CANADIAN SECURITY TRADERS ASSOCIATION, INC.
P.O. Box 3, 31 Adelaide Street East

Toronto, Ontario M5C 2H8

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Market Regulation Branch

Ontario Securities Commission

20 Queen St. West, 22nd Floor

Toronto, ON

M5H 3S8

marketregulation@osc.gov.on.ca

And to:

Michael Grecoff

Securities Market Specialist

British Columbia Securities Commission

701 West Georgia Street

P.O. Box 10142, Pacific Centre

Vancouver, BC V7Y 1L2

Email: MGrecoff@bcsc.bc.ca

And to:

Mark Faulkner

Vice President, Listings and Regulation

CNSX Markets Inc.

100 King Street West, Suite 7210,

Toronto, ON, M5X 1E1

Email: Mark.Faulkner@thecse.com

RE: Proposed Fee Model for TSX and TSXV Listed Securities Trading on the Canadian Securities Exchange – Notice of Proposed Change and Request for Comment

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 four distinct regions (Toronto, Montreal, Prairies 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 CSTA Trading Issues Committee (TIC) 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 views and statements provided below do not necessarily reflect those of all CSTA members or of their employers.

The TIC appreciates the opportunity to comment on the 2021 Fee Proposal by the Canadian Securities Exchange (CSE). Given the proposed fee change is substantially similar to what was previously proposed and withdrawn back in 2016, our comments are also substantially similar. Under the 2021 CSE proposal, the fees passive participants would pay to post liquidity are dependent upon the nature of the counterparty and type of liquidity being provided. Interaction with spread crossing, guaranteed-minimum-fill (GMF) orders would have an inverted fee schedule while provision of traditional lit market liquidity would have a traditional maker-taker structure. In this context, the TIC believes the GMF mechanism is being used as a proxy to identify the presence of retail orders and to provide the retail brokers with preferential trading fees with minimal risk or obligations from liquidity providers. We re-iterate our long-standing opposition to any proposal that provides for and incentivizes the segmentation of retail trading away from the rest of the marketplace. Our comments will focus on the following two points:

Fair access – how would the Fee Proposal, which entails the passive side of a trade paying trading fees depending on the nature of an incoming order, impact fair access to such passive participants?

Informational advantage – would the passive participant on the CSE have an informational advantage over other market participants since they would have information about the nature of the incoming order flow and, specifically, about the nature of the counterparties to their trades, that is not available to other market participants.

Fair Access

In our opinion, it is inappropriate to offer differential pricing for precisely the same fill in the lit market depending on the nature of the counterparty. In April 2013, Alpha Exchange ("Alpha") made a similar proposal that was subsequently denied regulatory approval. Whether the differentiated fee is applied to an order that is executed passively (CSE's current Fee Proposal) or actively (Alpha's proposal which was denied), this does not change the underlying rationale. We believe that it is unfair to passive participants to have their fees determined by the nature of an incoming order and not by their own actions or decisions.

The proposed fee model constitutes an unreasonable degree of marketplace discrimination and is a violation of the Fair Access requirements in NI 21-101:

5.1 Access Requirements

(3) A marketplace must not

(a) permit unreasonable discrimination among clients, issuers and marketplace participants, or

(b) impose any burden on competition that is not reasonably necessary and appropriate.

Reasonable degrees of marketplace discrimination are already well embedded into our market structure. For example, lit orders have priority over dark orders, large orders are subject to a different order exposure rule then small orders, market orders take priority over limit orders and passive orders are charged different transaction fees than active orders. In our view, such examples are all reasonable degrees of marketplace discrimination. In each case the discrimination is based upon the orders' characteristics and/or the actions of the routing broker. Unreasonable discrimination would include discrimination across exchange participants or client types or any other inherent characteristic or proxy measure that is immutable.

Specifically, in the 2021 CSE proposal, our concern rests with the CSE's use of the GMF eligibility criteria. The GMF definition effectively identifies orders with the same characteristics as retail orders e.g. small size, non-recurring and spread crossing. Thus, while the fee model doesn't explicitly vary with the type of client (institutional vs. retail) a fee model based on the GMF eligibility criteria effectively has the same result: spread crossing retail orders pay less than otherwise similar institutional orders. Such discriminatory pricing by a marketplace is unreasonable and constituents an impediment on order by order competition for liquidity. Thus, we believe the proposed fee model violates the Fair Access requirements of NI 21-101.

Information Leakage

It is important to note that the information disclosed by trading with the current CSE GMF facility and TSX MGF facility is not equivalent to the information leakage in the Fee Proposal. The CSE is proposing to provide fee information that allows for the reverse engineering of the participant type, whereas the current TSX MGF and CSE GMF only allow for identification when a trade was executed within the Minimum Fill facilities themselves.

The CSE proposes a fee model that would allow liquidity providers the ability to identify the nature of their trading counterparty (GMF eligible aka retail or GMF non-eligible aka non-retail) by reverse engineering the transaction fees paid on a trade-by-trade basis at the end of the day. This private fee information would not be available to all marketplace participants and could be used to identify the presence and recurrence of large, directional, multi-day, non-retail orders.

Identifying the presence of a large, potentially recurring, non-GMF eligible order is extremely valuable. Indeed, most traders would happily quote a larger displayed size or slightly better price if they knew the other side of a potential trade was a GMF or retail order. What is often over-looked is that the inverse of that statement is also true: most traders would want to show a slightly smaller size or slightly worse price if they knew the other side of a potential trade was from a non-retail order. Thus, any economic efficiencies resulting from the effective display of a retail marker (GMF or other proxy) also come at the expense of the non-retail order. We believe any marketplace that allows for the leakage of private client information, directly or indirectly via transaction fees or any other criteria, potentially jeopardizes the execution quality of non-retail orders and thus creates an unreasonable burden on order by order competition.

The 2021 CSE Fee Proposal violates the Fair Access requirements of NI 21-101 and creates an undue burden on order by order competition by providing an informational advantage to some participants that is not available to others. The proposal should not be granted regulatory approval.

The CSE seeks to:

- Improve fill quality and fill size per agency order which will, in turn, lower dealer back-office costs and reduce information leakage caused by the current practice of multiple sweeps.
- Protect passive liquidity providers against specific proprietary trading strategies, allowing visible quotes to persist long enough to interact with incoming GMF eligible orders.
- Maintain reduced execution costs for investment dealers managing GMF-eligible orders by continuing to provide a rebate for active orders on the TSX and TSXV listed securities.

We don’t disagree with any of these goals; however, we do object to the methods the CSE is proposing to achieve these goals. If a marketplace can only manage to improve the retail trading experience at the expense of non-retail traders, then the collective interest of all participants is no better off. It is not the role of a marketplace to redistribute the benefits of price discovery across clients. A marketplace should be free from unreasonable discrimination and should not impose any unnecessary burden on order by order competition.

We thank you for the opportunity to comment. Please feel free to contact any of the Trading Issues Committee leads if you have any further questions or wish to continue the discussions.