TriAct® CANADA MARKETPLACE

January 17, 2011

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Autorite des marches Financiers
Manitoba Securities Commission
Ontario Securities Commission
New Brunswick Securities Office
Office of the Attorney General, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Nunavut
Registrar of Securities, Yukon Territory

Attention:

John Stevenson
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, ON M5H 3S8

Madame Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, Tour de la Bourse
Montréal (Québec) H4Z 1G3

James Twiss – Vice President, Market Regulation Policy
Kevin McCoy – Senior Policy Analyst, Market Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 1600, 121 King Street West,
Toronto, ON M5H 3T9

Dear Mme. Beaudoin & Messrs. Stevenson, Twiss and McCoy:

TriAct Canada Marketplace LP ("TriAct") is pleased to have the opportunity to comment on the Joint CSA/IIROC Position Paper, 23-405, on Dark Liquidity in the Canadian Market.

TriAct (a wholly-owned subsidiary of ITG Canada Corp.) is an Alternative Trading System that operates MATCH Now^{SM}, Canada's leading dark pool for Canadian listed securities. MATCH Now is a broker-neutral, fully confidential trading book where order information is not visible to other traders and buy and sell orders are matched using a combination of frequent call matches and continuous execution opportunities.

TriAct supports the objectives outlined by the CSA and IIROC position paper and believes that the MATCH Now business model is aligned with those objectives. We support the efforts of the Canadian regulators to establish a framework that is consistent with the principles outlined in the position paper and also with the principles and guidance proposed by the Technical Committee of the International Organization of Securities Commissions (IOSCO) on dark orders and dark pools. However, we do not believe that there is any evidence that suggests that the public interest of Canadian investors requires new restrictions for dark liquidity in National Instrument 21-101, Marketplace Operation.

It is important to note that dark trading is still a relatively small portion of trading and liquidity in Canada. Dark pools have only recently and occasionally exceeded 2% of total executed volume in Canada, whereas it is often represented by industry reports that in the U.S. and Europe they have accounted for more than 10% and 4%, respectively. In addition, 98% of the stocks traded on MATCH Now are on the IIROC Highly Liquid Stock list[1]. By this qualification we would suggest that these Highly Liquid Securities enjoy significant price discovery. In addition, based on a recent review of MATCH Now trades, the average spread at trade execution was approximately 1.4 cents, which supports the view that most securities traded on MATCH Now achieve significant price discovery in the transparent markets. It is clear through empirical evidence that price discovery is not suffering because of trades that are now executing on MATCH Now.

In a recent article[2]entitled "Are We Missing the Evidence in the Global Dark Pool Debate?", author Ian Domowitz[3]examines recent research on dark pool trading. Mr. Domowitz concluded that there is no concrete evidence to support the idea that dark pool trading has a detrimental effect on market quality and execution performance. In addition, three academic experts[4] on market structure recently analyzed activity on 11 large US dark pools, representing nearly half the dark liquidity market share in the U.S. The report concluded that: "*Higher dark pool activity is associated with lower quoted spreads, lower effective spreads, small price impact and low short-term volatility. Securities with large amounts of dark pool trading are characterized by greater quoted depth in the lit markets, and exhibit smaller order imbalances relative to share volume than stocks for which dark pool trading is minimal.*"

CSA/IIROC Staff Recommendation #1: "The only exemption to pre-trade transparency should be for orders that meet a minimum size threshold."

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[1] A "highly-liquid security" is defined as a listed security or quoted security that:

- has traded, in total, on one or more marketplaces as reported on a consolidated market display during a 60-day period ending not earlier than 10 days prior to the commencement of the restricted period:
  - an average of at least 100 times per trading day, and
  - with an average trading value of at least $1,000,000 per trading day; or
- is subject to U.S. Securities and Exchange Commission Regulation M and is considered to be an "actively-traded security" under that regulation. An actively traded security under Regulation M must have an average daily trading volume of at least $1 million and a public float of at least $150 million.

[2] Ian Domowitz ,ITG Insights, Volume 1, Number 10, December 8, 2010: *Are We Missing the Evidence in the Global Dark Pool Debate?*

[3] Ian Domowitz is Managing Director of ITG Inc., responsible for ITG's networking, research and analytical products. Previously, he served as Smeal Professor of Finance at Pennsylvania State University and has also held positions with Northwestern's Kellogg School of Management, Columbia University, The CFTC, IMF and the World Bank.

