

# IIROC NOTICE

**Rules Notice**  
**Request for Comments**  
UMIR

*Please distribute internally to:*  
Legal and Compliance  
Trading

*Contact:*

Sonali GuptaBhaya  
Senior Policy Counsel, Market Regulation Policy  
Telephone: 416.646.7272  
Fax: 416.646.7265  
e-mail: [sguptabhaya@iiroc.ca](mailto:sguptabhaya@iiroc.ca)

**15-0023**  
**January 29, 2015**

## **Re-Publication of Proposed Dark Rules Anti-Avoidance Provision**

### **Executive Summary**

IIROC is proposing amendments (“Proposed Amendments”) to the Order Exposure Rule<sup>1</sup> that would limit the ability of a Participant to execute a client order of 50 standard trading units or less (a “small client order”) on a foreign organized regulated market (“FORM”) unless the order is entered on a market that displays order information (and the order is either displayed or executed on entry) or executed at a “better price”<sup>2</sup> (“Proposed Anti-Avoidance Provision”).

The purpose of the Proposed Anti-Avoidance Provision is to further the policy objective of pre-trade transparency supported by the Order Exposure Rule and achieve consistency in the application of the requirement to obtain a “better price” under the Canadian dark liquidity framework. We think that price improvement of anything less than what would constitute a “better price” is not sufficiently meaningful to deny the Canadian market the benefit of transparency. The Proposed Anti-Avoidance Provision would help ensure that small client orders that contribute to Canadian price discovery are not by-passed by orders routed to a

---

<sup>1</sup> UMIR 6.3

<sup>2</sup> A “better price” is defined in UMIR as price improvement of at least one trading increment except when the difference between the best ask price and the best bid price is a single trading increment, then price improvement of at least a half-increment.



foreign jurisdiction that can step ahead of the Canadian posted orders by an amount that would not be sufficient in Canada.

The Order Exposure Rule and the requirement to obtain a “better price” work together to help maintain the quality of Canadian price discovery and in turn help maintain the competitiveness of our equity markets. This re-publication<sup>3</sup> is intended to foster public debate regarding the best approach to balance the effects that an increase in order routing by certain Participants to U.S. markets would have on the health of our markets as a whole.

The Proposed Anti-Avoidance Provision would apply to small client orders originating from all accounts, irrespective of the residency of the account holder, the currency in which the account is denominated, or the type of account (i.e. retail or institutional).

If implemented, the Proposed Anti-Avoidance Provision may require certain Participants to make changes to their systems used to route small client orders. Participants would also be expected to revise their policies and procedures to ensure that small client orders that are routed to a FORM would be exposed for display or executed at a “better price”.

If approved, the Proposed Amendments would become effective approximately 90 days after publication of the notice of approval.

---

<sup>3</sup> The Proposed Anti-Avoidance Provision was included with certain other proposed amendments to UMIR related to the execution and reporting of “off-marketplace” trades that were published for comment on April 13, 2012 (“2012 Proposed Amendments”). See IIROC Notice [12-0131](#) – *Provisions Respecting the Execution and Reporting of Certain “Off-Marketplace” Trades* (April 13, 2012).



## Rules Notice – Table of Contents

1.	POLICY DEVELOPMENT PROCESS .....	4
2.	BACKGROUND TO THE PROPOSED AMENDMENTS .....	5
2.1	“ORDER EXPOSURE” REQUIREMENTS IN CANADA .....	5
2.2	“BETTER PRICE” REQUIREMENTS IN CANADA AND EXECUTING ON FORMS .....	5
3.	PURPOSE OF THE PROPOSED AMENDMENTS .....	6
4.	PREVIOUS PUBLICATION OF PROPOSED AMENDMENTS.....	7
4.1	COMMENTERS’ CONCERNS REGARDING PROPOSED ANTI-AVOIDANCE PROVISION AND IIROC RESPONSES .....	7
5.	DISCUSSION OF PROPOSED AMENDMENTS.....	11
5.1	PROPOSED ANTI-AVOIDANCE PROVISION .....	11
5.1.1	Consideration of Canadian Non-Transparent Marketplaces.....	12
5.1.2	Executing with Dark Orders on a Transparent FORM .....	12
5.1.3	Execution of Crosses on a FORM .....	12
5.1.4	“Better Price” Determination .....	12
5.2	EDITORIAL AND CONSEQUENTIAL AMENDMENTS .....	13
6.	ALTERNATIVES CONSIDERED .....	13
6.1	REVISE DEFINITION OF FORM .....	13
6.2	MAINTAIN STATUS QUO.....	14
7.	SUMMARY OF THE IMPACT OF THE PROPOSED AMENDMENTS.....	14
8.	TECHNOLOGICAL IMPLICATIONS AND IMPLEMENTATION PLAN.....	14
9.	QUESTIONS.....	15
10.	APPENDICES .....	15
	APPENDIX “A” .....	16
	APPENDIX “B”.....	17
	APPENDIX “C”.....	18



## 1. Policy Development Process

The Market Rules Advisory Committee (“MRAC”) of IIROC considered this matter.<sup>4</sup> MRAC is an advisory committee comprised of representatives of each of the marketplaces for which IIROC acts as a regulation services provider, Participants, institutional investors and subscribers, and the legal and compliance community.

The Board of Directors of IIROC (“Board”) has determined the Proposed Amendments to be in the public interest.

Comments are requested on all aspects of the Proposed Amendments, including any matter which they do not specifically address. Comments on the Proposed Amendments should be in writing and delivered by **March 30, 2015** to:

Sonali GuptaBhaya  
Senior Policy Counsel, Market Regulation Policy,  
Investment Industry Regulatory Organization of Canada,  
Suite 2000,  
121 King Street West,  
Toronto, Ontario. M5H 3T9  
Fax: 416.646.7265  
e-mail: [sguptabhaya@iiroc.ca](mailto:sguptabhaya@iiroc.ca)

A copy should also be provided to the Recognizing Regulators<sup>5</sup> by forwarding a copy to:

Susan Greenglass  
Director, Market Regulation  
Ontario Securities Commission  
Suite 1903, Box 55,  
20 Queen Street West  
Toronto, Ontario. M5H 3S8  
Fax: (416) 595-8940  
e-mail: [marketregulation@osc.gov.on.ca](mailto:marketregulation@osc.gov.on.ca)

***Commenters should be aware that a copy of their comment letter will be made publicly available on the IIROC website ([www.iiroc.ca](http://www.iiroc.ca)).***

---

<sup>4</sup> Consideration by MRAC should not be construed as approval or endorsement of the Proposed Anti-Avoidance Provision. Members of MRAC are expected to provide their personal advice on topics and that advice may not represent the views of their respective organizations as expressed during the public comment process.

<sup>5</sup> IIROC has been recognized as a self-regulatory organization by each of the Canadian provincial securities regulatory authorities (the “Recognizing Regulators”).



After considering the comments on the Proposed Amendments received in response to this Request for Comments together with any comments of the Recognizing Regulators, IIROC may recommend that revisions be made to the Proposed Amendments. If the revisions are of a non-material nature, the Board has authorized the President to approve the revisions on behalf of IIROC and the Proposed Amendments as revised will be subject to approval by the Recognizing Regulators. If the revisions are material, the Proposed Amendments as revised will be submitted to the Board for ratification and, if ratified, will be republished for further public comment.

