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Dear Sirs/Mesdames:

Re: OSC Staff Notice and Request for Comment regarding Proposed Structure of Trading Facilities for a New Exchange Proposed to be Established by Aequitas Innovations Inc. (the "Notice and Request for Comment")

TMX Group Limited ("**TMX Group**") welcomes the opportunity to comment on the Notice and Request for Comment as published by the Ontario Securities Commission (the "**OSC**") on August 13, 2013.

TMX Group has a long history of serving Canada's public markets. We constantly strive to identify opportunities to address industry and market structure issues and to develop innovative solutions to meet our customers' diverse and emerging needs.

At the same time, we believe in the benefits of our customers having choice, so we continue to encourage competition and innovation among Canadian marketplaces, as long as fundamental principles underlying the effective functioning of our market are not compromised.

We understand that Aequitas is proposing to establish an exchange with a marketplace model which in many aspects is inconsistent with the current Canadian regulatory framework and conflicts with many fundamental principles under which our market operates. TMX Group believes that careful consideration must be given to a number of areas in the Aequitas Proposal. Many of the recommendations contained in the proposal raise concerns about impact on market quality, fairness, costs being imposed on industry participants, and the role of HFTs, both across the market in general and on Aequitas.

This letter summarizes TMX Group's views on a number of the issues raised by the OSC in the Notice and Request for Comment. Our submission is based on, and restricted to, the limited information and issues raised in the Notice and Request for Comment. As further details become available regarding Aequitas, we expect to have the opportunity to comment further in subsequent regulatory consultations as well as to emphasize the importance of having a level-playing field among marketplaces.

More detailed responses to the specific questions asked in the Notice and Request for Comment are in Appendix A. All capitalized terms have the same meanings as defined in the Notice and Request for Comment, unless otherwise defined in this letter.

Protecting Canada's Capital Markets

Certain aspects of the Aequitas Proposal are inconsistent with existing rules which were developed to protect all participants and preserve fundamental values of our market. We have closely considered whether it is possible to align the proposal with the objectives and principles on which the marketplace rules were developed (such as price discovery, fairness, transparency, and market integrity) and whether the anticipated benefits warrant the rule changes, industry integration costs, increased complexity and risks the proposed model would impose on the industry.

The Aequitas Proposal includes three order books: Dark, Lit and a Hybrid book. TMX Group is of the view that this proposal, and in particular the proposal for the Hybrid book, compromises the price discovery process and market integrity, two of the key characteristics of an efficient and effective market. We also believe that the cost to the industry to adopt this unique model far outweighs the anticipated benefits.

Hybrid Book, Market Integrity and Price Discovery

The proposal is unclear regarding whether the Hybrid book will be subject to the Order Protection Rule (OPR) and therefore be a protected market. To fully assess and understand the impact of the proposed Hybrid book on market integrity and price discovery, we have considered both scenarios of whether the Hybrid book is a protected or unprotected market.

Hybrid as Unprotected Market

If Hybrid is not a protected market, then Hybrid quotes do not contribute to the Consolidated Market Display (as defined by UMIR), and will not effectively contribute to price discovery.

This qualifies Hybrid as a dark pool, and therefore Hybrid should abide by the Dark Rules, including minimum price improvement requirements, size restrictions and giving priority to lit liquidity on the Aequitas market's books.

If however Hybrid is allowed to operate without Dark Rule restrictions, placing orders on Hybrid and away from visible marketplaces could have a negative impact on the price discovery process and on the liquidity available to those participants that are required to, or have elected to, display their orders on a visible market. This result would be fundamentally inconsistent with CSA and IIROC principles underlying the Dark trading regime, thereby undermining market quality. It is difficult to reconcile the policy rationale underlying the different regulation of Dark and lit trading to address a hybrid market as proposed.

Also, if Hybrid is allowed to operate as an unprotected market and without Dark Rule restrictions, we can expect additional dark pools with segmented client access to look for ways to qualify as a 'hybrid' market and avoid the restriction of Dark Rules. This may lead to a proliferation of closed-access, semi-transparent liquidity pools, and increased liquidity fragmentation which cannot be virtually consolidated through OPR and the Consolidated Market Display.

