CIBC World Markets Inc.
Brookfield Place
161 Bay Street, 4th Floor
Toronto, ON
M5J 2S8

March 30, 2015

Sonali GuptaBhaya
Senior Policy Counsel, Market Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 2000
121 King Street West
Toronto, ON M5H 3T9
Fax (416) 646-7265
Email: sguptabhaya@iiroc.ca

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

RE: RE-PUBLICATION OF PROPOSED DARK RULES ANTI-AVOIDANCE PROVISION - REQUEST FOR COMMENTS

CIBC World Markets Inc. ("CIBC") thanks you for this opportunity to comment on the proposed dark rules anti-avoidance provision ("proposed rules"). We are supportive of the policy objective to maintain a healthy and competitive Canadian market, though we have concerns with restrictive trade barriers if the proposed rules come into effect which we believe may hinder Canadian market efficiency and competitiveness, contrary to the policy objective. We are concerned that these proposed rules may put Canada at a competitive disadvantage for trading in interlisted securities and thus harm the health of Canadian capital markets.

These proposed rules, intended to protect interlisted order flow from migrating south of Canadian borders, were originally introduced as part of the overall dark rule amendment to UMIR related to the execution and reporting of "off-marketplace" trades that were published for comment in 2012. At that time, the proposed rules were collectively rejected by industry participants. The reasons provided for rejection remain the same today and we specifically highlight:

- Unfair to Canadian participants & investors
- Compromises the ability to obtain best execution
- Increases technology costs and technology developments

We acknowledge there is a tenuous balance between the protection of Canadian capital markets (market level) and best execution obligations of a participant to our clients' flow (order level). Because as a broker-dealer we are required to "diligently pursue the execution of each client order on the most advantageous execution terms reasonably available under the circumstances", as per UMIR Rule 5.1 ("Best Execution"), it is from this position that we address our comments on the proposed rules.

We recognize IIROC's concern that retail and small institutional order flow is being routed to US markets, and that the proposed rules aim to encourage trading on Canadian marketplaces. However, we believe that the introduction of new and potentially restrictive rules should be based on quantitative evidence that has been presented to all market participants, and we have not seen data to suggest that there has been a material increase in the volume of orders being sent to the US. For greater clarity, the

proposed rules may be addressing an issue that doesn't exist, and these proposed rules could have serious unintended consequences.

NON-TARIFF TRADE BARRIERS

New regulatory initiatives without clear substantiation of the existence of an issue should be avoided. In our view, the implementation of the proposed rules is akin to the creation of a non-tariff barrier to trade. These proposed rules will aim to control and contain order flow in interlisted names to the Canadian markets and therefore may not allow markets to function efficiently. In our opinion this will ultimately hurt Canadian investors and dealers by unduly limiting access to liquidity in a larger multijurisdictional market, putting Canadian broker dealers at a competitive disadvantage relative to US broker dealers who have this capability, limiting marketplace competition and reducing the efficiency of existing trading capabilities. Furthermore, Canadian and US buy side clients alike can choose to opt out of a restrictive Canadian regulatory environment.

The solution may not be to ring fence Canada but instead to remove the regulatory bifurcation. If the truth is that there is greater liquidity in the US markets, the original implementation of the Dark Rules may have put Canada at a disadvantage, and if this is the issue, perhaps a better approach would be to address this disadvantage instead.

WHY DO ORDERS TRADE IN US DARK POOLS

There is a straightforward explanation for why US markets are considered in routing decisions – Best Execution. More explicitly, the reasons include access to a larger and more liquid market, price improvement opportunities and lower explicit costs to trade.

In the original dark rule proposal, IIROC noted "the concern with respect to the potential loss of passive liquidity to other jurisdictions. However, the offsetting factor will be that the opportunity to obtain meaningful price improvement may attract more active order flow to "check" the dark pools before being entered on a transparent market." This does not appear to have been the outcome. US dark pools are a healthy percentage of interlisted order flow. In other words, "meaningful" price improvement is secondary to access to the liquidity. Second to the TSX order books, US dark pools trade the greatest percentage of interlisted volumes, representing 18% of overall (interlisted) trading. This is a significant amount of liquidity to eliminate from routing decisions should the proposed rules be enacted.

For interlisted securities, brokers, on behalf of their retail and institutional clients, will make order routing decisions primarily based on explicit price improvement (inclusive of FX adjustments). If for example, there is no liquidity in a Canadian dark venue, which by rule must execute with "meaningful" price improvement of one trading increment, or midpoint in the event of a one tick spread, client orders may first look to US dark pools for other levels of price improvement prior to executing at the bid/offer in visible venues. We believe that this is consistent with Best Execution obligations where a broker is attempting to provide clients with the benefit of both price improvement for their order immediacy, by accessing the greatest amount of liquidity available.

Furthermore, growth in US interlisted market share may not represent a displacement of flows from Canada to the US, but may be a result of many other factors such as home country bias, currency fluctuations, and sector-level fluctuations. Put another way, we may not be observing the diversion of orders southbound, but rather orders that did not originate in - or ever enter - Canadian borders. It would make sense that this order flow will continue to execute in US markets despite the introduction of these proposed rules which would only be applicable to the Canadian participants. This would put the Canadian dealers, and ultimately their retail and institutional clients at a disadvantage, while having negligible impact on Canada's share of interlisted trading.

