



RE: PROPOSED AMENDMENTS AND GUIDANCE RESPECTING TRADE INCREMENTS

January 27, 2025



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January 27, 2025

Attention:

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Dear Mr. Bailey:

We write in response to CIRO's request for comments on its [Proposed Amendments Respecting Trading Increments](#) (the "**Proposed Amendments**") and [Proposed Guidance on Applicable Trading Increments](#) (the "**Proposed Guidance**"), which raise important issues related to the harmonization and competitiveness of Canada's securities marketplaces.

EXECUTIVE SUMMARY

We appreciate that the objective of CIRO's Proposed Amendments is to harmonize trading increments for certain inter-listed securities with the increments established by the United States Securities Exchange Commission under Rule 612 of Regulation National Market System (the "**SEC Regulations**"). We agree that failing to harmonize minimum trading increments for inter-listed securities with the amended SEC Regulations could result in reduced order flows on Canadian marketplaces and an incremental redirection of orders to US ventures. As such, we generally support the Proposed Amendments.

However, to foster competitive capital markets and encourage capital formation, Canada's securities regulations must do more than achieve parity with SEC Regulations. Whereas the SEC Regulations were amended with the strategic goal of improving the competitiveness of the U.S. securities market, in Canada, the Proposed Amendments and Proposed Guidance are, unfortunately, simply intended to keep pace with the SEC Regulations.

We recommend efforts be made to achieve an innovative, Canadian, globally differentiated approach that improves the competitiveness of the Canada's financial markets. These include

A) Flexibility:

- On whether to adopt or reject SEC Regulations based on market impact.
- For Alternative Trading Systems and Exchanges to serve their customers at higher or differing increments.
- To administratively adjust increment levels for foreign exchange movements.
- To include non-interlisted securities

B) Thorough Reviews of Factors Leading to Liquidity

These include a review of lot sizes, execution frequency, fees and fee caps.

The Logic and Purpose of SEC Regulations

There are economic drivers to the SEC Regulations which are unique to the US market.

The SEC states, in part ... *“Many nms stocks would likely be priced more competitively if not constrained by a market-wide minimum pricing increment of \$0.01.”*¹ Why?

Trading increments are one of several elements that generate potential intermediation benefits to investors and market makers. Market makers provide (addressable) liquidity in return for the opportunity to generate spread revenue net of all trading costs. The achieved spread (the Average Time Weighted Spread “ATWS”) is the result of efforts of many market makers and client participants.. Trading increments, lot sizes and execution latency are exogenous factors outside a market maker’s control which generate potential spread revenue. Sub-penny increments (or smaller lot sizes and latency) are risk reducing. With lower minimum increments (or lot sizes and latency), all else equal, a market maker, takes less risk for the same capital, or over time, and can provide more capital (addressable liquidity) with the same risk.

In particularly deep markets such as the United States, even while securities may trade at a penny increment, it is still possible for the ATWS to be in fractions of a penny. The ATWS is independently achieved from the minimum trading or quotation increment². The ATWS can therefore be lower than the minimum trading increments. An ATWS that is sub-penny in “normal” markets, reflects the natural spread and liquidity of a security regardless of their notional price. Highly liquid names may have ATWS at a sub-penny or so close to zero, such that market maker liquidity may not be necessary in normal trading circumstances.

Sub penny quoting on a net basis across books is a US reality. Market makers may counter-intuitively participate heavily in dark pools and wholesale markets in the US due to differences in order treatment, pricing, and rebates in dark pools and through nuances of US market structure.

The SEC Regulations are intended to reflect US market realities and to reduce market maker risk on mega-cap expensive stocks unique to US markets. To the extent that highly liquid securities continue to have ever increasing notional price, reducing the increment or quoted spread, reduces the risks of market makers to those names. With lower increments, market makers may increase their exposed liquidity on each side and/or increase their frequency of quotation, while reducing their risk. Competitive forces continue to narrow the ATWS, especially for highly capital-intensive names.

Canada’s Unique Market Conditions

Canada generally does not have stocks trading at highest notional US prices or with ATWS near zero. Canada has a uniqueness to punch above its weight, with the converse problem of the United States: natural spreads that are too wide and multiples of the minimum tick size.

Canada has effectively three radically different equity market pools:

¹ U.S. Securities and Exchange Commission, [SEC Adopts Rules to Amend Minimum Pricing Increments and Access Fee Caps to Enhance the Transparency of Better Priced Orders](#) (Sep 18, 2024).

² For example, if the minimum trading increment were \$1 and min quote was a \$1, but a security was continuously traded back and forth at bids and offers of \$100 all day long, the ATWS would still be \$0 for that day.

