Select Vantage

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Dear Sirs and Mesdames,

Re: CSA Staff Notice and Request for Comment 23-323 – *Trading Fee Rebate Pilot Study*

Thank you for this opportunity to submit a comment letter on the Pilot Study.

Select Vantage Canada Inc. and its parent company Select Vantage Inc. are significant contributors to liquidity on Canadian equity markets, particularly in junior-listed names. We are commercially indifferent to whether or not rebates are paid and in what manner they are paid - *i.e.*, whether paid on active order flow ("inverted" markets) or passive order flow. In Canada, we are typically significant fee payers, and not receivers of rebates. Internationally, we trade in numerous markets that do not offer rebates. Generally speaking, our traders are able to adapt to regulatory changes in market micro-structure.

However, we strongly believe in the value of consistent and predictable micro-market rules for all industry participants. "Live" experimentation of the type proposed in the Pilot Study should not be undertaken unless there is a compelling reason for such a regulatory intervention. We know of no other industry where regulators have so dramatically intervened in how vendors price their products solely to analyze whether or not further regulations on pricing should be imposed. This proposal appears to be driven by the desire to pre-empt the Americans in their own pilot study so that Canadian academics can debate further intervention in our equity markets. We note that some American equities market incentives (for example, rebates or discounts contingent on tiered volume traded) simply do not exist in Canada, and so we question why we are concerning ourselves with a made-in-America policy study.

If the end-goal of this study is to consider the permanent limitation or banning of rebates in transaction pricing, what other features will marketplaces be expected to compete over? Will it be on speed of connectivity, which favours the fastest?

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We see several reasons why this study's dramatic intervention in market pricing is ill advised:

1. *CSA should first consider less intrusive means of studying the issues raised.* In co-ordination with IIROC, the CSA currently has the authority to audit the routing practices of dealers and best execution policies that address how routing decisions are made. Has this been attempted through a sample review of dealers' routing practices? Why suspend operation of rebates across hundreds of stocks when there is a less intrusive means of studying potential conflict?

2. *Has any historical data been analysed in a similar fashion*? Given the robust competition between marketplaces, differing rebate structures – particularly, inverting the maker-taker model to pay for "active" orders – have been introduced over discrete periods of time. Through IIROC, the CSA has access to all Canadian historical equities trading data. If the study anticipates seeing statistically significant changes in trading patterns, then a review of historical trade data should likewise uncover statistically significant changes following changes in respective marketplaces' rebate structures. Has such a study been attempted?

3. *Effect of dealer pricing.* Some dealer firms charge institutional clients using a "cost-plus" model rather than an "all-in pricing" model. Cost-plus pricing passes on to the client all rebates earned on the particular client's trades, thereby limiting the incentive of a self-interested dealer to route to venues to maximize rebates for the firm at the expense of best execution for the client. We see no mention of this factor in the pilot study. Has the CSA determined roughly what percentage of Canadian client order flow is charged on such a cost-plus model? The greater the proportion of stock volume traded under a cost-plus model of pricing, the less analytical value this study will have. From a policy perspective, how is it fair to deny institutional clients market payment for providing liquidity so academics can study the impact of a rebate suspension on the entire industry?

4. *Venue ownership.* A potentially greater source of conflict arises in situations where dealers are material shareholders in venues they route client orders to – in other words, a dealer receives an indirect economic benefit with every order executed on that dealer's own marketplace. This Pilot Study appears to do nothing to measure this potential conflict (whereas the form of study suggested in #1 above would).

5. *Other incentives for order flow.* Every stock exchange and ATS engages in marketing targeted at convincing dealers to use their competing services. What is the impact of such benefits on routing choices? Again, this study will do nothing to examine this potential conflict (whereas the form of study suggested in #1 above would).

6. *ETF market-making (response to Questions #3 and #7 of the Pilot Study Request for Comment).* In selecting stocks for participation in the rebate suspension, consideration should be given to exclude stocks that form part of exchange-traded funds. Speed of execution is imperative to ETF market makers when assembling ETF units by purchasing the relevant proportions of underlying stocks, and so the benefit of earning a rebate on such stocks will be a very low, or even non-existent, incentive for them when purchasing such stocks. Therefore, such market making in stocks contained within ETF units will dilute the analytical value of examining the effect of a rebate suspension. Conversely, we do not believe that temporarily suspending other marketplace incentives provided to ETF market makers to create such units is the answer as this will simply involve even more intrusion into market forces responsible for creating ETF investment products relied on by many investors.

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Sincerely,

Daniel Schlaepfer
President

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Vice President, Regulatory Affairs and General Counsel