## **2. Background to the Proposed Amendments**

### **2.1 “Order Exposure” Requirements in Canada**

The Order Exposure Rule requires a Participant to immediately enter a client order for 50 standard trading units<sup>6</sup> or less on a marketplace that displays order information. The reference to “50 standard trading units or less” of a security pertains to the size of the order that is received by a Participant. Child orders derived from a parent order that is greater than 50 standard trading units would not fall within the requirements of the Order Exposure Rule.

The policy objective of the Order Exposure Rule is to strengthen public price discovery by adding liquidity in the displayed markets. UMIR and securities legislation then seeks to protect such orders from trade-throughs. In particular, Part 6 of National Instrument 23-101 (“Order Protection Rule”) protects displayed orders, including small client orders that have been displayed in accordance with the Order Exposure Rule.

### **2.2 “Better Price” Requirements in Canada and Executing on FORMs**

There are exceptions to the Order Exposure Rule.<sup>7</sup> For example, a Participant may withhold a small client order from immediate entry on a displayed marketplace if the order is executed at a “better price”.<sup>8</sup> In 2012, UMIR 6.6 - *Provision of Price Improvement by a Dark Order* was implemented as part of a dark liquidity framework, which amended the definition of “better

---

<sup>6</sup> For the purposes of UMIR, 50 standard trading units represents: 5,000 shares of a security with a price of \$1.00 or more; 25,000 shares of a security with a price of at least \$0.10 and less than \$1.00; and 50,000 shares of a security with a price of less than \$0.10.

<sup>7</sup> Permitted exceptions in UMIR 6.3 include:

- (a) if the client has specified different instructions;
- (b) if the order is executed immediately at a better price;
- (c) if the order is returned for the terms of the order to be confirmed;
- (d) if the order is withheld pending confirmation that the order complies with applicable securities requirements;
- (e) if entering the order based on market conditions would not be in the interests of the client;
- (f) if the order has a value greater than \$100,000;
- (g) if the order part of a trade to be made in accordance with UMIR 6.4 by means other than entry on a marketplace; or
- (h) if the client has directed or consented that the order be entered on a marketplace as a Call Market Order, an Opening Order, a Special Terms Order, a Volume-Weighted Average Price Order, a Market-on-Close Order, a Basis Order or a Closing Price Order.

<sup>8</sup> UMIR 6.3(1)(b).



price”.<sup>9</sup> Under UMIR 6.6, when executing against an order for 50 standard trading units or less or an order for \$100,000 or less, a dark order<sup>10</sup> cannot trade ahead of an order displayed at the best price unless the dark order improves the displayed order price by at least one trading increment (or at least half a trading increment for securities with a bid-ask spread of one trading increment).<sup>11</sup> Together, the Order Exposure Rule and dark liquidity framework support pre-trade price discovery and the overall quality of the Canadian market.

Another exception to the Order Exposure Rule<sup>12</sup> allows a Participant to withhold a small client order from immediate entry on a displayed marketplace if the order is executed on a FORM.<sup>13</sup> The theory underpinning this exception is that, for securities inter-listed between exchanges in Canada and the United States, arbitrage activities between transparent markets will generally keep prices “in line” and that the best execution obligations of a Participant would require it to “diligently pursue the execution of each client order on the most advantageous execution terms reasonably available under the circumstances”.<sup>14</sup>

This exception, however, raises concerns in that it effectively allows small client orders to be entered on a non-transparent FORM and be executed at a price inferior to that which would be required if executed against a dark order in Canada.<sup>15</sup>

### 3. Purpose of the Proposed Amendments

Without a parallel obligation on Participants, such as the Proposed Anti-Avoidance Provision, to receive price improvement at a “better price” when trading small client orders in non-transparent markets outside of Canada, the policy objectives of the Order Exposure Rule and the dark liquidity framework are not completely met and the price discovery mechanism and overall quality of the Canadian market could be negatively affected if Canadian dealers send retail order flow to a foreign market on a broad basis. We think that price improvement of anything less than what would constitute a “better price” is not sufficiently meaningful to deny the Canadian market the benefit of transparency. Therefore, the Proposed Amendments would require that a small client order receives a comparable level of price improvement whether it executes against a “dark order” in Canada or on a non-transparent FORM. IIROC is of the view that publishing the Proposed Anti-Avoidance Provision for comment is valuable to

---

<sup>9</sup> In addition to setting the minimum level of price improvement for small client orders trading with a dark order, the dark liquidity framework also included prioritizing the execution of visible orders over dark orders on the same marketplace at the same price and providing IIROC with the ability to designate a minimum size for dark orders.

<sup>10</sup> A dark order, as defined in UMIR, is an order for which no portion is displayed at the time of entry on a marketplace in a consolidated market display. Any order which is immediately executable on entry or which is a “specialty” type of order that may execute at a price outside the best bid price/best ask price spread is excluded from the definition of dark order.

<sup>11</sup> UMIR 6.6 (1)(a) - *Provision of Price Improvement by a Dark Order* provides that if a Participant or Access Person enters an order on a marketplace for the purchase or sale of a security, that order may execute with a dark order provided the order entered by the Participant or Access Person is executed at a better price.

<sup>12</sup> UMIR 6.3(1)(g).

<sup>13</sup> The term “foreign organized regulated market” is defined in UMIR. See also IIROC Notice [14-0293](#) – *Guidance on the Definition of “Foreign Organized Regulated Market”* (December 15, 2014).

<sup>14</sup> See UMIR 5.1 and in particular, Parts 3 and 4 of Policy 5.1.

<sup>15</sup> U.S. rules do not require a minimum level of price improvement for orders that trade against a dark order as is mandated in Canada.



stimulate public debate as to the best approach to achieve consistency in the application of the dark liquidity framework.

We have learned that certain Participants are now sending or intend to send retail orders for listed securities to be executed by U.S. broker-dealers (also referred to as wholesalers) typically away from the public markets through internalization or in proprietary non-transparent alternative trading systems with minimal price improvement. These Participants have explained that they send or are considering sending, their small client order flow to the U.S. because the costs associated with execution are lower and because the orders may be filled at a superior price (sometimes as little as 1/10<sup>th</sup> of a cent per share) than they would if executed on a displayed market in Canada.

We are concerned that if even a small percentage of retail order flow from large dealers is directed to U.S. broker-dealers and by-passes the Canadian market, this could negatively impact price discovery in Canada and in turn, the quality of our equity markets.

#### **4. Previous Publication of Proposed Amendments**

On April 13, 2012, the 2012 Proposed Amendments respecting the execution and reporting of certain “off-marketplace” trades and which included the Proposed Anti-Avoidance Provision, were published for comment.<sup>16</sup> Nine comment letters were received with the majority opposed to the Proposed Anti-Avoidance Provision.

IIROC did not finalize the Proposed Anti-Avoidance Provision after it was published for comment in 2012 given the belief that Participants were not actively sending significant retail order flow outside of Canada; however we did commit to monitor developments and re-consider the proposal if and when needed. In light of the developments in the routing practices of certain Participants to the U.S. and IIROC’s concerns about the potential negative impact of these practices on the Canadian market, we are re-publishing the Proposed Anti-Avoidance Provision to, among other things, seek feedback as to whether an anti-avoidance provision is more appropriate now in light of the growth in southbound order flow and its potential harm to Canadian market quality.

