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May 23, 2018

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Transaction Fee Pilot for National Market System ("NMS") Stocks, File No. S7-05-18

Dear Mr. Fields:

BlackRock, Inc. (together with its affiliates, "BlackRock")[1] appreciates the opportunity to comment on the Securities and Exchange Commission ("Commission") rule filing to implement a Transaction Fee Pilot for NMS Stocks. As proposed, the pilot would study the effects of transaction-based fees and rebates on order routing behavior, execution quality, and market quality to facilitate a data-driven evaluation of the need for regulatory action.

BlackRock strongly supports the objectives of the pilot and commends the Commission's efforts to maintain fair and effective markets. As we noted in our market structure *ViewPoint*, the existing access fee cap is outdated and permits market forces to drive fees and rebates to excessive levels relative to the current magnitude of commissions and bid-ask spreads.[2] In turn, this creates a conflict of interest for brokers in routing client orders and contributes to the perpetuation of market fragmentation and complexity. BlackRock believes that lowering access fees and rebates would reduce their distortive effect on order routing, price transparency, and market quality. Accordingly, we welcome a pilot program which studies the impact of transaction fees and rebates on market structure.

We believe that the overall structure of the pilot will be effective at yielding relevant insights regarding the influence of transaction fees on the market. The test groups have been thoughtfully designed and the scope of securities and venues included is both appropriate and sufficiently comprehensive. However, there are a few elements which we recommend that the Commission should consider in order to improve upon the current proposal.

We believe that the addition of exchange-traded products ("ETPs") to the pilot would produce a more inclusive analysis of rebates and fees across all segments of NMS stocks. However, the ETP industry is fiercely competitive with multiple issuers offering comparable products tracking similar underlying benchmarks. Given the efficacy of rebates and incentives in attracting liquidity and promoting price discovery, a fundamental concern is that the assignment of look-

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1 BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers, and other financial institutions, as well as individuals around the world. BlackRock is the investment adviser to the iShares family of exchange-traded funds ("ETFs"). BlackRock also advises non-US ETFs.

2 BlackRock, *ViewPoint – US Equity Market Structure: An Investor Perspective*, (Apr. 2014), available at http://www.blackrock.com/corporate/en-us/literature/whitepaper/viewpoint-us-equity-market-structure-april-2014.pdf.

alike ETPs to different pilot test groups may encumber those securities subject to constrained transaction fee models with a significant competitive disadvantage. We recommend that the Commission should include ETPs if a fair and level playing field can be maintained across competing products for the duration of the pilot, such as ensuring that ETPs tracking similar benchmarks are placed in the same test group.

While we seek to mitigate the distortive effect of fees and rebates, we also recognize that incentives may exert a beneficial influence which outweighs any negative impact on less liquid, thinly-traded securities. Specifically, rebates may improve market quality in these securities and attract liquidity by compensating market makers for exposing their orders to information leakage and adverse selection.[3] As the Commission has previously noted, NMS stocks exhibit a broad spectrum of quoting and trading characteristics with nearly 40% of all securities trading less than 50,000 shares per day.[4] Chairman Clayton has even expressed concern that this segment of the market may not be adequately served under our current equity market structure.[5] Data from the pilot will be essential in providing a better understanding of the interaction between rebates and illiquid, small capitalization stocks. However, the Commission should consider the possibility that the optimal solution may not be a "one-size-fits-all" approach, but a multi-tiered model where the level of fees and rebates are determined by the liquidity, price or bid-ask spread of a stock. Further, for some groups of securities, even higher rebates may be warranted to enhance liquidity and market quality.

We believe that the pilot as currently structured is simple and straight-forward to both implement and comprehend. The addition of other overlapping elements, such as a trade-at rule or wider tick sizes, would overcomplicate the proposal and risk compromising the integrity of the pilot. As a result, we believe that the Commission should avoid introducing other confounding factors which would render the resulting pilot data difficult to evaluate. The tick size pilot, in particular, should be allowed to expire under its current terms, as it has not produced the intended results of improving market quality or liquidity for small and mid-sized companies; instead, it has harmed market efficiency by increasing trading costs for end-investors.[6]

A proper evaluation of the impact of the pilot should holistically assess the effect of transaction fees on overall market quality and transparency. Some market participants will be inclined to focus exclusively on bid-ask spreads and quoted display size; however, these are just a subset of the dimensions which reflect market quality. Further, wider spreads and lower display sizes may not necessarily be negative outcomes if they are associated with elevated price transparency over the net economics of trading or a reduction in excessive market intermediation. Estimates of institutional trading costs from broker dealers or trading analytics firms would provide a more accurate assessment of the impact to end-investors than using the bid-ask spread as a proxy. Measures of market fragmentation or order type usage may help to gauge the degree of market complexity across test groups. Additionally, metrics such as

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[3] BlackRock, Letter from Richie Prager, Head of Trading and Liquidity Strategies, to SEC Chair Mary Jo White (Sep. 12, 2014), available at: https://www.blackrock.com/corporate/literature/publication/blk-equity-market-structure-letter-sec-091214.pdf.

[4] Division of Trading and Markets, *Empirical Analysis of Liquidity Demographics and Market Quality For Thinly-Traded NMS Stocks*, (Apr. 10, 2018), available at: https://www.sec.gov/files/thinly_traded_eqs_data_summary.pdf.

[5] SEC Chairman Jay Clayton, *Remarks at the Equity Market Structure Symposium Sponsored by the University of Chicago and the STA Foundation* (Apr. 10, 2018) available at https://www.sec.gov/news/speech/speech-clayton-2018-04-10.

[6] BlackRock's internal analysis on the tick size pilot has shown that stocks assigned to the test groups incur 35-45% more transaction costs than stocks assigned to the control group. Analyses from ITG and Bernstein have demonstrated similarly injurious effects on investor execution costs. *See* Colleen Ruane and Phil Pearson, ITG, *Tick Pilot Update* (Jan. 2017), available at https://www.itg.com/thinking-article/tick-pilot-update/; Nataliya Bershova and Paul Jaquet, Bernstein Electronic Trading, *Tick Size Pilot – A Year In* (Nov. 2017).

realized spreads may help to assess the quality of executions on exchanges to the extent that lower transaction fees improve the routing priority of venues and decrease adverse selection. The Commission should examine the overall influence of transaction fees on all aspects of market quality.

We thank the Commission for this opportunity to comment upon and express our support for the transaction fee pilot. BlackRock believes that the suggestions we have proposed will improve the efficacy of the pilot and help to generate more meaningful data. Please contact the undersigned if you have any additional questions or comments on our perspectives.

Sincerely,

Hubert De Jesus
Global Head of Market Structure and Electronic Trading

Joanne Medero
U.S. Head of Global Public Policy