[4] *"Diving into Dark Pools,"* by Saritna Buti (University of Toronto - Joseph L. Rotman School of Management), Barbar Rindi (Bocconi University - IGIER; Bocconi University) and Ingrid Werner (The Ohio State University - Fisher College of Business), Dice Center WIP 2010-10, Fisher College of Business WP 2010-03-010).

We agree that any regulatory framework on market structure should promote price discovery and therefore encourage orders to be transparent to the public and subject to pre-trade transparency. However, this objective should not be accomplished through the imposition of regulations that restrict the use of dark liquidity, especially when the obligation of best execution is optimally achieved by employing a combination of displayed and dark liquidity.

Dealers need the flexibility to determine how to best execute their client and proprietary orders irrespective of their size. The facts and circumstances of the market conditions, liquidity, costs, and timing are just some of the factors that guide a trader through the best execution process. We maintain that the current Universal Market Integrity Rules (UMIR) already address the objectives outlined in the proposals with Order Exposure requirements for orders of less than 50 Standard Trading Units. Specifically, UMIR 6.3 (Exposure of Client Orders) provides guidance on situations where an order may not need to be "immediately" entered "on a marketplace that displays orders." Under UMIR 6.3 (e), the participant is permitted to determine, based on market conditions, whether the entering of an order would or would not be in the best interests of the client, regardless of the order's size. These provisions support the notion that a participant should have some discretion even with smaller sized orders to protect the interests of their clients. Specific to the entry of orders in a dark pool, UMIR section 6.3 (h) provides that if the client has directed or consented to the order being entered on a marketplace as: (i) a Call Market Order or (v) a Market-on-Close Order, a participant has always had the ability to send smaller orders to dark destinations. Based on the above mentioned provisions, the UMIR clearly has sufficient and effective rules for dealers to address the concerns raised by the CSA/IIROC.

We fundamentally believe that it is inappropriate to introduce order size restrictions in NI 21-101. In fact we believe that any size restriction would ultimately be detrimental to dealers and investors achieving Best Execution as it would limit access to dark liquidity and trading opportunities. To further illustrate our point, we submit the following concerns and positions:

- It is essential for sell-side and buy-side traders to be able to determine how best to manage their orders. They may use a variety of trading strategies and venues which should be able to include dark liquidity in a transparent market. The trader could also choose to use an algorithm or even manually piece out their orders across various venues at their discretion. To place size restrictions on how a trader can allocate passive orders will impede the trader's ability to use his/her experience and judgment on how to achieve Best Execution. In turn, if a trader could possibly get a better price than what is displayed on even a small order, then it should be the trader's choice if not, an obligation, to seek out that price improvement. MATCH Now seeks to provide traders with an additional tool to achieve Best Execution; it does this by integrating with smart routers, providing various trading options and features, including price improvement over the displayed quote, as well as minimizing the cost to access liquidity.

- Even with the option to choose minimum size on passive orders, we note that our clients typically do not use this feature. The average order size posted by institutional investors in MATCH Now is, on average, less than 2,000 shares which results in average execution sizes that are similar to the displayed markets of between 300 to 500 shares. We acknowledge that currently around 80% of MATCH Now trades involve Market flow orders. However, our customers have demonstrated that dark liquidity can successfully facilitate the interaction of retail and algorithmic order flow with large block orders.

- Clients that post large block trades in a dark pool are concerned about the risk of information leakage and its effect on market impact. We therefore suggest that if it is absolutely necessary for the CSA and IIROC to establish a minimum size, then it should be no greater than 5 board lots, which would minimize the value of any signals from post trade reporting provided by dark pools and dark orders. We also note that there is no historical evidence presented by the CSA or IIROC that small-sized dark orders have impeded price discovery. We also note that market integrity appears to benefit from the dark liquidity posted in the TSX Market-on-Close facility with lower price volatility at the end of the day.