Hybrid as Protected Market

If Hybrid is a protected market, it must contribute its quotes to the Consolidated Market Display and be protected under the Order Protection Rule. However, since Short-Marking Exempt (SME) participants cannot trade against Hybrid quotes, they need to filter them out, which creates a bifurcated industry Consolidated Market Display and NBBO. One would exclude Hybrid quotes and apply to SME participants and the other would include Hybrid quotes and apply to non-SME participants. This raises significant concerns for the foundation of our existing regulatory framework:

- Compromises the unity and integrity of the consolidated tape in representing protected quotes that contribute to the public price discovery process.
- Leads to investor and participant confusion, and loss of market integrity and investor confidence, over the integrity of the quote and market.
- As other hybrid models are introduced to the market, with possibly different bases for flow segmentation, the NBBO and Consolidated Market Display are further fragmented imposing a significant risk to market integrity.
- Investor orders posted on Hybrid can be traded through by SME participants, challenging the price priority – the foundation of investor perception of fairness.
- Introduces confusion and issues for any existing CSA and IIROC rules referencing the Consolidated Market Display, as well as marketplace and participant operations that reference the NBBO for pegging and re-pricing activities.

A single virtual consolidated book where all quotes are protected (which cannot be achieved if Hybrid quotes are included) is fundamental for market efficiency and integrity, as it is intuitive, priority is clear, it supports the visible price discovery process, it breeds investor confidence, and it promotes the concept of fairness.

Effectiveness and Fairness of Proposed Model

Industry participants generally agree that evolution in technology and the global regulatory framework has significantly impacted how today's public markets function. Industry experts around the world, including practitioners, regulators and academics, are working together to assess the impact of these changes on market efficiency and stability. In addition, efforts are underway globally to identify the risks of this new reality and identify solutions to mitigate these risks. These are complex issues for which there is currently a wide range of informed and conflicting views. Careful consideration of these issues is required to ensure that any new regulation or market structure models function appropriately and do not eliminate benefits obtained to date.

The Aequitas Proposal takes a strong view on issues underlying today's markets, and suggests that certain trading practices by high frequency traders lead to erosion of market quality and eventual loss of investor confidence. Therefore they propose to prevent SME participants from taking liquidity from the Aequitas Dark and Hybrid books. Aequitas has premised its proposal on issues for which there is no consensus, and propose a solution that will not resolve the issues.

In our view there are a number of issues with this proposal:

- Hybrid book will allow all participants to post liquidity, including HFT. Many of the 'predatory' HFT strategies, including 'disappearing quotes', 'passive front running' and 'quote pennying' are based on posting and cancelling posted liquidity at precise moments in time, and will therefore not be excluded from the Hybrid market.

- Orders designated with the SME marker, which Aequitas proposes to restrict, are not an effective or appropriate representation of HFT activity. The SME marker was designed with an entirely different purpose in mind related to short selling[1]. Practice shows that not all HFTs are SMEs and not all SMEs are HFTs. In addition, HFTs are broadening their trading strategies, making the SME marker an even farther departure from a proxy for HFT activity.

- Using the SME marker excludes a whole class of traders that do not engage in the type of activity Aequitas is looking to restrict.[2] Such SME participants, including market makers, provide the service of bridging buyers and sellers in time, or across markets, which positively contributes to liquidity. These SME participants should not have their access restricted.

We note that the US market operates with a number of liquidity pools with restricted active access such as Hybrid, and there is no evidence of that structure reducing volatility or overall HFT activity.

Anticipated Benefits do Not Justify Industry Costs

The current Aequitas proposal will impose significant adoption costs on industry participants due to its unique and complex market structure.

In addition to the costs associated with any new marketplace entrant, additional costs unique to the Aequitas Proposal include but are not limited to the following areas:

- Dual NBBO processing / book building

- Increased Information Processor costs to support dual NBBO products, potentially leading to increased consumer costs

- Inconsistencies between any market-by-order and market-by-price data displays incorporating Hybrid data, as Hybrid data cannot be displayed on an order-by-order level

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[1] SME designated active volume represented only 7.9% and 8.6% of TSX total volume in July 2013 and August 2013 respectively.
[2] TSX estimates that over 30% of SME designated volume on TSX is not associated with firms/traders that conduct or support HFT activity.

