Chapter 13

SROs, Marketplaces, Clearing Agencies and Trade Repositories

13.2   Marketplaces

13.2.1   Canadian Securities Exchange − Significant Change Subject to Public Comment − Amendments to Trading System Functionality & Features − Notice and Request for Comment

Notice 2017-009

April 27, 2017

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CANADIAN SECURITIES EXCHANGE

SIGNIFICANT CHANGE SUBJECT TO PUBLIC COMMENT

AMENDMENTS TO TRADING SYSTEM FUNCTIONALITY & FEATURES

NOTICE AND REQUEST FOR COMMENT

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The Exchange is filing this Notice and Exhibit E to Form 21-101F1 in accordance with the process for the Review and Approval of Rules and Information Contained in Form 21-101F1 and the Exhibits Thereto attached as Appendix B to the Exchange's recognition order ("Protocol").

A.   DESCRIPTION OF THE PROPOSED AMENDMENTS

The Canadian Securities Exchange ("CSE" or the "Exchange") is implementing changes to add price protection and reduce price volatility of oddlot trades.

For securities with a designated market maker (MM), tradeable oddlot orders currently execute automatically against the market maker's account at the National Best Bid or Offer (NBBO, comprised of protected market quotes). Oddlot orders on securities without a MM will seek out oddlot orders in the book, matching on an "any part" basis (as opposed to the "all-or-none" matching on other marketplaces).

Rather than individual price protection (i.e. "50 tick limit") on oddlot orders, the trading engine will restrict oddlot trades to at or between the NBBO. Oddlot orders will trade or book at or between the NBBO, with better limit orders being repriced to the opposite side. When one or both sides of the NBBO are absent, a Single Oddlot Price ("SOP") will be calculated, and odd lot orders will trade or book at that single price.

Detailed proposed changes to the oddlot functionality are blacklined, below.

- Oddlot orders and trades are considered Special Terms trades, in accordance with UMIR.
- Oddlots will only trade at or between the NBBO
- Oddlot orders trade any part ~~and can match outside the board lot bid/ask.~~
- ~~Regular odd lot orders are included in the 50 tick bid/ask protection limit. The price tick protection parameters are set off the first trade of market orders and better price limit orders~~
- ~~Active odd lot orders will be protected by trading or booking at their limit price up to the freeze parameter limit as specified on the security. This protection is in effect in continuous trading~~
- Oddlot Price Protection: Market or better limit oddlot orders may be repriced based on the following Oddlot Price Protection (OPP) requirements:
    - a) NBBO – oddlot orders that are priced at or better than the opposite side of the NBBO will be repriced to that price. They will interact with existing oddlot orders at or better than that price, then the balance will trade with the Market Maker or will book there, as applicable. Oddlot orders priced between the NBBO will book or trade at their limit or better, depending on oddlot orders in the book.
    - b) For a one-sided market, the SOP will be a calculation based on the existing bid or offer, and the last sale price
        - i.   If the bid < last sale, or ask > last sale, use last sale price;
        - ii.   If the bid > last sale, or ask < last sale, use the bid/ask
    - c) If there is no NBBO then the SOP will be the last sale price.

- Oddlot Market and Mixed lot market orders are accepted in preopen
- Oddlot orders will be held in a queue in pre-open, and after the market opens (with or without boardlot trades) oddlot orders in queue will enter the continuous trading session in order of original entry (by time priority) and trade at the NBBO or SOP
- On GMF enabled stocks (i.e. those with a Market Maker), as the NBBO changes, booked Oddlots that would be tradeable at the current NBBO will become active and autotrade at the current NBBO with the Market Maker
- ~~For securities that are enabled GMF, odd lot orders will be auto traded at the CSE bid/ask with the designated market maker responsible for the security if they cannot be filled by odd lots in the book at or better than the bid/ask board lot market.~~
- If there is no NBBO, oddlots will only trade at a Single Oddlot Price (SOP). Oddlots priced at or better than the SOP will book or trade at the SOP.
- For GMF enabled stocks Oddlot orders will trade with the book the then Market Maker will fill balance at the NBBO OR the Single Oddlot Price.
- Oddlots trade by price/time priority.
- Oddlots trade only with other odd lots or the market maker for stocks that are enabled with GMF.
- Oddlot trades will not affect the Last Sale Price.
- ~~Are subject to Thresholds.~~
- Oddlot orders may have all the regular attributes of board lots (e.g. Anonymous, Short, NCIB etc.).
- Oddlot orders may be any duration ~~except for FOK.~~

B.   Expected Implementation Date: September, 2017

Availability for testing in the CSE GTE was announced January 31, 2017 and testing commenced on March 6, 2017. The functionality will not be part of the May 2017 release and has been removed from the GTE until after that release.

C.   Rationale and Analysis

Oddlot orders that are entered as market orders or with deep price limits can match well outside the displayed quote, resulting in poor fill quality.

IIROC, in an attempt to curb the practice of entering oddlot order with deep price limits, published a Rules Notice[1] ("Notice") that stated IIROC would no longer rule on oddlot trades, and participants must not pass on poor fills to clients, but rather make an adjustment in the client's favour at their own expense. In principal, the Notice was intended to modify the behaviour that caused the poor fills. In practice, IIROC's Guidance has led to some confusion about whether the absence of a ruling on certain trades represents a tacit approval of the trades, or whether the marketplaces now have the authority to cancel erroneous oddlot trades.

The CSE has determined the most appropriate approach to preventing such trades is to implement price restrictions on oddlot executions that will be effective with or without a MM, and with or without a full NBBO.

D.   Expected Impact

The changes are being implemented in response to customer demand, and to improve the quality of oddlot fills and maintain the integrity of the price discovery mechanism.

E.   Systemic Risk

The CSE does not believe that any increase in systemic risk would be introduced with the approval of the proposals.

F.   Compliance with Ontario Securities Law

There will be no impact on the CSE's compliance with Ontario securities law. The changes do not alter any of the requirements for fair access or the maintenance of fair and orderly markets.

G.   Consultation

The CSE has consulted with a number of dealers and industry stakeholders and considered the feedback received during informal dialogue.

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[1]   IIROC Rules Notice 13-0297 Variation and Cancellation of Odd Lot Trades, http://www.iiroc.ca/Documents/2013/f9404291-d1fa-4ca8-889f-0c7a61a11fe2_en.pdf

H.   Technology Changes

CSE is not aware of any technological changes that will be required by participants or vendors.

I.   Alternatives

The Exchange considered variations of price limits, as well as cancelling oddlot order with significantly better limits than the NBBO. Also under consideration was the ability to have a flexible Exchange-defined premium or discount to the NBBO. Restricting trades to within the NBBO is the solution that most accurately reflects the desired quality and integrity of the market.

J.   Other Markets or Jurisdictions

Other exchanges (TSX, TSX-Alpha, TSX Venture Exchange, Aequitas Neo) and Nasdaq Canada's CX2 have facilities that include the automatic execution of odd lot trades against the account of an individual/participant/subscriber (a "Specialist") that has been appointed by the exchange or marketplace for that purpose. To promote quality of fills, the other exchanges rely on the fact that the majority of securities are assigned to a Specialist. For those securities that are not assigned, odd lot orders may book at the opposite side of the market (market orders) or their price limit. If price information is not available, the order may book at the last sale price. In the case of CX2, only tradable IOC orders are accepted.

K.   Comments

Submit comments on the proposed amendments no later than June 12, 2017 to:

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