##### **4.1 Commenters’ Concerns Regarding Proposed Anti-Avoidance Provision and IIROC Responses**

In response to the 2012 Proposed Amendments, commenters cited a number of concerns with the Proposed Anti-Avoidance Provision. Commenters’ main concerns along with IIROC’s consideration of these concerns are summarized below. Please also see Appendix “C” for a more detailed summary of the comments received in response to the 2012 Proposed Amendments and IIROC’s responses.

---

<sup>16</sup> The 2012 Proposed Amendments also included proposed changes related to the reporting of certain “off-marketplace” trades as well as some editorial and consequential amendments. We are currently reviewing these aspects of the 2012 Proposed Amendments.



#### (a) Compromises Ability to Obtain Best Execution

Many commenters indicated that the Proposed Anti-Avoidance Provision would limit the venues on which investors can find liquidity and restrict a Participant's ability to find the best price, thereby impairing a Participant's ability to obtain best execution. Commenters were also concerned that the Proposed Anti-Avoidance Provision would significantly impact best execution for retail clients who are sensitive to factors other than price such as speed and certainty of execution.

*IIROC agrees that achieving best execution is an extremely important requirement for Participants to meet; however we also need to balance the effects that an increase in order flow to the U.S. would have on the health of our markets as a whole. The Order Exposure Rule was implemented to support price discovery. A goal of the Proposed Anti-Avoidance Provision is to ensure that small client orders that contribute to price discovery are not by-passed by orders in a foreign jurisdiction that can step ahead of the Canadian posted orders by an amount that would not be sufficient in Canada. These two responsibilities work together to help maintain the robustness of the Canadian transparent market and in turn help maintain the quality of our equity markets. We think that price improvement of anything less than what would constitute a "better price" is not sufficiently meaningful to deny the Canadian market the benefit of transparency, and that ensuring small client orders receive a comparable level of price improvement whether executed with a dark order in Canada or on a FORM with no pre-trade transparency is one way for Canadian investors to continue to have a strong market in Canada in which to transact.*

#### (b) Complications for Third-Party Foreign Dealers

Commenters noted that when sending a client order to the U.S., control of this order is in the hands of a third party and the Participant is not aware if the order is executed on a non-transparent or transparent market. As well, concerns were raised that Participants would have to require foreign service providers to comply with Canadian regulatory standards and that business with these foreign service providers would have to cease if Canadian firms could not obtain an indemnity from these third-party firms.

*The intention is that the Participant would determine at the time of its routing decision whether it would be able to obtain a "better price" by sending a small client order to a FORM. Therefore, a Participant may send an order to a foreign service provider with a specific limit price that would ensure that if the order is executed, it would be at a "better price" as measured at the time the order was sent by the Participant. This approach may reduce certain complications for foreign dealers.*

#### (c) Technology Changes and Increased Costs

A number of commenters disagreed with the assertion that there are no technological implications of the Proposed Anti-Avoidance Provision. Certain commenters indicated that new algorithms would need to be created, routers would need to be modified, manual processes and the centralization of certain systems and supervisory structures would be needed in order to comply with the Proposed Anti-Avoidance Provision. As well, certain





commenters indicated that requiring foreign service providers to undertake special procedures when executing trades from Canadian firms would significantly add to costs as Canadian firms would have to absorb these technical and operational costs.

*We note that Participants are not required to access FORMs and no changes are needed unless the Participant chooses to send small client orders that are subject to the Order Exposure Rule to FORMs. For these Participants, we acknowledge that changes related to routing practices would likely need to be made. We believe that this would be a proportionate cost for those Participants, relative to the potential harm to the Canadian market that could occur as a result of this activity.*

#### (d) Unfair to Canadian Investors

Some commenters stated the proposed provision would provide preferential access to professional traders and high frequency traders to U.S. non-transparent markets over small client orders. Specifically it was noted that a professional trader or high frequency trader could trade with a small client order in a worse-priced displayed market in Canada and then immediately cover its position in the U.S. non-transparent market and collect the price improvement which would have otherwise been paid to the Canadian client.

Some commenters also were of the view that the Proposed Anti-Avoidance Provision would harm mostly retail Canadian investors since placing smaller orders on Canadian lit markets would expose these orders to opportunistic or short duration order flow which is inconsistent with best execution because this will force investors to interact with more non-natural liquidity.

*An objective of the Proposed Anti-Avoidance Provision is to ensure that the requirements put in place under the dark liquidity framework and the Order Exposure Rule are consistently applied so that the policy objectives of both requirements are appropriately met. Therefore, we continue to believe that it is appropriate to limit the Proposed Anti-Avoidance Provision to small client orders. As well, our understanding is that some of the order flow sent to the U.S. is internalized by U.S. broker-dealers, which could also be categorized as non-natural liquidity.*

#### (e) Unfair to Participants

A commenter was of the view that, despite implementation of the Proposed Anti-Avoidance Provision, small client order flow would still be sent to the U.S. because Canadian clients and non-Participants would deal directly with U.S. broker-dealers to avoid excessive transaction costs in the Canadian market and this would disadvantage Participants.

*It is our understanding that while some Participants pass along marketplace transaction costs to their clients, many do not. Under such circumstances, there would seem to be little incentive for a client to deal directly with a U.S. broker-dealer to avoid Canadian marketplace fees when these costs are not currently borne by the client.*

#### (f) Difficulty in Enforcing Proposal

A commenter pointed out that it would be difficult to enforce the Proposed Anti-Avoidance Provision due to the documentation required to accurately record specific execution venues and foreign exchange rates for each fill on each order as well as the Canadian best bid or offer



(“CBBO”) at the time of routing. This commenter also noted that it would be necessary to review on a fill-by-fill currency-adjusted basis whether fills from non-transparent venues provided sufficient price improvement. Another difficulty with complying with the proposed provision is that there has been great variation in the method and reliability of execution venue reporting by various U.S. broker-dealers.

*IIROC’s intention is that compliance with the proposed provision would turn on the information the Participant used at the time of the routing decision rather than solely looking at the actual execution price obtained. See section 5.1.4 “Better Price” Determination for further detail.*

#### (g) Inclusion of Non-Canadian and Foreign Currency Denominated Accounts

Almost all commenters favoured only applying the Proposed Anti-Avoidance Provision to orders from Canadian accounts denominated in Canadian currency. Some commenters were of the view that applying the proposed provision to orders from foreign accounts would put Participants at a competitive disadvantage because non-Canadian accounts can deal with brokers in their local jurisdiction that would be able to trade on non-Canadian venues, lit or dark. Another commenter explained that it is not practical to require orders for a Canadian account denominated in a foreign currency to achieve a “better price” versus the CBBO for non-transparent venue fills.

*IIROC’s proposal is to maintain the original scope of the application of the Proposed Anti-Avoidance Provision which would extend to non-Canadian accounts and to accounts denominated in a foreign currency. We acknowledge the comments received; however we believe that it is important to apply the policy on a consistent basis to ensure that the policy objectives of the Order Exposure Rule and the dark liquidity framework are achieved.*

*We think that not including foreign currency denominated accounts could create an arbitrary distinction.*

## **4.2 Suggested Alternatives to Proposed Anti-Avoidance Provision and IIROC Responses**

Commenters suggested a variety of alternatives to the proposed provision including addressing high marketplace trading fees, using an informed blanket consent and applying principles-based best execution guidelines.

#### (a) Address high fees

A few commenters suggested that a better way to address the migration of Canadian order flow to the U.S. is to address the root cause of the behaviour – high transaction costs.

