

Regulating dark trading: Order flow segmentation and market quality*Carole Comerton-Forde^a, Katya Malinova^b, Andreas Park^{c*}^a *UNSW Business School, UNSW Business School Building, NSW, 2052.*^b *University of Toronto*^c *University of Toronto Mississauga and Rotman School of Management***ABSTRACT**

We examine the impact of a rule in the Canadian equities market that requires dark orders to offer price improvement over displayed orders. We show that this rule eliminated intermediation of retail orders in the dark and shifted retail orders onto the lit market with the lowest trading fee. Intermediaries shifted liquidity supply to this market leading to increased displayed liquidity. We conclude that reducing retail order segmentation enhances lit liquidity. Despite the improvement in liquidity, retail traders receive less price improvement. Retail brokers pay higher trading fees to exchanges, and high-frequency traders earn higher revenues from trading fees.

JEL classification: G14

Keywords: Dark trading, Trade-at rule, Price improvement, Segmentation, Retail internalization

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