- Dual Data Feed integration into most electronic trading systems
- Development of new smart order router strategies based on user type
- Doubling of historical level-one quote and trade data sets, with and without Hybrid data
- Changing and/or providing exceptions to a number of key CSA and IIROC rules, specifically the Order Protection Rule, Dark Rules, Fair Access and Order Exposure rule, and any other rules referencing the Consolidated Market Display
- Investor and participant re-education on OPR, Fair Access, Dark Rules, and the consolidated book

There is no industry consensus on the issues that the Aequitas Proposal purports to address. It is uncertain whether the proposed model will address any or all of the issues raised by Aequitas. TMX Group therefore submits that it would not be appropriate or beneficial to proceed with rule changes, market structure complications, technical work, and captive industry cost involved in permitting Aequitas to proceed as proposed.

Rule Making Process

The Canadian regulatory framework is well developed, our retail participation rates are high and our markets have among the lowest HFT participation rates among developed markets globally. Other countries are looking at Canada as a positive example of effectively dealing with the evolution of market structure for equities trading.

As well described in the Notice and Request for Comment, the current regulatory framework is the result of thorough consultative processes, and we believe that this path of thoughtful and comprehensive review of regulatory proposals should be continued.

If the proposed Hybrid model is to be implemented, certain aspects of the regulatory framework will need to be amended, including Fair Access and Client Segmentation, Order Protection Rule, Order Exposure Rule, Dark Rules and the application of Consolidated Market Display, with broad consequences.

We submit that it is premature and inappropriate to modify these existing policies specifically to accommodate, or in response to, the Aequitas Proposal and without significant consideration to the broader implications of such changes outside of the model. TMX Group has significant concerns with the ‘policy by default’ approach that arises through product or proposal approvals that significantly alter the prevailing market structure and are inconsistent with the principles and objectives of the current regulatory framework. The rule review should be conducted and completed independent of the Aequitas Proposal. Any resulting rule changes must be clear on the revised underlying principles and objectives, be applicable to the market as a whole, be applied to all marketplaces and participants who wish to develop new models and change existing ones, and must allow ample time for the industry and market to assess and adapt prior to approval of any revised framework.

In fact, a number of regulatory initiatives looking to examine and assess many policies and market structure issues (e.g., Order Protection Rule review, IIROC’s HOT/HFT study, marketplace trading fees) predate the Aequitas proposal and are well underway. TMX Group continues to support these initiatives which look at changes holistically, and leverage evidence based research and a comprehensive public consultation process. TMX Group believes that these efforts should be permitted to come to a conclusion before any new market models are permitted that contravene the existing regulatory framework.

We support the regulator's efforts to consult publicly in advance of the formal application by Aequitas. The proposed design of the Aequitas model is extremely nuanced and complex, and will impose broad and significant changes on the operation and integrity of our market which must be thoroughly assessed and considered prior to any implementation.

Should you wish to discuss any of the comments with us in more detail, we would be pleased to respond.

Yours truly,

Kevan Cowan
President, TSX Markets
TMX Group Head, Equities

APPENDIX A

A. Segmentation of order flow

1. Segmentation of order flow in the context of the principles underlying OPR

> ***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?***

OPR should apply to all visible orders in order to protect the integrity of the consolidated order book and promote investor confidence.

> ***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?***

The main objective underlying OPR is protecting the better priced order, which promotes investor confidence, perception of fairness and price discovery and protects market integrity.

Therefore, if OPR is to apply to Hybrid, then it should apply in all cases, regardless of the type of participant, or else the orders on Hybrid (which could include “natural investors”, whether retail or institutional) would in some cases be traded through, undermining the OPR objective and investor confidence.

If OPR is not to apply to Hybrid, then Hybrid should be governed by the Dark Rules and abide by Dark Rule restrictions, including price improvement, size restrictions and giving priority to lit liquidity on the marketplace’s own order-books.