Fundamental to our position is a belief that the existing regulatory framework has allowed for dark pools to be well integrated into the Canadian marketplace. Artificial constraints on a structure that provides real value to the market will create missed opportunities and reduce efficiencies. Without convincing evidence to demonstrate and substantiate that dark liquidity is damaging market quality and integrity, the introduction of restrictive barriers for Canadian broker-dealers to access US dark pools only serves to eliminate opportunities to trade relative to US-based brokers who can still access liquidity on both sides of the border, and thereby increases opportunity costs for our clients and clients of other Canadian broker dealers, thus weakening Canadian capital markets.

RESTRICTING THE RETAIL FLOW

Placing a size restriction on the proposed rules (under 50 board lots) will have the negative consequence of restricting many orders from participating in dark pools. Orders should not be disadvantaged by regulation because they are not of sufficient size to participate, such as retail or small institutional order flow. Forcing smaller orders to post on visible markets unfairly limits their available execution options without any particular rationale.

Both average order and trade sizes have steadily declined over the years. The slicing of orders is a risk-management strategy, reducing both market risk and footprint. Executing in dark pools is another way to manage these risks. Market participants have the necessary tools and expertise to represent orders in a multi-market environment. What is the benefit of forcing market participants to choose between slicing and dark execution, when their US counterparts can use either or both strategies to optimize execution?

If an order size restriction is set for dark liquidity, despite the imbalances this would create, the size threshold should, at a minimum contemplate changes to current and expected future average order and trade sizes.

PROTECTION OF OUR MARKETS

Our concerns around these proposed rules stems from the belief that restrictions on trading interlisted securities in US dark pools creates barriers to trade that may ultimately discourage investors from participating in Canadian equities, thereby leading to the creation of greater harm in the long term.

Marketplaces may believe they will benefit from the repatriation of small orders from US venues. However, we do not believe this will necessarily be the outcome. One foreseeable unintended consequence of ring-fencing order flow within Canada is that the very same fence may simply keep the order flow from coming to Canada in the first place. Like all unilateral trade barriers, it puts Canadian dealers at a disadvantage relative to US dealers who would still have trading access to US dark pools for interlisted securities without satisfying Canadian price improvement rules and may actually encourage further interlisted migration to the US.

Currently, the US does not have a similar regulatory framework for dark pools and interlisted orders originating from US broker dealers can execute on dark venues in the US without being subject to this mandatory price improvement. US dealers will have access to US markets and Canadian markets. This flow can execute in the US at more competitive prices and exchange fees. Bifurcation of the markets by regulation will lead to increased arbitrage opportunities whereby investors will ultimately find themselves in a worse position. In other words, we raise concerns around fairness and maintenance of a level playing field relative to US dealers, as well as around the inevitable loopholes which may be created as a result of differing regulatory standards.

We also note that changes to the “trade-at-rule” in US markets are currently under serious consideration, which would mean that trades in US markets could only be executed off-exchange (ie. dark pools) if at a significantly better price than that displayed on-exchange. In other words, US dark

rules may converge towards Canadian rules, and US dark pools could no longer trade at the bid or offer and would have to provide price improvement similar to our Canadian framework. We suggest that at the very least, this is an inopportune time for Canadian regulators to shut off access to the real liquidity on those dark venues. We recommend waiting for a resolution to the trade-at discussion.

Finally, we are of the opinion that it may be inconsistent and complex to introduce more restrictive execution measures at a time when the Order Protection Rules (OPR) are under review. A more appropriate approach may simply be continued compliance with best execution obligations where brokers evaluate price improvement and liquidity conditions in order to satisfy client obligations. Best execution should not simply be measured by trading price increments.

TECHNOLOGY IMPLICATIONS

The proposed rules apply only to orders under 50 board lots. Should this come to pass, there will be technology developments and amendments required by broker dealers to allow for a distinction between the routing and treatment of larger orders and smaller orders received from clients. In general, trading technology provides gating and filtering on order receipt, where order size may be taken into consideration. However, market access is a lower level filter which may be unaware of the larger (parent) order size. In order to reconcile and satisfy the proposed rules, there will be significant technology development required to provide gating rules contemplate order size as a determinant of routing strategy. We also note that complications arise should the (original) client order change, such as sizing up or down.

These proposed rules will also introduce greater complexity to smart order routing logic and to trading platforms in general. If in fact we will be required to comply with this rule set then a sufficiently lengthy implementation period well in excess of the standard 90 days should be provided.

CONCLUSION

In general, we are of the view that Canada has done a good job of fostering competition, balancing regulatory oversight, and allowing business concerns to drive innovations in the markets. We are required to compete globally for capital, and this has required Canada to foster, establish and maintain high quality capital markets. We recognize and appreciate the intent of policy changes, to address inefficiencies in the market. However, we are also sensitive to our markets being inextricably tied to our large US neighbor, and the negative consequences of regulatory arbitrage. In particular for interlisted trading, the primary benefit of US dark pools is access to a larger pool of liquidity, and therefore greater trading opportunity irrespective of the given size of an order.

Thank you for the opportunity to provide our comments on the proposed anti-avoidance rules. Please feel free to contact us with any questions or requests for clarification.

Sincerely,

"Heather Killian"
Executive Director, Equity Markets
CIBC World Markets Inc.