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VIA EMAIL

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Attention: OSC Staff and Mr. Thompson

**Re: CX2 Canada ATS Notice of Initial Operations Report and Request for
Feedback**

TMX is pleased to respond to the Notice of Initial Operations Report and Request for Feedback filed by Chi-X Canada ATS for the proposed introduction of their second Canadian marketplace CX2 Canada ATS. Our comments focus on implications of extending the benefit of broker preferencing to anonymous orders and drawing attention to the proposed omission of cross interference in the CX2 order book. We believe that permitting the benefit of broker preferencing to anonymous orders may produce negative impacts to market quality and the price discovery mechanism of visible markets in Canada.

Anonymous Broker Preferencing

Broker Preferencing is an accepted and valued feature of the Canadian market along with the underlying principle of broker preferencing being transparency. Broker preferencing is a unique allocation attribute enacted on many Canadian equity marketplaces. The advantages afforded by broker preferencing attempt to bring the benefits of internalization on-exchange and include strengthened price discovery, increased transparency and visible liquidity. It is an accepted understanding that those who receive the benefits of broker preferencing do so by contributing to the transparency of the visible book.

Orders in the book which are attributed provide valuable information as to the number of participants that are contributing to establishing a market for those securities. Participants viewing an order book which is only comprised of non-attributed orders are unable to determine if one participant is making the market and influencing the price of the security or if there is greater participation. It has also been suggested that broker attribution increases liquidity in a security as brokers are able to determine who has tradable interest.

When an order receives allocation priority due to broker preferencing, broker attribution provides information as to why this event occurred. Brokers resting in the book have the ability to verify why they did not receive a fill. The absence of broker attribution would create uncertainty as to the proper functioning of markets as each side of the trade may not be attributed, therefore making it difficult to determine if the trade was actually a result of broker preferencing or an advantage received for some unknown reason. In addition extending the benefit of broker preferencing to anonymous orders removes the incentive for brokers to remain attributed, which further encourages reduced transparency in the visible book. We would also note that the recent decision prohibiting broker preferencing of jitney orders illustrates recognition by the industry and the regulators of the risks associated with extending an allocation benefit to orders facilitating anonymity.

An unintended consequence of extending broker preferencing to anonymous orders and also to the undisclosed volume of iceberg orders is the potential for a dramatic increase in the use of the iceberg order type and reduction in displayed volume. TMX has always held that transparency is an invaluable pillar of market quality and should be incented. This in part has been achieved on the TMX markets through the allocation priority given to an iceberg's disclosed volume. Extending the benefits of broker preferencing to anonymous orders and the undisclosed volume of icebergs may encourage a reduction of disclosed volume to the minimum permissible board lot, further eroding visible volume in the displayed markets. A reduction in disclosed volume may also increase the probability of price volatility in the displayed markets. With the exponential use of routing strategies involving the bypass marker, a reduction of disclosed volume may leave the markets more susceptible to price shocks as bypass orders, which only interact with disclosed volumes, clear out thin price levels.

Intentional Crosses

Our understanding is that the proposed operations of CX2 Canada ATS will not subject intentional crosses to interference from orders that are enabled for broker preferencing. We feel it is important that participants are aware that time priority of the visible book may be undermined in CX2. Within the proposed allocation methodology of CX2 where time priority is maintained when multiple passive orders receive the benefit of broker preferencing, some participants may be under the impression that time priority should also be adhered to when orders are submitted from the same broker as an intentional cross. If there is an order already displaying their intention in the book at the same price from the same firm, it is important to understand that the booked order's time priority will not be honoured and the cross will not be subject to interference.

Conclusion

It is our view that OSC staff should not permit CX2 to extend broker preferencing to apply to those orders marked anonymous given the potential impact to transparency, price discovery and market quality. We would also encourage CX2 to ensure that the proposed handling of intentional crosses is fully transparent so that participants are aware of when time priority is not being maintained in the visible book.

Thank you for the opportunity to provide our comments on the Request for Feedback filed by Chi-X Canada ATS. Please feel free to contact us with any questions or requests for clarification.

Best Regards,



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cc : Robert Fotheringham, TMX Group
Amer Chaudrey, TMX Group