The third option, where OPR applies only to select participants, leads to a bifurcated NBBO and raises the following issues:

- Compromising the unity and integrity of the consolidated tape in representing protected quotes that contribute to the public price discovery process
- Introducing confusion over the true NBBO and changing the fundamental way in which the consolidated quote is viewed and considered in relation to protected quotes
- Encouraging a proliferation of other OPR-exempt models producing further fragmentation of the consolidated tape/NBBO and therefore posing a significant risk to market integrity
- Trade-throughs of investor orders posted on Hybrid by SME participants, challenging the price priority – the foundation of investor perception of fairness
- Introducing confusion and issues for any existing CSA and IIROC rules referencing the consolidated display as well as marketplace and participant operations that reference the NBBO for pegging and re-pricing activities

> ***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 stated above, if certain participants are restricted from taking liquidity from Hybrid, then in order to protect the integrity of the public quote, Hybrid quotes should not participate in the consolidated display.

> ***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 believe that if Hybrid is to proceed with segmented access, it should be treated as a Dark pool, and therefore its quotes should not be incorporated in the NBBO for the purposes of the Dark Rules or any other rules referencing NBBO or Consolidated Market Display.

2. Segmentation of order flow in the context of the principles underlying fair access

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

> ***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?***

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

In order to protect market integrity, we submit that any segmentation in the lit book should be limited to trading incentives (i.e. supporting different fees for different participants). Market models which go beyond that and prevent visible flow interaction will lead to fragmentation of the consolidated display and therefore negatively impact the price discovery process.

The Hybrid book would introduce client segmentation in accessing a visible market, therefore bifurcating the visible market, limiting access to the best displayed price and negatively impacting investor perception of fairness. This is fundamentally inconsistent with the objectives underlying the fair access requirements.

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

No, the SME marker was designed for an entirely different purpose and is not an appropriate proxy.

- Orders designated with the SME marker, which Aequitas proposes to restrict, are not an effective or appropriate representation of HFT activity. Practice shows that not all HFTs are SMEs and not all SMEs are HFTs.

- The SME marker was designed for an entirely different purpose, in relation to short selling.

- It is relatively easy for a SME participant to modify its trading patterns to not qualify for SME marking.

- Using the SME marker excludes a whole class of traders from the market that do not engage in the type of activity Aequitas is looking to restrict. Many SME participants, including market makers, provide the service of bridging buyers and sellers in time, or across markets, which positively contributes to liquidity. They should not have their access restricted.

We further note that Hybrid will allow all participants to post liquidity, including HFT. Many of the ‘predatory’ HFT strategies, including ‘disappearing quotes’, ‘passive front running’ and ‘quote pennying’ are based on posting and cancelling posted liquidity at precise moments in time, and will therefore not be excluded from the Hybrid market.

B. Aequitas market making program

1. Market maker priority

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

Matching priority is a form of incentives given to market makers in return for fulfilling their obligations. We support marketplaces having the ability to design competitive market making programs with different incentive/rewards models, as long as the program adoption is subject to competitive forces and participants can choose whether to participate when posting liquidity.

Since sufficient details regarding the Aequitas market making program are not published, we are not in a position to comment on the balance between the obligations and benefits, and the anticipated effectiveness of the model. However, it is our view that an order book which combines NBBO pegging with market making priority will lead to the market maker being at the top of the book the majority of the time, therefore having significant advantage over all other participants in the book (other than same broker's orders. According to the Notice and Request for Comment, it is expected that market makers would be HFT firms (specifically DEA client market makers).

> ***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 Dark, Lit and Hybrid are three books of the same market, then it is reasonable to tie benefits in one book to the obligations in another. However, this structure does require that lit liquidity on any book must have priority over any dark or semi-dark liquidity on any other book, as per the Dark Rules.

If Dark, Lit and Hybrid books are structured as separate marketplaces, then benefits and obligations must be applied to each marketplace separately or otherwise there would be a bundling of services across different marketplaces contrary to Fair Access requirements (i.e., if the Aequitas Lit market maker qualifies for the benefits in the Aequitas Hybrid book, then market makers from any other lit marketplace should also qualify.)

> ***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?***

As stated above, we support marketplaces being allowed to design competitive market making programs, and believe that competitive forces will drive efficiencies from each program.

