



July 28, 2011

By electronic delivery

Alberta Securities Commission
Autorité des marchés financières
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

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Re: National Instrument 23-103, Electronic Trading and Direct Electronic Access to Marketplaces

For your Consideration:

Alpha supports any initiative aimed at the proper management of risks which appears to be the focus of proposed NI 23-103, and we commend the CSA for reviewing the issues.

General Comments

Regulators should rely on principle- based requirements for risk management with close oversight review of how firms implement those principles. Proper risk management is very important to the financial services industry; however we question the statement that there are no current requirements to cover these risks. We believe that both IIROC and the securities regulators have the authority under current rules to do oversight of all issues relating to electronic trading.¹ In fact electronic trading has existed in Canada since the 1980s without any specific concerns being identified. We would encourage the CSA to rely on IIROC to use its oversight tools to monitor how dealers manage their risks in the area of client direct access as well as in other areas, rather than restricting how a dealer manages its business where there is no evidence of an issue or harm.²

The introduction of additional markers is useful for improving monitoring by the regulators. We do support the introduction of additional markers that would help IIROC or the securities regulators within the frame of their oversight roles, and allow for the collection of statistics and facts that would identify issues and support future regulatory initiatives where there is evidence of an issue or harm.

Marketplaces should strive to achieve fair and orderly markets; but must be allowed to have the tools to support this objective. Alpha has always believed that it is the role of a marketplace to put in place requirements, policies and procedures aimed at achieving market quality, which we believe includes fair and orderly trading. However, in order to be effective in achieving that goal, a marketplace must have the tools in place to not only monitor but to take action when it finds a problem. In addition, it is not inconsistent for marketplaces to promote market quality while IIROC or another RSP promotes and focuses on market integrity.

Specific Comments

1. Definition of Direct Electronic Access (DEA)

The definition of “direct electronic access” focuses on access to transmit orders without “re-entry or additional order management” by the dealer. We believe the focus should be on

¹ For example, IIROC uses an extensive Financial and Operational Risk Assessment Model that includes consideration of the firm's specific lines of business or financial products and has a risk control category regarding risk management and control. Section 7.1 of UMIRS includes supervisory responsibilities whether the order is entered by the firm or by its clients. Section 11.1 of NI 31-103 requires a registered firm to establish and maintain policies and procedures and a system of controls and supervision sufficient to “manage the risks associated with its business in accordance with prudent business practices.”

² We note no description has been provided of IIROC's current practices.

whether or not the dealer has any involvement in the order management, i.e. if there is any involvement it is not direct electronic access. The use of the language “re-entry or additional” may be confusing and apply to unintended activity.

2. The requirements focus on risk management and supervisory controls, policies and procedures

We support the CSA’s approach to focus on controls, policies and procedures; however, we believe the specific controls set out in section 3(3) are more appropriate as guidance rather than strict requirements applicable in all situations. Which controls are applicable should depend on the nature of the dealer’s customers and business, as well as its approach to risk.

We also question whether the requirement for dealers “to ensure that the entry of orders does not interfere with fair and orderly markets” is too broad. While dealers have historically acted as gatekeepers, they have not been required to “ensure”. This has been the role of IIROC. We believe the current IIROC requirements set out in Part 7 of UMIRS is sufficient to achieve the regulators’ objectives without creating any uncertainty around the roles of dealers.

3. Use of Automated Order System

The proposed rule includes not only the order systems of the dealer but also of its clients. It requires a dealer to have knowledge of the client’s order routing systems as well as to test or properly confirm that such testing be done. While Alpha agrees that the dealer must be held responsible for all orders routed to a marketplace under its firm ID, it questions whether it is practical or necessary for a dealer to be knowledgeable of its client’s systems. This should be one of the tools that a dealer has available to it to manage risks but it should be the dealer’s choice whether to use it or not.

4. Scope of DEA

A participant dealer may only provide access to another registrant if it is another participant dealer or a portfolio manager. This definition excludes Exempt Market Dealers, which includes a category of stakeholders which used to be known as international dealers. Historically DEA has been made available to sophisticated parties which have included foreign dealers. The reason for the proposal to limit the use of DEA was cited as regulatory arbitrage. In fact, there has been equivalent access to other jurisdictions through such rules as 15a-6 in the United States. We do not believe that regulatory arbitrage would occur.

