GLOBAL BANKING AND MARKETS

Scotiabank

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British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority (Saskatchewan)
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

c/o - by email

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Re: **CSA Notice and Request for Comment - Proposed Amendments to the Companion Policy to National Instrument 23-101 Trading Rules: Application of the Order Protection Rule to Marketplaces Imposing Systematic Order Processing Delays**

Dear Sirs/Mesdames,

Scotia Capital Inc. (“Scotiabank”) appreciates the opportunity to comment on the proposed amendments to National Instrument 23-101.

In previous comment letters we have raised concerns around the application of OPR to the proposed Alpha market (as well as Aequitas Neo for LST market participants) and the need to consider removing protected status from those markets. We appreciate the regulatory response to the issues raised by ourselves and others and generally feel that the proposals are a reasonable approach.

Questions

Question 1: What are your views on whether OPR should apply to marketplaces that impose an order processing delay? If OPR should apply to marketplaces that impose an order processing *delay, should it apply to some or all of them? What factors should be considered in determining whether OPR should apply to marketplaces that impose an order processing delay?*

We would differentiate between speedbumps applying to all orders and those on only a subset.

The Alpha speedbump, for example, is explicitly designed to allow liquidity providers to cancel their orders between the time other participants attempt to access the orders and when a trade would occur. A smart order router routing to all markets simultaneously could find that the order it expected to match with on Alpha was cancelled by the liquidity provider in response to the trade reports on the other marketplaces. Thus it makes sense to say that the order is not really accessible as the liquidity provider has an option to cancel it.

The Neo speedbump has a similar effect on Latency Sensitive Traders (LST) who may attempt to access offers which are either cancelled or lifted by other participants while the LST order is delayed by a speedbump.

This is in contrast to the speedbump used by the IEX market in the United States where all order instructions are delayed by an equal amount of time with a goal of delaying the market data coming out of the venue and making sure that mid-point based trades are priced appropriately. In this case messages are still processed in the order received and the Alpha issue of selectively fading liquidity does not exist. The speedbump is also very short (~350 microseconds). We do not think there is any issue with this type of market being protected.

In the event of longer speedbumps there are other potential problems. Consider a market with these ask prices:

Market A	Market B	Market C	Speedbump Market
1000@10.50	1000@10.50	1000@10.50	1000@10.50

Which then becomes:

Market A	Market B	Market C	Speedbump Market
1000@10.51	1000@10.51	1000@10.51	1000@10.50

In this case there is no reasonable expectation that the 10.50 ask on the Speedbump Market is accessible as it has very likely already been either lifted by the same buyer(s) as the other markets or cancelled by the liquidity provider. However it will complicate things for algos which want to bid at 10.50 on other markets or access the 10.51 offers. This is unavoidable to some extent as there will never be exactly the same latency between all markets and participants, but should not persist for an extended period of time.

The other question is what constitutes a systematic delay. Consider these options:

- Programmatic delays
- Slow trading engines
- Running orders through very long cables
- Forcing users to connect to a point-of presence far from the trading engine

These all have essentially the same effect and should be treated the same. Some Canadian marketplaces have been referred to as having “natural speedbumps” based on their slower order processing engines and this is viewed as a feature by users in some cases. We see it as problematic to use “intentional” in the definition as it allows marketplaces to achieve the same effect as long as they do not declare this as a feature.

Our suggestion would be that a protected market should be required to:

- Process all order messages on an equal basis (with some allowance for small technical variance where customers connect to separate order entry gateways)
- Process orders “immediately”, where immediately is considered to be within the latency of the slowest currently operating marketplaces

The first requirement would unprotect Aequitas Neo and Alpha. The second would currently have no effect, but could be used in the future.

Question 2: In an environment where not all displayed orders on visible marketplaces are protected under OPR because marketplaces impose an order processing delay, what are your views with respect to the outcomes for protected and unprotected visible marketplaces and for trading on those marketplaces? In responding, please consider the impacts on:

(a) various market participants including retail and institutional investors, and liquidity providers;

We do not foresee major impacts on most investors from the existence of unprotected marketplaces. They may see the occasional locked market or apparent trade through which will need to be explained, but the changes should generally be transparent.

(b) liquidity on both protected and unprotected visible marketplaces;

We do not expect the loss of protection to have significant impacts on existing marketplaces. It may (appropriately) make it more difficult to launch a new marketplace if it were to be launched as an unprotected market, as the operator would need to convince participants there is significant value to connect.

(c) price discovery;

We do not anticipate a significant impact on price discovery. We expect that the norm will still be for the protected markets to be on the NBBO and market locks, crosses, and trade-throughs caused by the unprotected markets to be relatively rare.

(d) complexities and changes you anticipate from participating in both protected and unprotected visible marketplaces, including costs and effort; and

We do not see significant changes being needed for dealing with both protected and unprotected markets. If it became common to have locked or crossed markets strategies might need to be re-evaluated to take this into account. We do not expect this outcome immediately.

The primary complication is for algorithms and smart order routers interacting with the proposed Alpha model. They may wish to treat Alpha differently from other marketplaces as there is significantly more risk of missing fills when the liquidity provider cancels their offering before a trade occurs. This may lead to dedicated trading strategies for dealing with the Alpha market as well as an adjustment of router evaluation metrics which may need to recognize that the Alpha quote may not be accessible.

This should be doable with existing systems and personnel, so the primary cost is the opportunity cost of vendors and Participant staff working on this rather than other initiatives. We remain of the view that the Alpha model seems to be an attempt to segment retail flow within existing regulations and it would be preferable for regulations to allow a model of segmenting this flow directly rather than adding needless complexity to the entire marketplace through the use of speedbumps or other mechanisms.

(e) the provision and use of consolidated data.

The various vendors providing consolidated market data sources may need to introduce a new feed including protected-only data. This involves some effort and increase in network and system load, but should be basically a duplication of existing systems.

Users of consolidated data should determine which feed is most appropriate for their purposes and may need small updates to use a different feed.

Question 3: A key objective of OPR is to recognize and support the role of retail participation in the market. If the Proposed Amendments are finalized, what changes if any, do you expect will be required for dealers handling retail order flow? What changes if any, do you expect in terms of outcomes for retail clients?

We don't expect dealers will need to make any specific changes for retail order flow beyond those already discussed. As the OPR regime will still apply to most trading the existence of a limited number of unprotected venues should have little impact on retail clients.

The overall outcome for retail clients in the near term will depend on whether the Alpha experiment is a success. If it does lead to liquidity providers posting significantly larger size than is currently available it should lead to an improvement in fill quality and lower fees on active orders, which would benefit retail clients while controlling broker execution costs. If the experiment does not succeed, then retail clients should see little impact.

Question 4: Are there implications that have not been addressed above that should be considered? How do you suggest they be addressed?

Not that we would raise at this time.

As always, we appreciate the opportunity to comment on these proposed changes and would be pleased to provide any more details if desired.

Sincerely,

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