*We note that in response to dealers’ complaints regarding high trading fees in Canada, the Canadian Securities Administrators (“CSA”) have proposed changes that would cap active trading fees charged by marketplaces. The CSA have also proposed to conduct a pilot study on the effects of the removal of payment of rebates by marketplaces. While these steps may address active trading costs in Canada, we are concerned that action on fees alone may not sufficiently stem the increase in order flow of Canadian securities being sent to the U.S.*



*We question whether the root cause of U.S.-bound order flow is solely related to high transaction costs because currently there are multiple marketplaces with inverted maker-taker fee models that are available for Participants to use to counter high active trading fees but these marketplaces are not often employed. We understand that migration of Canadian order flow to the U.S. may in part be related to the willingness of U.S. wholesalers to execute against retail client flow for fractional price improvement, in many cases for free or with payment for order flow. While we believe that the catalyst for sending order flow to the U.S. is dealer economics, it may be simplistic to conclude that marketplace fees alone are driving this behaviour.*

(b) Informed Blanket Consent

One commenter suggested that a provision be added to permit clients to provide a blanket consent to having their orders executed on non-transparent foreign markets with the understanding that Canadian requirements respecting “better price” would not apply to those orders.

*In our view a blanket consent would not be appropriate. The proposal is intended to maintain consistency with the policy objectives of the dark liquidity framework and blanket consents would result in circumventing these objectives. The structure of the Order Exposure Rule allows the client to instruct, on an order-by-order basis, that an order may be withheld rather than immediately displayed. In accordance with clause (a) of the Order Exposure Rule and Policy 6.3, a Participant is able to act on the specific instructions of the client so long as the Participant does not solicit the instruction.*

(c) Apply principles-based best execution guidelines

Another commenter noted that an alternative to the proposed provision would be to apply principles-based best execution guidelines versus setting a notional minimum price improvement threshold.

*The purpose of the Proposed Anti-Avoidance Provision is to maintain consistency with the policy objectives of the dark liquidity framework. This proposal does not change best execution obligations which remains a principles-based rule.*

## **5. Discussion of Proposed Amendments**

### **5.1 Proposed Anti-Avoidance Provision**

As mentioned above, the Proposed Anti-Avoidance Provision would limit the ability of a client order for 50 standard trading units or less to be executed on a FORM unless the order had been entered on a market that displays order information (and the order is either displayed or executed on entry) or executed at a better price. The Proposed Anti-Avoidance Provision would mean that a Participant may send a small client order to be traded on a non-transparent FORM provided that the execution price was at a “better price” for the client relative to the CBBO taking into account the currency exchange rate. We note that the Proposed Anti-Avoidance Provision would apply to small client orders originating from all



accounts, irrespective of the residency of the account holder, the currency in which the account is denominated, or the type of account (i.e. retail or institutional).

In addition to the concerns cited above, certain commenters requested clarification on the application of the Proposed Anti-Avoidance Provision. We address these clarification requests below.

### **5.1.1 Consideration of Canadian Non-Transparent Marketplaces**

The Proposed Anti-Avoidance Provision would not require a Participant to route to a non-transparent marketplace in Canada before accessing a FORM. However, we note that Part 2 of Policy 5.1 sets out factors related to the consideration of non-transparent marketplaces in the context of “best execution”. These factors include whether the displayed volume in the consolidated market display is not adequate to fully execute the client order on advantageous terms for the client and whether the non-transparent marketplace has demonstrated that there is a reasonable likelihood that the marketplace will have liquidity for the specific security.

### **5.1.2 Executing with Dark Orders on a Transparent FORM**

Once an order is entered on a FORM that publicly displays and provides timely information on orders, there would be no restriction on the execution of that order. The entry of the order on a FORM that is a lit market, would meet the requirement in the Proposed Anti-Avoidance Provision. Thus, the order could execute with a dark order posted within the lit book of a FORM at any price. The requirements in proposed UMIR 6.3(1)(g)(i) would be met if an order is entered on a transparent FORM and the order is executed on entry or displayed on that FORM. Proposed UMIR 6.3(1)(g)(i) would not impose a requirement to obtain a “better price” if the order is sent to a transparent FORM but executes with a dark order on that lit market. We are of the view that if a small client order is sent to a transparent FORM for execution or display then the policy objectives of the dark liquidity framework and Order Exposure Rule are adequately met.

### **5.1.3 Execution of Crosses on a Transparent FORM**

A Participant that sends a small client order to a U.S. broker-dealer that matches two orders and then executes these orders as a cross on a transparent FORM would not be in compliance with the Proposed Anti-Avoidance Provision. UMIR 6.3(1)(g)(i) is meant to be applied so that an order sent to a transparent FORM interacts with the liquidity resting on the transparent FORM and is therefore executed on entry or is displayed. Since the two orders comprising a cross would not be able to execute with the resting liquidity of the FORM, we would consider that the entry of a cross would not meet the requirements of UMIR 6.3(1)(g)(i).

### **5.1.4 “Better Price” Determination**

IIROC recognizes the challenges firms face in executing orders at a “better price” in a foreign market due to quickly fluctuating prices and exchange rates. Therefore, the test for compliance with the Proposed Anti-Avoidance Provision would occur at the time of the



Participant's routing decision rather than by examining the results of the actual execution. Upon comparing the price of a security in a foreign jurisdiction and in Canada and determining that the currency-adjusted fill would be at a "better price" to the CBBO if executed in the foreign jurisdiction, a Participant would be able to send the order to be executed on a non-transparent FORM. We would expect that the Participant would maintain an appropriate audit trail of relevant prices and exchange rates so that the "better price" determination can be adequately evaluated as to whether it was reasonable for the Participant to conclude it would be able to obtain a "better price" when routing to a FORM.

## **5.2 Editorial and Consequential Amendments**

The Proposed Amendments would also make the following consequential changes to Part 6 of Policy 6.4 of UMIR:

- apply the provisions dealing with foreign currency translation to the requirements in 6.3(1)(g)(ii) of the Order Exposure Rule to determine if certain orders executed on a FORM received a "better-price";
- delete the sentence "The Market Regulator regards a difference of one trading increment or less as "marginal" because the difference would be attributable to currency conversion."

The proposed change to apply the provisions dealing with foreign currency translation to the requirements in 6.3(1)(g)(ii) is identical to that included in the 2012 Proposed Amendments. We have proposed this change so that Participants use a consistent exchange rate when conducting foreign exchange conversion.

The sentence in Part 6 of Policy 6.4 referring to the difference of one trading increment as "marginal" was part of the former Best Price Obligation and had been carried over with consequential changes related to the implementation of the Order Protection Rule. Given current market structure, IIROC is of the view that this provision is no longer relevant and proposes that it be deleted.

## **6. Alternatives Considered**

In addition to the alternative approaches to the 2012 Proposed Amendments as suggested by commenters, we also considered a couple of other alternatives. Descriptions of these alternatives and our consideration of them are below.

### **6.1 Revise definition of FORM**

We looked at the possibility of revising the definition of FORM to address our concerns regarding order flow being sent to the U.S. Specifically, we studied whether the definition could be altered so that, in addition to the current criteria, a FORM would only encompass markets that provide pre-trade transparency. While this alternative would further the policy objective of supporting pre-trade price discovery, it would completely prevent Participants from sending small client orders to foreign non-transparent markets. We ultimately rejected this approach as we think the consequences of this change would be overly restrictive.



