

The Pulse of Finance

Newedge



BY FAX AND OVERNIGHT MAIL

August 19, 2010

Market Regulation Branch
Ontario Securities Commission
Suite 1902, Box 55
20 Queen Street West
Toronto, ON M5H 3S8

Re: Newedge Comment Letter/Alpha ATS LP–Notice of Proposed Changes 13.2.3

Dear Sir or Madam:

We are writing on behalf of Newedge Group SA (“Newedge”) to provide you our views on Alpha ATS LP–Notice of Proposed Changes 13.2.3, published on July 16, 2010. Thank you for providing us with this opportunity to respond. As we set forth below, we believe that implementation of the Alpha IntraSpread™ Facility (“Alpha Facility”) will further erode transparency in the Canadian equity market and exacerbate the already unequal “playing field” with respect to market access.

BACKGROUND

Newedge Group, SA (“Newedge”), which is one of the world’s largest brokerage organizations, offers its customers clearing and execution facilities across multiple asset classes including futures, securities (fixed income and equities), options, FX and various OTC instruments.¹ Newedge maintains offices in over 15 countries, and is a member of over 80 exchanges worldwide. Newedge estimates that its customers – who are principally institutional – executed and cleared approximately 2.9 billion exchange-trade contracts in 2009. As of 31 December 2009, Newedge had an estimated global market share in listed derivatives of 12.1% (clearing) and 11.1% (execution), and over \$54.8 billion of client assets on deposit.

Newedge Canada, Inc. (“NC”) is a 100% subsidiary of Newedge. NC, which has offices in Montreal, Toronto and Calgary, is one of the leading brokerage firms in Canada. NC executes transactions on behalf of its customers on an agency and riskless principal basis across a variety of asset classes,

¹ “Newedge” refers to Newedge Group, a 50%-50% joint venture between Credit Agricole Corporate and Investment Bank (formerly Calyon) and Societe Generale, headquartered in Paris, France, and all of its worldwide branches, subsidiaries and other units.

including equity, equity options, futures, fixed income and OTC derivatives. NC, which is a member of CDS as well as all primary exchanges in Canada, self-clears the great majority of transactions it and its customers execute. NC provides “live” brokerage services to its customers, as well as direct market access (“DMA”). NC’s customers, which are exclusively institutional, include other registered broker-dealers and future commission merchants, banks, pension plans, government entities, hedge funds and professional trading groups. NC does not act as a dealer nor a market maker, does not engage in investment banking activities, and does not trade securities or futures on a proprietary basis.

DISCUSSION

The Alpha Facility includes two new order types – the Dark Order and the Seek Dark Liquidity Order™. Key aspects of these order types appear to be that they will:

1. be used to manage passive interest
2. involve no pre-trade transparency
3. provide potential price improvement in fractions (less than \$0.01)
4. not trade with each other

In our view, implementation of the Alpha Facility will benefit a small number of investors at the expense of overall market transparency, and will exacerbate the already unequal playing field that exists with respect to the current market structure in Canada. Specifically, it is well-recognized that passive interest is a key driver for high frequency participants whereby a main objective of their trading strategy is to earn passive rebates on the marketplaces. In conjunction with the proposed dark order types by Alpha, 50% fee cuts for participation into IntraSpread™ were also announced. Consequently, we believe the Alpha Facility will draw significant visible liquidity out of the market from high frequency traders, which will further erode the visible price discovery mechanism within the Canadian equity markets².

Indeed, it is for this very reason – *i.e.*, the erosion of price transparency by dark pools – that in October 2009 the SEC proposed lowering the average daily trading volume threshold that would trigger the order display and execution access requirements for an ATS from 5% to 0.25%.³ In the same circular of proposed changes, the SEC stated consolidated market data both pre-trade and post-trade is the primary vehicle for public price transparency in the U.S. equity markets.⁴ We believe the SEC’s concerns are equally applicable to the Canadian equity markets, and that any rules issued

² Reviewing the publicly available TSX trading leader’s list for July 2010 the liquidity control of Alpha’s members is in excess of 50%. See: http://www.tmxmoney.com/en/market_activity/trading_list_leaders.html.

³ Securities Exchange Commission, Proposed rules and amendments to join-industry plans, <http://www.sec.gov/rules/proposed/2009/34-60997.pdf> (October 2009)

⁴ Securities Exchange Commission, Proposed rules and amendments to join-industry plans, <http://www.sec.gov/rules/proposed/2009/34-60997.pdf> (October 2009)

impacting market transparency and open access negatively are inconsistent with key OSC or IIROC principles.⁵

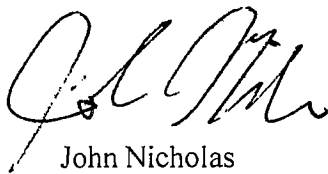
We also note that the proposed price improvement that would take place with an SDL™ order of less than \$0.01 increments appears to be in conflict with current practice. Indeed, for orders whereby the security is trading above \$0.50 orders on marketplaces must be entered in whole cents. UMIR Rule 6.3 (1) implies a dealer must quickly enter a client order on a visible marketplace unless the dealer executes the client order upon receipt at a better price. Price improvement has been historically improved by at least one trading increment as supported in UMIR Rule 6.3 “Exposure of Client Orders.” Consequently, in our view, the current Alpha Facility proposal is inconsistent with established Canadian equity market rules and practice.

It is in the interest of the industry and the integrity of our capital markets to be given full disclosure of how the two proposed order types will truly function and not just a cursory explanation currently provided within Alpha’s submission. For example, there is no clarity how orders at the same executable price will be allocated with various spreads. In addition, if Alpha is a continuous marketplace and in absence of any special terms, why won’t a Dark Order not set the Last Sale Price?

More generally, we believe there already are a number of dark pools operating in Canada that, as noted above, are eroding price discovery and creating an unequal playing field in the equity markets. Consequently, we urge OSC and IIROC to review the activities of these market centres and promptly take any actions necessary to ensure that they operate in a manner that is consistent with overall OSC and IIROC market objectives, structure and mandates.

Please do not hesitate to contact the undersigned at (646-557-8516).

Sincerely,



John Nicholas
US Securities Compliance Director and
Global Securities Compliance Coordinator
Newedge USA LLC

⁵ See, e.g., OSC’s Vision (“fostering a culture of integrity and instilling investor confidence in the capital markets”); OSC Goals (“[c]hampion investor protection, especially for retail investors”); OSC Mandate (“provide protection to investors from unfair, improper practices and to foster fair and efficient capital markets and confidence in capital markets”); IIROC Mandate (“We set and enforce high quality regulatory and investment industry standards, protect investors and strengthen market integrity, while maintaining efficient and competitive capital markets”); IIROC Vision (“We will be known for our integrity and transparency and our fair and balanced solutions”).