropriate regulatory oversight and sponsored by an IIROC member. That said, if Aequitas can demonstrate to the regulators that it has sufficient and robust controls in place to monitor DEA clients, a sponsorship by an IIROC member may be sufficient.

Question 13: Will an un-level playing field be created between DEA client market makers and registered investment dealers that also seek to become market makers on Aequitas' proposed exchange? If so, what are the potential implications in terms of fairness or market integrity?

Competition for market maker positions may be a positive development as it will foster fairness in the marketplace. As long as both types of market makers are subject to the same standards and controls, we believe that fairness and market integrity will not be compromised.

Question 14: How might Hybrid impact the quality and integrity of the visible market as a whole?

Hybrid, as proposed by Aequitas, could potentially improve the liquidity of the exchange-traded stocks and bring benefits to long-term investors. If that proves to be the case, we believe that market quality and integrity will be maintained. The quality and integrity of markets would be enhanced by a Hybrid market that provides an opportunity for investors to meet and trade at a price of their choice, free from intermediation. Canadian markets would be more competitive.

Question 15: Please comment on whether the potential benefits of Hybrid for the marketplace participants in Hybrid outweigh any potential risks to the market as a whole? Please identify the relevant benefits and risks.

Any innovation in the marketplace has potential benefits, but could also have a negative impact on overall market structure and integrity. Thus we need to weigh both sides and favour those proposals whose benefits outweigh any possible unintended consequences.

In our view, the possible risks of Hybrid are as follows: i) predatory-type HFT participants who manipulate their strategies to circumvent the SME marker, thereby muddying the transparency of participant behavior; ii) regulators allowing an exemption to the OPR may set a precedent that opens the flood gates to a further fragmented and complex marketplace; and iii) the segregation of flow based on participant type may create other unexpected consequences, leading to further fragmentation and various complexities (technology and regulatory).

Additional market fragmentation may be an acceptable consequence if the detrimental impacts of HFT would be greatly reduced or eliminated altogether by the proposed exchange. If successful, Aequitas has the potential to change the way that global exchange models operate.

We believe that the success of the Aequitas' business model depends on market forces. Should market participants recognize the potential benefits, the marketplace will thrive and, in turn, may outweigh the potential risks to market participants who are associated with trying and evaluating the new marketplace.

Question 16: How should the principles of the current regulatory framework and any potential for changes to that framework impact the OSC's consideration of Hybrid? For example, should Hybrid go forward on a pilot basis and be reevaluated based upon some criteria or threshold? What type of criteria or threshold might be appropriate to minimize potential negative impact?

The proposal submitted by Aequitas is sufficiently different from other existing models, not only in Canada but globally, and hence should be given an opportunity to prove itself. We have seen a lot of marketplaces come to Canada recently which, in our view, didn't bring meaningful innovation. There are too many marketplaces that base their business models on charging maker/taker fees, attracting numerous intermediaries and not bringing any meaningful benefit to the buy side and overall market liquidity. We welcome a new model which may provide a solution to some existing market inefficiencies. Unless we are given an opportunity to test the proposed model, it will be hard to evaluate its final impact on the marketplace. Regulators should consider creating criteria and thresholds (e.g. market share, average trade size, or reliability of spreads) to evaluate efficacy of both the newly proposed and existing marketplaces.

Question 17: Alternatively, should Hybrid be required to be modified to fit clearly within the established regulatory framework for either visible or dark liquidity? If so, how?

No. The groundbreaking market creation model that is being presented by Aequitas in their Hybrid market needs to be given a chance to function and demonstrate if long-term benefits exist for Canadian investors. Investors should be given the opportunity to decide whether a marketplace free of intermediation will be functional and evaluate the price protection within the Hybrid market. The OSC should be encouraging this type of innovation as it gives investors the opportunity to trade without intermediation.

We thank the OSC for considering our comments on the Notice. Should you have any questions or require further information, please do not hesitate to contact the undersigned.

Sincerely,

"Daniel E. Chornous"

Daniel E. Chornous, CFA
Chief Investment Officer
RBC Global Asset Management Inc.