## **6.2 Maintain Status Quo**

Another alternative that we contemplated was the option of taking no regulatory action other than to continue to monitor developments in this area. While this alternative has the benefit of not imposing any changes for Participants to implement, we concluded that this was not a viable alternative as it would neither further the policy objectives of the Order Exposure Rule and the dark liquidity framework nor actively address the possible negative impact on Canadian markets if Participants send significant small client order flow to a foreign market.

## **7. Summary of the Impact of the Proposed Amendments**

The most significant impact of the Proposed Anti-Avoidance Provision is that it would limit Participants to execute small client orders on a FORM unless the order had been entered on a market that displays order information (and the order is either displayed or executed on entry) or executed a “better price”.

In complying with the Proposed Anti-Avoidance Provision, a Participant would:

- not be required to apply the proposed provision if the order received from the client is greater than 50 standard trading units,
- not be required to obtain a “better price” if an order is entered on a FORM which publicly displays and provides timely information on orders but executes with a dark order on that FORM,
- be required to apply the proposed provision to orders from both Canadian and non-Canadian accounts, including accounts denominated in a foreign currency,
- be able to make the determination of “better price” at the time of its routing decision; and
- still be able to, in accordance with clause (a) of the Order Exposure Rule and Policy 6.3, act on the specific instructions of its client so long as the Participant does not solicit the instruction.

## **8. Technological Implications and Implementation Plan**

Commenters to the 2012 Proposed Amendments indicated that the Proposed Anti-Avoidance Provision could require technology changes such as the creation of new algorithms, centralization of certain systems and new tags to pass on required information to U.S. executing broker-dealers. We also note that Participants would be expected to revise their policies and procedures to ensure that small client orders that are routed to a FORM would be either entered for display or executed at a “better price”.

We are of the view that Participants are not required to access FORMs; however, if a Participant uses a business model in which it does access FORMs, IIROC believes that the costs of any required policy, procedure or technology changes would be proportionate to the harm that could ensue as a result of the inconsistent application of a policy that has been established to require the provision of meaningful price improvement by dark orders to small client orders.



IIROC would expect that, if the Proposed Amendments are approved by the Recognizing Regulators, the amendments would become effective approximately **90 days** after the date IIROC publishes the notice of approval. This would allow Participants to make any necessary technology changes and update their policies and procedures to ensure that small client orders routed to a FORM would be exposed for display or executed at a better price.

## **9. Questions**

While comment is requested on all aspects of the Proposed Amendments, comment is specifically requested on the following questions:

1. Are there alternative approaches which would ensure that the policy objectives of the Order Exposure Rule and the dark liquidity framework are achieved?
2. Are U.S. dollar denominated accounts, by their nature, distinct from other client accounts such that they should be permitted to trade in the U.S. without reference to the CBBO? If an exception to UMIR 6.3 existed for U.S. dollar denominated accounts, could the exception be exploited contrary to the principles espoused in the Order Exposure Rule?
3. Does the proposed implementation date of **90 days** following the publication of the notice of approval of the Proposed Amendments provide sufficient time to accommodate any development work that may be required to be performed by Participants?

## **10. Appendices**

- Appendix “A” sets out the text of the Proposed Amendments to UMIR respecting the Proposed Anti-Avoidance Provision;
- Appendix “B” contains the text of the relevant provisions of UMIR as they would read on the adoption of the Proposed Amendments; and
- Appendix “C” contains a summary of the comment letters received in response to the 2012 Proposed Amendments relating to the Proposed Anti-Avoidance Provision and IIROC’s response to those comments.<sup>17</sup>

---

<sup>17</sup> The other aspects of the 2012 Proposed Amendments are currently under review and will be dealt with separately.



## **Appendix “A”**

### **Provisions Respecting the Proposed Dark Rules Anti-Avoidance Provision**

Rule 6.3 of the Universal Market Integrity Rules is hereby amended by:

1. deleting clause (g) of subsection (1) and substituting the following:
  - (g) the order is part of a trade to be made in accordance with Rule 6.4 by means other than entry on a marketplace provided, if the order was executed on a foreign organized regulated market, the order was:
    - (i) entered on a market which publicly displays and provides timely information on orders and the order executed on entry or was displayed, or
    - (ii) executed at a better price;

Part 6 of Policy 6.4 to the Universal Market Integrity Rules is hereby amended by:

1. inserting the phrase “and, if applicable, whether the requirement in subclause (ii) of clause (g) of subsection (1) of Rule 6.3 to execute at a better price has been met” at the end of the first sentence;
2. deleting the sentence “The Market Regulator regards a difference of one trading increment or less as "marginal" because the difference would be attributable to currency conversion.”





**Appendix “B”**  
**Text of the Rules to Reflect Proposed Amendments Respecting**  
**the Dark Rules Anti-Avoidance Provision**

Text of Provisions Following Adoption of the Proposed Amendments	Text of Current Provisions Marked to Reflect Adoption of the Proposed Amendments
<p><b>6.3 Exposure of Client Orders</b></p> <p>(1) A Participant shall immediately enter for display on a marketplace that displays orders in accordance with Part 7 of the Marketplace Operation Instrument a client order to purchase or sell 50 standard trading units or less of a security unless:</p> <p>...</p> <p>(g) the order is part of a trade to be made in accordance with Rule 6.4 by means other than entry on a marketplace provided, if the order was executed on a foreign organized regulated market, the order was:</p> <p style="padding-left: 20px;">(i) entered on a market which publicly displays and provides timely information on orders, or</p> <p style="padding-left: 20px;">(ii) executed at a better price;</p> <p>....</p>	<p><b>6.3 Exposure of Client Orders</b></p> <p>(1) A Participant shall immediately enter for display on a marketplace that displays orders in accordance with Part 7 of the Marketplace Operation Instrument a client order to purchase or sell 50 standard trading units or less of a security unless:</p> <p>...</p> <p>(g) the order is part of a trade to be made in accordance with Rule 6.4 by means other than entry on a marketplace <u>provided, if the order was executed on a foreign organized regulated market, the order was:</u></p> <p style="padding-left: 20px;"><u>(i) entered on a market which publicly displays and provides timely information on orders and the order executed on entry or was displayed, or</u></p> <p style="padding-left: 20px;"><u>(ii) executed at a better price;</u></p> <p>....</p>
<p><b>Policy 6.4 Trades to be on a Marketplace</b></p> <p><b>Part 6 – Foreign Currency Translation</b></p> <p>(a) If a trade is to be executed on a foreign organized regulated market in a foreign currency, the foreign trade price shall be converted to Canadian dollars using the exchange rate the Participant would have applied in respect of a trade of similar size on a foreign organized regulated market in that foreign jurisdiction in order to determine whether the condition in subsection (3) of Rule 6.4 restricting avoidance of Part 6 of the Trading Rules has been met and, if applicable, whether the requirement in subclause (ii) of clause (g) of subsection (1) of Rule 6.3 to execute at a better price has been met. A Participant shall maintain with the record of the order the exchange rate used for the purpose of determining whether a better priced order existed on a marketplace and such information shall be provided to the Market Regulator upon request in such form and manner as may be reasonably required by the Market Regulator in accordance with subsection (3) of Rule 10.11.</p>	<p><b>Policy 6.4 Trades to be on a Marketplace</b></p> <p><b>Part 6 – Foreign Currency Translation</b></p> <p>(a) If a trade is to be executed on a foreign organized regulated market in a foreign currency, the foreign trade price shall be converted to Canadian dollars using the exchange rate the Participant would have applied in respect of a trade of similar size on a foreign organized regulated market in that foreign jurisdiction in order to determine whether the condition in subsection (3) of Rule 6.4 restricting avoidance of Part 6 of the Trading Rules has been met <u>and, if applicable, whether the requirement in subclause (ii) of clause (g) of subsection (1) of Rule 6.3 to execute at a better price has been met. The Market Regulator regards a difference of one trading increment or less as "marginal" because the difference would be attributable to currency conversion.</u> A Participant shall maintain with the record of the order the exchange rate used for the purpose of determining whether a better priced order existed on a marketplace and such information shall be provided to the Market Regulator upon request in such form and manner as may be reasonably required by the Market Regulator in accordance with subsection (3) of Rule 10.11.</p>