However, in order to qualify for IIROC market making benefits, obligations should be at least as onerous as those imposed on the listing market.

2. DEA clients as market makers

> ***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?***

There are few details on the proposed market making model. This prevents us from properly commenting on whether such a model would provide an appropriate level of accountability, supervision, monitoring and investigative processes and practices, whether through the sponsoring dealer or otherwise.

TMX Group is of the view that market making activities must comply with UMIR, and therefore be subject to IIROC supervision, either directly or through the sponsoring dealer.

Although the Aequitas Proposal indicates that the sponsoring dealer would be accountable for the actions of the DEA client market maker, the Notice and Request for Comment indicates that the sponsoring dealer might not be responsible for any actual violation of UMIR rules. We believe this leaves an oversight gap and therefore, based on our limited understanding of the proposal, we do not support such an arrangement.

> ***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?***

TMX is of the view that the same obligations, including regulatory supervision, should apply to all parties in the formal market making role. Theoretically, this could be a different set of obligations than the one that applies to parties engaging in trading activity other than market making, potentially leading to special registration status and IIROC membership specific to market makers. However, we submit that drawing a clear line between market making and other trading activity would likely prove to be a challenging task.

C. Potential impact of Hybrid on market quality and market integrity

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

As elaborated in our answers to questions 1 to 8, we submit that the design of Hybrid will have a broad impact on the whole market, including a negative impact on the efficiency of the price discovery process in visible markets and on investor confidence.

> ***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.***

In our view the potential benefits of Hybrid do not justify the potential risks related to market integrity and investor confidence as a result of:

- Reduced effectiveness of price discovery
- Orders posted on Hybrid being traded-through
- Orders posted on Hybrid switching from being visible to being dark as the NBBO changes, leading an investor to believe his/her order was cancelled
- Confusion from having different NBBO displays among different systems and vendors

In addition, TMX is of the view that the industry integration costs far outweigh the possible benefits of the Hybrid solution. In addition to the costs associated with any new marketplace entrant, additional costs unique to the current Aequitas Proposal include but are not limited to the following areas:

- Dual NBBO processing / book building
- Inconsistencies between any market-by-order and market-by-price data displays incorporating Hybrid data, as Hybrid data can not be displayed on order-by-order level

- Dual Data Feed integration into most electronic trading systems
- Development of new smart order router strategies based on user type
- Doubling of historical level-one quote and trade data sets, with and without Hybrid data
- Changing and/or providing exceptions to a number of key CSA and IIROC rules, specifically the Order Protection Rule, Dark Rules, Fair Access and Order Exposure rule, and any other rules referencing the Consolidated Market Display
- Investor and participant re-education on OPR, Fair Access, Dark Rules, and the consolidated book

Since there is no industry consensus on the issues that the Aequitas Proposal purports to address, and it is uncertain that the proposed new model would successfully address them, TMX Group submits that it would not be appropriate or beneficial to proceed with rule changes, market structure complications, technical work, and captive industry cost involved in its introduction to the market. There are a number of regulatory reviews underway which will be relevant to issues raised by the Aequitas Proposal which should be concluded before any new market models are permitted that contravene the existing regulatory framework.

D. Hybrid as a visible market

> ***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?***

While there may be circumstances when a pilot may be appropriate, we submit that this is not an appropriate case. Aspects of the Aequitas Proposal are inconsistent with the current regulatory framework and the principles that underlie it. The costs of adoption are very high and once incurred cannot be repatriated. Further, any changes to the underlying principles and objectives must be determined through a public consultation process taking into account the interests of the market as a whole, be applicable to all marketplaces and market participants, and allow ample time for the industry to prepare and adapt. Lastly, it would be very difficult to measure the impact of such a pilot on principles such as investor confidence and the quality of price formation.

> ***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?***

We submit that Hybrid could fit into the established regulatory framework if it is considered a dark pool and subject to Dark Rules, including price improvement, minimum size requirements and giving priority to lit liquidity on same marketplace's order books.

Hybrid quotes would not be protected and they would not contribute to the consolidated book and the NBBO and client segmentation would be supported.