



Asset Management

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Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Manitoba Securities Commission
New Brunswick Securities Commission
Nova Scotia Securities Commission
Ontario Securities Commission
Saskatchewan Financial Services Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Nunavut
Superintendent of Securities, Prince Edward Island

c/o John Stevenson, Secretary
Ontario Securities Commission
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Suite 1900, Box 55
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M^{re} Anne-Marie Beaudoin
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Dear Sirs and Mesdames:

**Re: Canadian Securities Administrators (“CSA”) Request for Comments –
Proposed Amendments to National Instrument 21-101, Marketplace
Operation and National Instrument 23-101, Trading Rules**

On behalf of TD Asset Management Inc. (“TDAM”), we appreciate the opportunity to



comment on the CSA proposal to amend National Instrument 21-101, *Marketplace Operation* and National Instrument 23-101, *Trading Rules* (collectively, the “Proposed Amendments”).

TDAM is a wholly owned subsidiary of The Toronto-Dominion Bank and is one of Canada’s largest asset managers. As of May 31, 2011, TDAM managed approximately \$175 billion for mutual funds, pooled funds and segregated accounts and provided investment advisory services to individual and institutional investors, pension funds, corporations, endowments, foundations and high net worth individuals.

We are responding in our capacity as an investment adviser.

General Comments

As one of the largest asset managers in Canada, TDAM represents the interests of many institutional and individual investors. It is important for large asset managers to have a variety of tools at their disposal, including Dark Pools and Dark Orders, to trade large blocks of securities without information leakage to the marketplace. In this regard, Dark Pools and Dark Orders benefit investors and our markets generally. They provide market participants more choice in determining optimal execution strategies and spur competition among trading venues. This ultimately helps in seeking to lower trading costs and is a factor which helps to provide best execution to the Canadian investing public.

TDAM has a strong interest in ensuring that the Canadian securities markets are competitive, and efficient in facilitating risk transfer for the benefit of all market participants. On the one hand, we recognize that Dark Pools and Dark Orders clearly bring certain benefits to investors that trade in large sizes, but on the other hand, raise concerns that they may impede price discovery and transparency - both important elements of an efficient market structure. Nevertheless, we see Dark Pools and Dark Orders to be of net benefit to the marketplace.

We recently provided comments to the Joint CSA/Investment Industry Regulatory Organization of Canada (“IIROC”) Position Paper 23-405, *Dark Liquidity in the Canadian Market* (“Position Paper”) on January 10, 2011. In our comment letter, we submitted that any new regulations affecting Dark Liquidity should be carefully considered and implemented only if it is clear that Dark Liquidity inhibits the overall functioning of the markets in a material and quantifiable manner. In the event that any amendments to existing legislation are proposed, they should be principles-based, striking a healthy balance between price and liquidity discovery, as any prescriptive rules could result in significant unintended consequences.

We commend the CSA for actively seeking input from market participants on the Proposed Amendments. TDAM is generally in agreement with proposals concerning the transparency around marketplaces, the guidance regarding the definition of an order, and clarifications as to when an indication of interest is considered an order.

We however, remain concerned that the Proposed Amendments impose rule based constraints on Dark Liquidity in the Canadian market in the absence of empirical studies evidencing the systemic risks of principles based regulation in this area. We believe that principles-based alternatives exist which would meet the CSA's immediate goals, which are to implement the structure for the regulation of Dark Liquidity as soon as possible, in addition to fostering fair and efficient capital markets and confidence in those markets. We will discuss these alternatives below.

Information Transparency Requirements for Markets Dealing in Exchange-Traded Securities

Our comments will focus on the CSA's proposal to establish a minimum size threshold for the exemption from the transparency requirements applicable to orders in NI 21-101. We continue to have concerns with respect to any measure that will establish regulations respecting Dark Pools which focus only on a minimum size threshold for posting liquidity. We believe that proposals to regulate this area in this manner could not only cause significant unintended consequences, some of which are noted below, but also bring uncertainty to the marketplace given the regulation services provider's proposed explicit ability to enforce minimum size thresholds that would impact the business models of existing and future Dark Pools in Canada.

20 comment letters were submitted to the CSA in response to the Position Paper, which sought the industry's views on imposing a minimum size threshold for accessing Dark Pools in Canada. The CSA provided that two thirds of respondents did not agree that a minimum size threshold would be beneficial to the Canadian market. Of the remaining one third which supported the proposal, the CSA noted that some of the respondents in this category were concerned that risks, such as the potential to game orders existed with the implementation of this regime. Additionally, a consensus on how to determine the minimum size was not reached among respondents that supported the proposal.

The CSA noted that it is important to establish a regulatory framework to address any market risks associated with Dark Pools as soon as possible. To do so, it is proposing to amend sub-sections 7.1(2) and 7.3(2) of NI 21-101 to establish a minimum size threshold as determined by a regulation services provider, which is expected at this time to be IIROC. **TDAM believes that establishing a framework to regulate Dark Pools by focusing solely on the minimum size threshold as a barrier to entry will not result in an improved market structure.** Alternatively, we submit that the CSA's goal of establishing the framework to regulate Dark Pools immediately would be met if the above sub-sections were amended in a manner which provides that the exemptions in sections 7.1 and 7.3 will apply under the circumstances that are prescribed by the regulation services provider. We strongly believe that additional industry review and commentary is required before providing IIROC with only one means of seeking to manage any risks associated with Dark Liquidity in Canada.