**Appendix “C”**  
**Comments Received in Response to**  
**IIROC Notice 12-0131 – Rules Notice - Request For Comments – UMIR**  
***Provisions Respecting the Execution and Reporting of Certain “Off-Marketplace” Trades***

On April 13, 2012, IIROC issued IIROC Notice 12-0131 requesting comments on *Provisions Respecting the Execution and Reporting of Certain “Off-Marketplace” Trades* (“2012 Proposed Amendments”). IIROC received comments on the 2012 Proposed Amendments from:

Canadian Security Traders Association, Inc. (“CSTA”)  
Investment Industry Association of Canada (“IIAC”)  
ITG Canada Corp. (“ITG”)  
RBC Dominion Securities Inc. (“RBC”)  
Scotia Capital Inc. (“Scotia”)  
TD Bank Group (“TD”)  
TD Securities (“TD Securities”)  
TriAct Canada Marketplace LP (“TriAct”)  
UBS Securities Canada (“UBS”)

A copy of the comment letters received in response to the 2012 Proposed Amendments is publicly available on the website of IIROC ([www.iiroc.ca](http://www.iiroc.ca)) under the heading “Policy” and sub-heading “Market Proposals/Comments”). The following table presents a summary of the comments received on the Proposed Anti-Avoidance Provision included in the 2012 Proposed Amendments together with IIROC’s responses to those comments. Column 1 of the table highlights the proposed changes to UMIR pertaining to the Proposed Anti-Avoidance Provision.

Please note that the other changes proposed in the 2012 Proposed Amendments are being addressed separately and are not part of this notice.



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
<p><b>6.3 Exposure of Client Orders</b></p> <p>(1) A Participant shall immediately enter for display on a marketplace that displays orders in accordance with Part 7 of the Marketplace Operation Instrument a client order to purchase or sell 50 standard trading units or less of a security unless:</p> <p>...</p> <p>(g) the order is part of a trade to be made in accordance with Rule 6.4 by means other than entry on a marketplace <u>provided, if the order was executed on a foreign organized regulated market, the order was:</u></p> <p>(i) <u>entered on a market which publicly displays and provides timely information on orders and the order executed on entry or was displayed, or</u></p> <p>(ii) <u>executed at a better price;</u></p> <p>.....</p>	<p><b>ITG</b> – Proposal will prevent Participants from accessing deeper liquidity in the U.S. and will result in worse execution prices for small orders originating in Canada.</p> <p>Believes that the proposed anti-avoidance rule contradicts the objective of UMIR by significantly limiting small orders access to better prices or liquidity on foreign dark markets.</p> <p><b>TD</b> – Canadian investors will lose access to the best priced U.S. liquidity.</p> <p><b>RBC</b> – Believes that the single-minded focus of ensuring “meaningful price improvement” will have significant unintended consequences that may erode overall client execution quality. Cites the case of retail clients who are sensitive to factors other than price (i.e. speed and certainty of execution).</p> <p><b>UBS</b> – restrictions on order routing to dark markets may cause traders to be more reluctant to expose their orders and their liquidity to other markets which may increase price volatility which may result in higher costs of trading and cause lower liquidity.</p> <hr/> <p><b>IIAC</b> – Concerned about the proposal to impose the “better price” requirement when executed on a non-transparent foreign organized regulated market as Canadian dealers would have to require foreign service providers to comply with Canadian regulatory standards. Would drive up cost of execution.</p> <p>Concerned that the provision would complicate the handling of orders for non-inter-listed securities.</p> <p><b>RBC and Scotia</b> – Believes that the implementation of an “anti-avoidance” provision would pose a significant challenge for Participants that trade through third-party unaffiliated broker-dealers when executing on foreign marketplaces (particularly as activity on dark marketplaces in the U.S. may account</p>	<p>IIROC agrees that achieving best execution is an important requirement for Participants to meet. One objective of IIROC’s market integrity rules is to foster fair, efficient and competitive capital markets across Canada. This means that we balance the interests of the two sides to every trade in the interest of a fair and orderly market. The Order Exposure Rule supports price discovery by requiring the display of small client orders. The goal of the Proposed Anti-Avoidance Provision is to ensure that these orders are not “bypassed” by orders in a foreign jurisdiction that can step ahead of the Canadian posted orders by an amount that would not be sufficient in Canada.</p> <hr/> <p>Our expectation is that the Participant would determine the “better price” prior to making the routing decision (i.e. the Participant would establish a limit price on the order that would ensure it is executed at a “better price”).</p> <p>We interpret the IIAC comment regarding non-interlisted securities to reflect a concern regarding securities that are not listed by a Canadian exchange. The Order Exposure Rule only applies in respect of listed securities and would therefore have no impact on the trading of foreign-exchange listed securities (unless such securities are inter-listed by a Canadian exchange).</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p>for upwards of 30% of executions).            May impose significant operational and administrative expense without any assurance that execution qualify for Canadian retail clients will be improved.</p>	
	<p><b>IIAC</b> – Where clients are informed about the differences in the price improvement rules, they should be permitted to instruct their firms to access foreign markets.  <b>TD</b> – Notes that a Direct Investing client who trades online has the option of selecting whether they wish to have their order transaction specifically on either the Canadian or the U.S. market. Concerned about the U.S. regulatory risk and best execution risk if this is restricted.</p>	<p>The Proposed Anti-Avoidance Provision has no effect in circumstances where the client has instructed or chosen the execution jurisdiction. The Proposed Anti-Avoidance Provision only relates to clause (g) of subsection (1) of the Order Exposure Rule. In accordance with UMIR 6.3(1)(a), a Participant is able to act on the specific instructions of the client when not exposing a small client order for display on a marketplace including instructions to execute an order outside of Canada. However, we note that when executing an order outside of Canada, the requirements of UMIR 6.4, including the exception in UMIR 6.4(2)(d) relating to the execution of a trade on a foreign organized regulated market, must still be met.</p>
	<p><b>ITG and IIAC</b> – The proposal will require technology changes such as the creation of new algorithms, centralization of certain systems and new tags to pass on required information to U.S. executing brokers.</p>	<p>The Proposed Anti-Avoidance Provision is intended to result in a consistent application of policy to reward pre-trade transparency, thereby maintaining the quality of our equity markets.            Participants are not required to access foreign organized regulated markets. However, if a Participant uses a business model that involves sending Canadian order flow to U.S. dealers, and has committed resources for this purpose, we acknowledge that changes to routing practices would need to occur. IIROC believes that the costs to change technology would be proportionate relative to the potential harm to the Canadian market that could occur as a result of significant client order flow migrating to the U.S.</p>
	<p><b>IIAC</b> – Believes that clients will move to foreign dealers so as to be able to buy and sell non-inter-listed securities or inter-listed securities that have greater liquidity in the foreign jurisdiction. May also discourage foreign firms from sending their order</p>	<p>If an order is immediately executable (and would not be booked), one would expect that the order would be routed to the marketplace or market that offered the best price (and if multiple marketplaces or markets offered that price) to the combination of markets with volume sufficient to provide</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p>flow to Canada as they would be required to reconfigure their routing requirements.</p>	<p>full execution.</p> <p>The Proposed Anti-Avoidance Provision would not apply to the handling of orders for securities which are not listed by a Canadian exchange.</p> <p>IIROC does not believe that the Proposed Anti-Avoidance Provision would have any effect on foreign firms that send orders for Canadian-listed securities to Canadian dealers for execution.</p>
	<p><b>ITG</b> – The proposal will require that dealers ensure small orders do not trade in non-Canadian dark markets unless the orders receive full tick price improvement on the Canadian NBBO after foreign currency exchange. Any dealer using third party algorithms and smart order routers will be extremely challenged. Believes that the result will be avoiding U.S. non-transparent markets for all orders because they will almost never receive the full price improvement. Dealers will choose to contain orders to Canadian markets which will result in captive flow trading “slightly worse than the U.S. NBBO”.</p> <p>U.S. brokers (handling orders from a Canadian broker) have a best execution obligation that will be unnecessarily encumbered if they are not allowed to access all available pools of liquidity in a reasonable manner.</p> <p>If a dealer routes an order on a U.S. lit market which has a slightly better price than the Canadian NBBO, why prohibit Canadian investors from interacting with a dark order on that venue at a better price? Risks moving institutional flow back to the “upstairs desk” where it is unattainable to retail clients and the trading mechanism is less transparent.</p>	<p>The proposal does not prohibit the interaction with a dark order on a lit venue. The condition in proposed subclause (1)(g)(i) of Rule 6.3 would be met if the order was entered on a market which publicly displays and provides information on orders and the order was executed on entry (with a lit or dark order) or was displayed.</p>
	<p><b>TD Securities</b> – Believes that it is unfair to restrict access to dark liquidity for client orders where the same restriction won’t exist in practice for professional traders or U.S.-based HFT firms.</p>	<p>An objective of the Proposed Anti-Avoidance Provision is to ensure that the requirements put in place under the dark liquidity framework and the Order Exposure Rule are consistently applied so that the policy objectives of both requirements are appropriately met. Therefore, we continue</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
		to think that it is appropriate to limit the Proposed Anti-Avoidance Provision to small client orders.
	<b>TD and TD Securities</b> – Concerned that small Canadian dealers may lose access to U.S. liquidity because they will have to end their relationships with U.S. partners who are unwilling or unable to restrict access to dark liquidity.	Compliance with the Proposed Anti-Avoidance Provision would require U.S. dealers to act in a way that respects the Canadian dealer’s “better price” requirement for its clients.
	<b>Scotia</b> – Could an order be traded in a U.S. non-transparent market at the U.S. NBBO provided the final result was a better price for the client than the Canadian NBBO taking into account the currency exchange rate?	As proposed, that would be permitted. “Better price” is measured solely in the context of the Canadian market.
	<b>Scotia, TD Securities and UBS</b> – What is the effect of dark orders integrated into the order book of a U.S. transparent market?	As proposed, there would be no restriction on the execution of the order on a transparent marketplace.
	<b>TD Securities</b> – Concerned that the proposal will eliminate the competitive influence the U.S. market has on Canadian fees by preventing U.S. dark markets being used as an alternative to Canadian marketplaces. U.S. dark liquidity “generally” provides price improvement and may provide size improvement.	We note that the Canadian Securities Administrators (CSA) are reviewing marketplace fees as part of the Order Protection Rule (OPR) review and have proposed regulatory action with respect to marketplace fees.
	<p><b>ITG and UBS</b> – Think that the proposal will force Canadian investors to interact with displayed venues which tend to have most of the opportunistic or short duration order flow which is inconsistent with best execution because this will force investors to interact with more non-natural order flow.</p> <p><b>TD</b> – Believes the proposal will lead to market arbitrage at the expense of Canadian investors. HFT or professional traders with access to U.S. dark liquidity may trade with a client order in the worse-priced displayed market and immediately cover their</p>	Comment is noted. Our understanding is that some of the small client order flow sent to the U.S. is being internalized by U.S. broker-dealers, which could also be categorized as non-natural order flow. We don’t believe that counterparty identity is typically a factor to be considered when trading as agent for retail clients.