CSA/IIROC Staff Recommendation #2: Two dark orders meeting the minimum size exemption should be able to execute at the NBBO. Meaningful price improvement should be required in all other circumstances, including all executions with orders not specifically marked in a manner indicating they are utilizing the minimum size exemption.

We reiterate that there should be no minimum size restrictions on dark orders and argue that there may be situations where executing at the NBBO is appropriate and consistent with best execution. In MATCH Now, when the displayed market is locked[5], the participant can elect to accept the NBBO price. The vast majority of clients elect for the NBBO in a locked market. We believe that this provides an advantage to both the dealer and their client. The dealer generally saves on execution costs, while the client gets access to liquidity at the best available price.

CSA/IIROC Staff Recommendation #3: Visible orders on a marketplace should execute before dark orders at the same price on the same marketplace. However, an exception could be made where two dark orders meeting the minimum size threshold can be executed at that price.

We agree with this CSA/IIROC recommendation. Visible orders should receive priority over dark orders in the same marketplace. This is an essential factor of rewarding price discovery and promoting market integrity. As noted above, we do not believe there needs to be a regulatory exemption based on order size for a locked market.

CSA/IIROC Staff Recommendation #4: Meaningful price improvement means that the price is improved over the NBBO by a minimum of one trading increment as defined in UMIR, except where the NBBO spread is already at the minimum tick. In this case, meaningful price improvement would be at the mid-point of the spread.

MATCH Now currently offers two levels of price improvement for orders: (1) mid-point for liquidity to liquidity matches and (2) 80/20 split[6] of the spread between posted dark liquidity and market bound active orders ("Marketflow orders"). We believe that the debate about valuing the amount of price improvement must also factor in the costs to execute the trade. CSA/IIROC note concerns about sub-penny quote jumping and that the amount should be meaningful. The total cost to the passive trade as well as the total savings earned on the active trade should be considered when addressing a market integrity question. Our view is that regulations should always look at the overall cost and

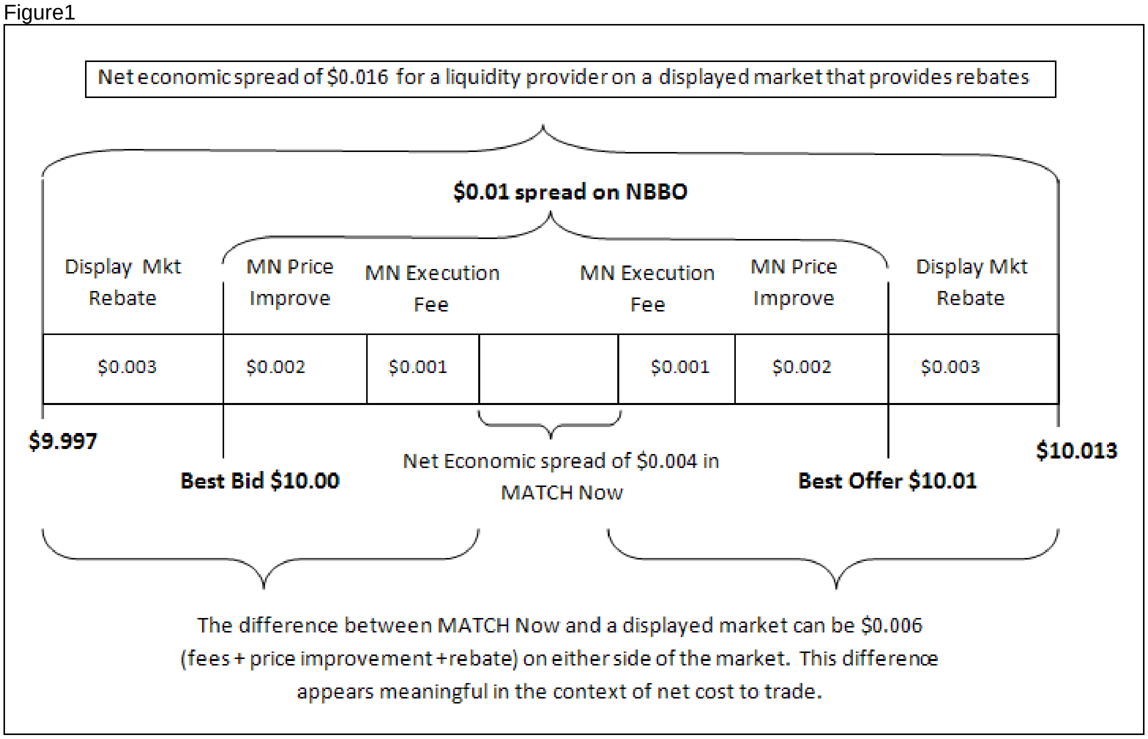
[5] This occurs when the highest displayed bid from one marketplace equals the lowest displayed offer from another marketplace.
[6] The maximum price improvement in this situation is one cent.