1. **Highly liquid, deeply traded, mostly non-intermediated inter-listed equity securities markets:** Canada is the only nation in the world that has a freely traded “inter-listed” market with the largest capital market. Our large cap companies benefit from exposure and liquidity in the United States, allowing their securities to trade as naturals. The global peer set of securities resembling the trading activity of these names may be S&P small and mid-cap companies. The inter-listed capability is a unique and competitive advantage of our markets on a global scale.
2. **Liquid, intermediated, non-inter-listed senior equity securities market:** This group includes the majority of the non-inter-listed names qualifying for listings on the senior Toronto Stock Exchange and trading as Tier A liquidity securities. The peer set for these companies may be commonly held equities which are domestically traded in markets such as Australia, Italy, and the Scandinavian countries. This tier of securities benefits from a highly competitive secondary trading mechanism, which itself is a unique asset to Canada compared to economies of a similar size.
3. **Illiquid, Tier B security, heavily intermediated secondary trading of junior and venture oriented equity securities:** These securities number in the 1000s across a variety of junior exchanges including TSX venture and the CSE. Market capitalizations range from 1/2mm to over \$100mm. In this regard, there are almost no marketplaces in the world which are as properly regulated and as robust in providing primary financing opportunity to such securities with the breadth of activity as Canada. This capability is also a unique and competitive advantage of our markets on a global scale, which remains challenged on a secondary trading basis.

Recommendations for Canada

We recommend that UMIR Rules and CIRO move beyond harmonization to focus on competitive advantages for Canadian markets and include:

I. Options

- a) if we are introducing a rule set to maintain competitiveness with the United States and determine that it ultimately does not achieve the desired result, for some subset, or the entire set of inter-listed securities, these proposals should not lock the industry into a competitive disadvantage, but should be tested and re-assessed for desired effect, or, alternatively, implemented on a pilot basis. Similarly, should these proposals provide Canada with a capital risk advantage, the option of maintain them should the SEC Regulations be rescinded due to SEC administrative changes.

The Proposed Amendments state that the minimum trading increment for inter-listed securities will be “designated from time to time by the Market Regulator.” In the current form, the Proposed Guidance defines the process by which trading increments will be designated and states: “CIRO will harmonize the applicable trading increment in Canada for that U.S. inter-listed security with the applicable minimum pricing increment in the United States [emphasis added].”³

In light of the above, we recommend that the Proposed Guidance be amended to state that CIRO maintains discretion to adopt the minimum trading increment set by the SEC and may designate

³ See s. 2 of the Proposed Guidance under heading, *Co-ordination of trading increments with the United States for a U.S. inter-listed security*.

a different trading increment if so determined.

- b) Flexibility for Alternative Trading Systems and Exchanges to serve their customers at increments which are greater than the minimum and differing from each other (i.e., quotation vs. execution). For example, stocks priced above \$100 may consider increments higher than a penny to factor in intermediation.
- c) Increment levels are subject to a schedule which can be adjusted administratively, should the market need to adjust quickly due to foreign exchange movements. On an exchange adjusted basis, the proposed tick size is USD\$0.0035 for Inter-listed in Canada. This is factored into liquidity providers algorithms and for now will provide a floor under the competitive share of liquidity provided in Canada. The rules and systems should be flexible enough that the increments are adjustable should f/x rates move in the other direction, and competitiveness diminished.

As currently drafted, the Proposed Guidance states that, “for purposes of harmonization” no currency conversion will be applied to Canadian trading increments.

In light of the above, to improve the competitiveness of Canada’s securities market, pricing increments for inter-listed securities should be calculated on an exchange-adjusted basis.

- d) The inclusion of non-inter-listed securities. If the benefits are as positive as expected for liquidity providers, they should be extended. For example – if a non-inter-listed security exhibits the same characteristics (ATWS, price, lot size and execution frequency) of an inter-listed security, it should also benefit from a lower minimum tick size, the opportunity to generate spread revenue and the opportunity to manage capital risks to market makers.
- e) For mid-frequency or low frequency securities increments may be redefined on a percentage basis.

II. Thorough Reviews of Factors Leading to Liquidity

Canada has an opportunity to lead through a review of all the factors leading to liquidity in search for more incentives to intermediation, and therefore increased liquidity. These are as follows:

a) A Review of Lot Sizes across all Tiers of Securities and all Marketplaces:

Lot sizes are an intermingled, integrated, and fundamental element in the incentive to generate liquidity in a marketplace. Addressing increments without lot sizes is a partial factor solution, and may lead to dramatically sub optimal results, supporting the need for optionality.

In particular, the quantity of equities being traded in the odd lot market continues to grow as driven by an increased interest in fractional securities. While not offered by all retail trading houses, the growth in this area changes demands on systems, and over time, the fixed costs of the entire industry.