Amending sub-sections 7.1(2) and 7.3(2) in this manner would empower IIROC to respond to marketplace risk in the most direct and efficient way possible. The Companion Policy to NI 21-101 should also be amended to provide that the regulation services provider may establish specific requirements for market participants seeking to rely on the exemptions contained in Part 7 of NI 21-101, including a minimum size threshold where considered necessary.

Since the Proposed Amendments provide IIROC with only one method to regulate Dark Pools, this creates a risk if it is determined that regulating the minimum size provides little to no effect on reducing market or systemic risks. Accordingly, NI 21-101 would need to be amended once again in order to enable IIROC to act in a different manner to reduce those observed risks. If the CSA adopts our proposal, IIROC could establish a minimum size threshold, and/or adopt any other method that it has determined can reduce any risks to the Canadian market associated with Dark Pools. Additionally, IIROC could flexibly establish different requirements for different marketplaces, where the characteristics of those marketplaces warrant the establishment of alternative regulatory responses to reduce risk. No further amendments to NI 21-101 would be required if IIROC moved forward with the establishment of a minimum size threshold, or adopted other requirements for accessing a Dark Pool.

As the CSA has stated, any measure to regulate Dark Liquidity by IIROC will still be open to industry input and comment. We believe that this next round of industry review and comment will have a greater beneficial impact to the Canadian marketplace if all available solutions and responses to marketplace risk are open to discussion. Otherwise, comments will merely consist of a debate as to the size of the threshold and how to calculate it, without any evidence to date that this will be the most effective way of establishing the controls necessary to reduce market or systemic risk in Canada.

As we provided in our response to the Position Paper, we continue to believe that establishing minimum size requirements to post Dark Orders could result in significant unintended consequences, some of which are detailed below.

- (i) **Risk of information leakage:** The minimum size threshold for posting limit orders increases the potential for participants trading actively in smaller size than the minimum posting amount (in particular, professional traders who seek to profit from information regarding large trading intentions) to become alerted to potentially large sized orders being resident in a Dark Pool. This could occur because those smaller size orders could be filled from the larger size minimum posting limit, which would indicate the existence of such minimum posted limit. Such information leakage could result in these participants trading ahead and moving prices against the large orders, reflected by the minimum posting limit. Where a minimum size threshold is not in play, the risk of such information leakage is reduced. We consider this to be the greatest risk in respect of establishing a minimum size threshold for accessing a Dark Pool.

- (ii) **Best execution:** Dark Pools are needed so that institutional investors in particular, have choice in executing their orders, and maintain anonymity, given their objectives and execution strategy. Limiting choice through prescriptive regulations would likely inhibit a money manager's ability to seek to obtain best execution.
- (iii) **Lower overall liquidity in the marketplace:** Due to the significant risk of information leakage from minimum size parameters, large orders will likely remain on the institutional trading desk without being exposed to the market in any shape or form for a longer period of time, which will not only increase trading costs related to the delay, but also reduce overall liquidity in the marketplace.
- (iv) **Reduced fills for retail orders in Dark Pools:** Due to the significant risk of information leakage from minimum size parameters, (as discussed in (i) above) Dark Orders will likely specify higher minimum fill requirements, which will cut opportunities out for smaller retail-type order flow from interacting with Dark Orders and achieving any potential price improvement.
- (v) **Liquidity migration to other jurisdictions:** Any new regulation related to Dark Liquidity should be considered in tandem with other international jurisdictions. If not, it may lead to the risk of regulatory arbitrage and liquidity migrating to other markets, especially in the case of inter-listed securities.

Investors and providers of Dark Pools and Dark Orders should have the unfettered ability to determine the minimum size parameters when optimizing execution strategies and positioning offerings to the marketplace, respectively. The structure of the market should be primarily driven by market forces based on the needs of market participants, and should not be limited prescriptively by regulation. Rather than imposing prescriptive regulations on Dark Pools and Dark Liquidity, regulations should focus on promoting greater confidence for large institutional players to transact in the visible markets by addressing broader market structure issues such as the lack of transparency around how marketplaces operate, the unlevel playing field for access to market data, and the lack of specific regulations/obligations for short-term professional traders that operate automated predatory strategies to determine institutional trading activity. These predatory strategies may not be adding any value to the marketplace.

Conclusion

We support regulations that are principles-based and provide flexibility where warranted. We agree with the CSA that implementing the framework for regulating Dark Pools as soon as possible is a prudent step to seek to reduce market and systemic risk in Canada. However, we believe that our suggested changes will make the Proposed Amendments more workable. We believe that additional research and industry review and comment is required prior to establishing a framework for regulating Dark Pools and Dark Orders which focuses solely on a minimum sized threshold. We propose that IIROC be given a broader mandate to regulate Dark Liquidity, such that all available responses to market and systemic risk may be open for review and industry comment, so that the Proposed Amendments to NI 21-101 do not need to be revisited once again to provide IIROC with this broader mandate at a later date.

We would be pleased to provide any further explanations or submissions with respect to matters described above and would make ourselves available for further discussion.

Yours truly,

A handwritten signature in blue ink, consisting of several loops and a long horizontal stroke extending to the right.

Craig Gaskin, CFA

Managing Director
Head of Trade Management