The determination of who should be allowed to be provided with DEA is a risk-based issue which should depend upon the risk controls that the dealer puts in place.

If a limitation must be set, then we strongly recommend that the traditional definitions of sophisticated clients (both individual and corporate) should be included as part of the list of parties to whom DEA may be provided.

The proposed restriction would limit access from foreign participants and is likely to have material negative consequences.

5. Marketplace Requirements

- a. Access to order and trade information, DEA client identifiers, and the ability to terminate access

Alpha supports these requirements, which will allow dealers as well as marketplaces to monitor behaviour and take action based on who has access. This should include the ability to terminate access at both the firm and trader ID level.

- b. Assess and document any controls, policies and procedures to ensure fair and orderly trading

Alpha has always believed that it is the role of a marketplace to put in place requirements, policies and procedures aimed at achieving market quality, which we believe includes fair and orderly trading. However, in order to be effective in achieving that goal, a marketplace must have the tools in place to not only monitor but to take action when it finds a problem.

This type of action should be supported by its contractual rights with its customers if it is not an exchange, or by its regulatory authority if it is an exchange. All such exercises of its authority can and should be subject to oversight review by the regulators to confirm such actions do not prevent fair access or are not an abuse of regulatory and/or commercial authority. Alpha has set out in its policies the tools it will use. It has stated that it will, in the appropriate circumstances (as described in the policies): cancel orders or trades; set risk thresholds; and/or suspend or terminate a trader or subscriber from access to the system or a facility. This is consistent with what other marketplaces in other jurisdictions are permitted to do.

However, the regulators in Canada (including IIROC) have not permitted the marketplaces including the exchanges in Canada to use their discretion when employing available tools. See specific discussion below. If obligations are imposed, then tools must be permitted or the obligation becomes very difficult to fulfill.

- c. RSP or Exchange doing surveillance setting thresholds

Alpha's understanding is that the thresholds described in the rule are intended to replace the current price band parameters that most marketplaces have in place to prevent clearly erroneous trades, as well as to allow IIROC to implement circuit breaker measures.

We would urge the CSA to distinguish between price band parameters (a percentage change in prices that causes restrictions on order entry or trading to allow a marketplace to review what is happening) and circuit breakers. Price band parameters are used by marketplaces as risk control measures to prevent clearly erroneous trades or circumstances like runaway algorithms. Circuit breakers have been introduced to prevent a more systemic problem like a market meltdown by giving all participants a break in trading.

While Alpha supports the regulators having the authority to implement circuit breakers to maintain market integrity and confidence, it believes that price band parameters should be

left to the discretion of the marketplace who will be best informed as to the nature of the activity on its market and how the risk should be managed. We would also support a requirement that marketplaces make their price band parameters transparent so that users of those marketplaces understand the differences between the various marketplaces. This is an important tool in risk management that should be left to the marketplaces, if the regulators want them to “ensure fair and orderly” markets.

We are also concerned that the thresholds include limits on volumes. These controls should be in place at the dealer level via their order management systems. Price band parameters and circuit breakers typically focus on pricing issues (either there was an unintended material error or impact on the price of the security). It would be difficult to establish a common volume threshold for all types of clients and all types of securities, which is why this is more appropriately left with the dealer who has order entry responsibilities.

- d. Limits on marketplace having the ability to take action where there is a clearly erroneous trade

The current proposal strictly limits a marketplace's ability to correct a problem on its marketplace by only allowing it to make changes or cancel trades when instructed by IIROC, requested by both sides of the trade, and/or in the case of a system issue. It has been Alpha's experience that there are times when a quality of market issue occurs but IIROC is unwilling to take action because it does not believe there is a market integrity issue.

This proposal is also inconsistent with the obligation that the CSA would like to impose on marketplaces in terms of ensuring fair and orderly markets.

While we absolutely agree that market integrity issues should be left to IIROC for alternative trading systems, we do not believe it is in the best interest of the markets to take away a marketplace's ability to act. We do agree that any actions should be documented, transparent and subject to after the fact oversight.

We would also note that this approach is inconsistent with the approach taken in other jurisdictions, and unnecessarily interferes with the contractual rights that marketplaces have with their customers.

We appreciate the opportunity to express our views and would be happy to answer any questions.

Sincerely,



Randee Pavalow
Head of Operations and Legal