impact to the industry before imposing prescriptive thresholds. The CSA/IIROC recommendations clearly support the mid-point matches as being meaningful price-improvement.

We believe that both of our price improvement models; mid-point matching on two dark orders, and 20% price improvement for Marketflow orders, provide meaningful price improvement. In addition to price improvement to the posted NBBO, on average MATCH Now charges substantially lower active execution fees on Marketflow than the displayed markets. These savings are captured by our subscribers but over the long term they should benefit investors as the cost of trading decreases.

To illustrate, the difference between entering liquidity in a market that provides rebates and a dark market that charges a fee and provides price improvement is typically more than a half cent on a one cent spread (figure 1).

Figure1



Liquidity providers in MATCH Now pay a premium for the opportunity to interact with quality liquidity and less risk of market impact from exposing their order on a displayed market. We therefore argue that the MATCH Now business model does not fall in the "sub-penny quote jumping" concerns raised by the CSA and IIROC.

We recently looked at the average amount of price improvement provided by liquidity providers and concluded that, based on the average spread of 1.4 cents, and assuming that 80% of the liquidity orders are trading with Marketflow orders, the resulting average price improvement is 0.36 cents per share. When you factor in the potential cost savings on the execution fees, we believe the net benefit to the active order on MATCH Now is meaningful. Furthermore, the cost to the liquidity provider is also significant since we do not provide rebates that could offset the cost of execution.

We may not have found the perfect balance between fees rebates and price improvement, but we believe that our current model does achieve the objectives outlined by the CSA and IIROC by providing meaningful price improvement from dark orders. Finding this balance is what market competition and innovation should be all about.

In the Spring of 2011, MATCH Now plans to offer an option to specify mid-price execution when trading with Marketflow orders. This new feature provides the trader with two new benefits: 1) it removes the signal provided by post trade reporting to the side of the liquidity provider and 2) it will give these orders priority over other liquidity providers that are only willing to provide 20% price improvement. As MATCH Now continues to offer a variety of trading options, subscribers and their customers will have the flexibility to develop trading strategies that best suit the outcomes they are seeking and ultimately facilitate best execution.

Summary

Market Structure is being examined by regulators on a global basis. European, Australian and American regulators are all raising concerns about dark orders and their potential impacts on price discovery and market integrity. However, we do not believe that there is conclusive evidence that dark liquidity has any negative impact on market integrity. To the contrary, many market structure experts seem supportive of dark pools and dark orders. This was evident from the "Consultation Paper 23-404 Dark Pools, Dark Orders, and other Developments in Market Structure in Canada" where the comments by and large supported dark pools in Canada. The debate in Canada arguably has moved from whether there should be dark pools and dark orders to how these pools of liquidity should operate. We suggest that, until there is evidence that price discovery and/or market integrity is at risk, regulators should not implement prescriptive restrictions on order size. We also caution that a subjective evaluation on what is meaningful should not eliminate business models currently in place that appear to provide significant benefits to both retail and institutional investors. And finally, we agree with Mr. Domowitz's overall conclusion that there is no evidence indicating that dark pool trading negatively affects execution quality in the marketplace. Specifically, Mr. Domowitz has stated, based on independent studies and ITG's own research that: "*It is too early to conclude that dark pool activity contributes to market quality in a causal sense. On the other hand, there is nothing to suggest the opposite. No empirical evidence based on dark pool data supports the notion that dark pool trading has a detrimental effect on quality of markets and executions."*

We would like to thank the CSA and IIROC for allowing us to share our experiences with dark trading, and to present our comments, concerns and suggestions.

Sincerely,

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