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p>position in the U.S. dark market, collecting the price improvement which would have otherwise been paid to the Canadian client.</p> <p><b>UBS</b> – Removing an investor’s ability to exercise choice will limit market efficiency and potentially dampen the benefits of competition and innovation.</p> <p><b>RBC</b> – How is a Participant expected to, in real time, account for changes in foreign exchange rates that may impact the price at which the order is executed?</p>	<p></p> <p>The proposal does not affect the existing ability of an investor to exercise choice. The proposal as published merely provides that, in the absence of specific client instructions, an order would have to be either: (i) entered on a marketplace or a foreign organized regulated market that displays orders; or (ii) executed at a “better price”.</p> <p>Our expectation is that the Participant would determine the “better price” prior to making the routing decision (i.e. the Participant would establish a limit price on the order that would ensure it is executed at a “better price”). IIROC’s intention is that the “test” for compliance with the Proposed Anti-Avoidance Provision would be determined at the time of the routing decision rather than only examining the results of the actual execution. We would expect that the Participant would maintain an appropriate audit trail of relevant information so that the “better price” determination can be adequately evaluated as to whether it was reasonable for the Participant to conclude it would be able to obtain a “better price” when routing to a foreign organized regulated market.</p>
	<p><b>Scotia</b> – Concerned that it would be difficult to enforce proposal. The documentation showing adherence to the rule requires work to accurately record specific execution venue and foreign exchange rate for each file on each order as well as the CBBO at the time of routing.</p> <p>IIROC would need to look on a fill by fill currency adjusted basis as to whether fills from dark venues provided sufficient price improvement. Scotia has seen great variation in the method and reliability of execution venue reporting by various U.S. dealers, so expects that there will be significant analysis and integration work required.</p>	<p>We agree that a Participant that routes small client orders for Canadian-listed securities to U.S. dealers would need to develop policies and procedures that, among other things, would result in an audit trail sufficient for the Participant and Market Regulator to review for compliance purposes.</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p><b>TD Securities</b> – Believes that the proposals are protectionist in nature and restricts access to global liquidity while entrenching excessively high transaction costs for Canadians.</p> <p>Under OPR, a displayed price level must be cleared by an active order rather than locking the market, regardless of the take fee charged by the marketplace. Competitive forces cannot be relied on to lower take fees in the visible market. Without effective competition from dark liquidity, only regulatory action can place a limit on take fees.</p>	<p>We note that the CSA have proposed regulatory action with respect to marketplace fees. We also understand from industry representatives that the economics that drive dealer routing decisions are not limited to marketplace fee considerations, but that other factors such as foreign exchange conversion rates and clearing costs affect dealer routing behaviour. We have been advised that labelling this matter as solely a marketplace fee issue is too narrow.</p>
<p><b>Policy 6.4 – Trades to be on a Marketplace</b>  <b>Part 6 – Foreign Currency Translation</b></p> <p>If a trade is to be executed on a foreign organized regulated market in a foreign currency, the foreign trade price shall be converted to Canadian dollars using the exchange rate the Participant would have applied in respect of a trade of similar size on a foreign organized regulated market in that foreign jurisdiction in order to determine whether the condition in subsection (3) of Rule 6.4 restricting avoidance of Part 6 of the Trading Rules has been met <u>and, if applicable, whether the requirement in subclause (ii) of clause (g) of subsection (1) of Rule 6.3 to execute at a better price has been met.</u> <del>The Market Regulator regards a difference of one trading increment or less as "marginal" because the difference would be attributable to currency conversion.</del> A Participant shall maintain with the record of the order the exchange rate used for the purpose of determining whether a better priced order existed on a marketplace and such information shall be provided to the Market Regulator upon request in such form and manner as may be reasonably required by the Market Regulator in accordance with subsection (3) of Rule 10.11.</p>	<p><b>Scotia</b> – What is the impact of the statement “the Market Regulator regards a difference of one trading increment or less as ‘marginal’ in the context of foreign currency translation?”</p>	<p>This statement was part of the former Best Price Obligation (Part 3 of former Policy 5.2) and had been carried over with consequential changes related to the implementation of OPR. Given current market structure, the provision is no longer relevant and IIROC would propose that it be deleted.</p>
<p><b>Questions:</b></p> <p><b>1.</b> The anti-avoidance rule introduced to UMIR on the introduction of OPR only applies to an order from a Canadian account denominated in Canadian funds. Should the anti-avoidance rule proposed in the Order Exposure Rule be similarly limited to provide greater flexibility to a Participant handling the order from a non-Canadian account or a</p>	<p><b>IIAC</b> – Yes. The Order Exposure Rule must be limited in order to provide clients with the widest access to foreign marketplaces. Question: Must firms route to a non-transparent marketplace in Canada before they access the U.S. market?</p>	<p>The Proposed Anti-Avoidance Provision would not restrict the ability of the client to instruct handling of the order other than by the entry of an order on a marketplace which is currently provided for in Rule 6.3(1)(a). Firms are not required to route to a non-transparent marketplace in Canada before they access the U.S. market.</p>





Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
<p>Canadian account denominated in a foreign currency?</p>	<p><b>RBC</b> – If anti-avoidance rule is approved, as proposed, the application should be limited.</p> <p><b>Scotia</b> – Yes. Not practical to require foreign currency denominated accounts to translate. Non-Canadian accounts are able to deal with brokers in their local jurisdiction without these requirements.</p> <p><b>IIAC</b> – Yes. This will provide clients with the widest access to foreign marketplaces and increase their ability to achieve best price and best execution.</p> <p><b>TD Securities</b> – Yes, but believes this creates an arbitrary distinction that is unfair to Canadian clients.</p>	<p>Comments are noted. We have not proposed a carve-out for non-Canadian accounts or a Canadian account denominated in a foreign currency primarily because we believe that it is important to apply the policy on a consistent basis to ensure that the policy objectives of the Order Exposure Rule and the dark liquidity framework are achieved.</p> <p>The Proposed Anti-Avoidance Provision would not restrict the ability of the client to instruct handling of the order other than by the entry of an order on a marketplace which is currently provided for in Rule 6.3(1)(a).</p>
<p>2. Are there alternative approaches which would ensure that the policy objectives of the Order Exposure Rule and the Dark Liquidity Amendments are achieved when an order is entered on a foreign organized regulated market?</p>	<p><b>RBC</b> – The protection of the price discovery mechanism should not come at the expense of investors’ access to liquidity. Suggests a provision be added to permit clients to provide a blanket consent to having their orders executed on non-transparent foreign market with the understanding that Canadian requirements respecting “better price” would not apply to those orders.</p> <p><b>IIAC</b> – Recommends that an informed consent provision could be introduced.</p>	<p>In IIROC’s view, provision for “blanket” consent would not be appropriate. The structure of the current rule allows the client to instruct that the order be handled other than as contemplated by the Order Exposure Rule (which may, for example, be in the form of the client selecting U.S. market execution or entering the U.S. symbol for an inter-listed security).</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p><b>Scotia</b> – Routing a Canadian dollar order to the U.S. is much more complicated than executing in Canada (foreign exchange, special settlement procedures and specialized order routing). Should address trading costs.</p>	<p>We note that the CSA are reviewing marketplace fees as part of the OPR review and have proposed regulatory action with respect to marketplace fees. These proposals are designed to address concerns that dealers have expressed regarding the level of trading fees in Canada.</p>
	<p><b>TD Securities</b> – Believes the alternative is to restore transparency of transaction costs, competition in marketplace fees and reducing the differential in Canadian and U.S. costs by eliminating or capping marketplace rebates.</p>	<p>See response to Scotia above.</p>
	<p><b>UBS</b> – Suggests the application of principles-based best execution guidelines. Alternatively the proposals should be specifically limited to “retail flow” (though do not believe different restrictions between retail investors and institutions are desirable). Suggests that the requirement should be for “execution quality improvement”.</p>	<p>In IIROC’s view, the best execution obligation should remain a principles-based rule. The Proposed Anti-Avoidance Provision is designed to result in a consistent application of policy to reward pre-trade transparency, and thereby maintain the quality of our equity markets.</p>
<p><b>General Comments</b></p>	<p><b>CSTA</b> – A majority of both buy-side and sell-side respondents to a CSTA survey agreed that the minimum price improvement should be one tick (or half-tick for a one tick spread). A majority of both buy-side and sell-side respondents agreed that “large” orders should be able to trade at the NBBO (while 12% of buy-side and 17% of sell-side believe that all dark orders should provide minimum price improvement regardless of trade size.</p>	<p>Comment is noted.</p>
	<p><b>ITG</b> – Reiterates opposition to amendments related to dark liquidity. Does not believe that dark trading harms price discovery. Over-arching concern is that it will force dealers to handle small orders in a manner that is different than they may wish to route larger orders.</p>	<p>Comment is noted.</p>
	<p><b>RBC</b> – Believes that the move away from a principled concept of best execution, specifically one that</p>	<p>Historically, UMIR contained two separate obligations being “best execution” which the Participant owed to the client</p>



Text of Provision Following Adoption of the Proposed Amendments	Commenter and Summary of Comments	IIROC Response to Commenter and Additional IIROC Commentary
	<p>preferences price over other aspects of best execution, represent an unprecedented and negative development for Canadian marketplaces and marketplace participants.</p> <p><b>TriAct</b> – Does not believe that the definition of “better price” is appropriate in the context of the maker/taker price models for trading fees.</p>	<p>and “best price” which the Participant owed to the market. Best execution was subordinate to best price. The best price obligation had been replaced with the introduction of the OPR but UMIR provides that compliance with OPR obligations overrides best execution considerations.</p> <p>IIROC acknowledges that “maker/taker” price models have changed the economics of trading for Participants. As a separate initiative, the CSA have proposed to conduct a pilot study on the effects of prohibiting the payment of rebates by marketplaces, including the maker/taker fee model in Canada.</p>
	<p><b>IIAC</b> – Must firms route to a dark pool in Canada before they access the U.S. market?</p>	<p>No. Under the UMIR “best execution” obligation, a Participant generally does not have to take account of possible liquidity in a non-transparent marketplace. Part 2 of Policy 5.1 sets out criteria when dark marketplaces in Canada should be considered and Part 3 sets out consideration for use of a foreign organized regulated market.</p>