

May 28, 2025

**Submitted via Email**

Attention:

**Kent Bailey**

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Dear Mr. Bailey:

**RE: CIRO - PROPOSED AMENDMENTS RESPECTING CONTINGENT DERIVATIVE ORDERS**

We write in response to CIRO's Request for Comments (the "**Request for Comments**") on its Proposed Amendments Respecting Contingent Derivative Orders (the "**Proposed Amendments**").

**OVERVIEW OF POSITION:**

The Proposed Amendments are intended to correspond with amendments made to the Toronto Stock Exchange Rule Book (the "**TSX Rulebook Amendments**"), which were designed to facilitate contingent option trades that are linked to trades of options on the Montreal Exchange ("**MX**"). The Proposed Amendments support that goal. In addition, contingent option trades are likely to have a *de minimis* market impact. As such, we do not oppose the Proposed Amendments.

However, the incremental approach to the TSX Rulebook Amendments and CIRO's Proposed Amendments presents opportunities for improvement in the public consultation process.

Price discovery is generally considered critical to determining fair value. It finds a fair market price through several interactions between buyers and sellers over time. Its diminishment is therefore generally considered harmful as it may reduce market efficiencies and returns. Caution and deep analysis should be exercised regarding any future carveouts.

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## RESPONSE TO REQUEST FOR COMMENTS

### A. The Consultation Process

#### i) Avoidance of Bifurcation

The Proposed Amendments follow the TSX Rulebook Amendments, which were subject to a public consultation process. No public comments were received. CIRO has published the Proposed Amendments pursuant to UMIR requirements to reflect an existing exemption order.

The Proposed Amendments to UMIR ought to have been the subject to public consultation prior to the TMX Rulebook Amendments being finalized. This would have allowed consideration of wider market issues and avoid the appearance that the Proposed Amendments are a *fait accompli*.

#### ii) Inclusion of Data

The Proposed Amendments do not reference any data on the expected volume and value of contingent option trades.

#### iii) Deeper Impact Analysis

Subject to exceptions, the CBOE requires contingent derivative orders, namely Qualified Contingent Cross (QCC) orders, to execute at or between the National Best Bid and Offer (NBBO). The Box Options Exchange (jointly owned by the TMX Group and dealers) also generally requires adherence to NBBO for contingent derivative orders, namely Complex Customer Cross Orders. A qualitative comparison to other marketplaces to support the Proposed Amendments was not included.

The Proposed Amendments do not detail how the proposed exclusions may impact price discovery over time. Further, no alternatives were considered in the Proposed Amendments.

### B. Price Discovery

The TSX Rulebook Amendments – and by extension CIRO’s Proposed Amendments – appear to imply that option market price discovery occurs independently from the cash markets and indicate that price discovery for a contingent derivative listed on the TSX can occur on the MX and bypass the TMX price discovery process. These presumptions are questionable. For every order, the MX considers the underlying price of the cash market when determining the key inputs of options pricing models (intrinsic value, theta, and volatility). It is the cash markets price discovery process that must be protected.

### C. Go Forward Considerations

In Canada, the derivatives markets may be seen as largely “upstairs,” with orders being executed away from centralized markets. There is a risk that further carveouts from the Central Limit Order Book (CLOB) requirements could have long-term impacts on price discovery. Caution should be exercised on any future carveouts that are driven by upstairs trading activity.

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Publication of the following would be beneficial prior to the introduction of any additional carve-outs:

- a) Analysis of whether price discovery is occurring and if so, where the costs of its protection and the impact on the CLOB if price discovery is elsewhere.
- b) Relevant marketplace data on special term orders: the quantity of volume, value, and trade by security tier with measure of market impact.

Respectfully submitted,

***Investment Industry Association of Canada***

***cc.***

**Trading & Markets Division**

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