The review would consider the possibility of introducing more addressable liquidity by adjusting board lot sizes by price, holding all else equal.

b) A Review of Execution Frequency:

Liquidity is a direct function of execution frequency coupled with increment and lot size risk drivers. The assumption and drive for inter-listed and non-inter-listed securities has, for the last two decades, revolved around using computing technology to increase execution frequency, by reducing a variety of latencies (quotation, execution, confirmation etc.). A variety of stakeholders and participant groups in the industry have indicated that extreme frequency may introduce other market harms, and some order types, mechanisms and exchanges have introduced limits on frequency via speed bumps, special order types or through special call markets (such as the market on close) which generate a significant participation from those seeking to avoid both buyers' and sellers' remorse.

The review would consider whether a deliberate market wide approach to reduce execution frequency enhances liquidity provision in Canada's illiquid securities market or subsets of Canada's market.

c) A Review of Fees and Fee Caps:

Potentially differing fee caps could offer competitive advantage for Canada. Different fees at the open, close and the central limit order book present many opportunities for arbitrage, liquidity gaps and discontinuity. For example, in a world with a reduced spread, the incremental fee difference in the market-on-close and the central order book, becomes a more material decision factor on where to place liquidity. Furthermore, to the extent that the US has fee caps, the elimination of fee caps (and therefore rebates) may attract capital to Canada.

We note: [CSA Notice and Request for Comment – Proposed Amendments to National Instrument 23-101 Trading Rules and Proposed Changes to Companion Policy 23-101 Trading Rules](#)

Answers to CISO's questions are included in Schedule A.

Respectfully submitted,

Investment Industry Association of Canada

cc.

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Schedule A

Answers to CIRO Questions

General Comment:

We understand that, for the purposes of the Proposed Amendments, it is necessary to differentiate between securities that are listed on exchanges in Canada from securities that are inter-listed on exchanges in Canada and the United States. However, on a principled basis, we recommend that CIRO refrain from adopting “U.S. Inter-Listed Security” as the defined term. We note that “U.S. Inter-Listed Security” implies and gives reference to US-listed and originated securities that have been listed on an exchange in Canada and not Canadian listed and originated securities. For the latter, Canadians took the financial and business risks to underwrite, trade and develop these companies. We suggest that CIRO adopt a more neutral term such as, for example, “North American Inter-Listed Security” for its Proposed Amendment.

Responses to Consultation Questions

Question No. 1:

In the future, we may consider whether to apply changes to trading increments to all Canadian-listed securities. We welcome any preliminary feedback in this regard.

See prior comments. A coherent, deliberate and integrated approach to trading increments which also factor in minimum board lot sizes, the incentives for ever reduced latency, and other costs of intermediation (including net fees and foreign exchange) which will promote the right balance of incentives across all the constituents creating liquidity in the unique aspects of Canadian markets is necessary as Canadian markets look forward. Reducing minimum increments may make sense for Canadian listed securities as part of an integrated set of changes that also addresses lot sizes, execution frequency, fee caps, forex, and other costs.

Concerns have been expressed regarding low volume junior issuers (TSXV & CSE) where sub-penny pricing could have a negative impact on liquidity.

Question No. 2

As noted, we expect significant implementation efforts by industry if the Proposed Amendments are finalized. Recognizing that the compliance date for the amendments to Rule 612 is November 3, 2025, and acknowledging the need for harmonization, what is the expected minimum required time for various stakeholders (Dealer Members, marketplaces, information vendors etc.) to be prepared for an aligned implementation date in Canada?

Presently ½ penny increments already exist for securities trading under \$1. Any physical increases in network capacity, processing, memory, and/or storage are not predictable. These changes will also require integration testing across systems, which may cause unforeseen delays in implementation. We therefore recommend that CISO adopt a two-step process that includes a preliminary attestation and plan for adoption.

Question No. 3

Rule 612 provides for a 1-month implementation window at the end of each semi-annual evaluation period (i.e., a 1-month window between establishing the increment and the effective date). Is this sufficient time for Canadian marketplaces to amend trading increments for listed securities in Canada?

No concern.

Questions No. 4

Rule 612 requires the primary listing exchange in the United States to measure the time weighted average quoted spread for each NMS stock, a measurement that determines the applicable minimum pricing increment. The primary listing exchange is also required to provide the applicable minimum pricing increment to various information processors for dissemination. We are soliciting feedback on the best approach to disseminating the applicable trading increment in Canada based on the data disseminated in the United States.

To ensure the harmonization of rates, CISO will need to disseminate the same information within the 30-day period contemplated by the SEC Regulations. We note that this could be accomplished by publishing an updated increment schedule on its website.