December 4, 2018

By E-mail and FedEx
Mr. Brent J. Fields
Secretary, U.S. Securities and Exchange Commission
100 F Street NE, Washington, D.C. 20549

Re: Transaction Fee Pilot for NMS Stocks, Securities Exchange Act Release No.82873 (March 14, 2018), 83 FR 13008 (March 26, 2018) (File No. S7-05-18)

Dear Mr. Fields:

I am writing to comment on New York Stock Exchange's (NYSE) November 20, 2018 comment letter criticizing the Division of Economic and Risk Analysis (DERA) for the posting of a study[1] on the Tick Size Pilot Program (Tick Pilot) where DERA tested whether knowledge of the rule change that mandated wider spreads materially impacted stock prices and found that it did not.

The Clear Purpose and Value of DERA's Event Study

DERA's event study is informative to a central criticism NYSE has repeatedly alleged regarding the Transaction Fee Pilot (TFP). NYSE has expressed concern that upon implementation of the TFP, spreads will widen in stocks chosen for the "low rebate" or "no rebate" buckets and that wider spreads will harm issuers of the impacted stocks. Using data from the recent Tick Pilot, DERA analyzed the market's immediate reaction to the publication of the stocks selected to have their spreads widened and found no significant reaction.

In the case of the TFP, it is not certain that spreads will widen – that is the hypothesis of an entity that clearly and publicly opposes the TFP. However, in the case of the Tick Pilot, it was certain that for a select subset of stocks in the Tick Pilot, spreads would widen to 5 cents. The Tick Pilot therefore provides an excellent opportunity to test whether wider spreads would impact the price of a stock, thus negatively increasing issuers' cost of capital.

As reflected in this excerpt from DERA's event study, to ensure that the analysis considered the widening of spreads, the authors thoughtfully tested the subset of stocks that had spreads lower than 5 cents:

> We find that the announcement of the assignment of stocks to the Test Groups and the Control Group did not have an impact on their prices. In particular, the announcement did not generate significant abnormal returns for stocks assigned the Test Groups, neither in absolute terms nor relative to stocks assigned to the Control Group. These results hold even when we limit the analysis to stocks with pre-Pilot quoted spreads smaller than $.05.[13]

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[1] *Does the Tick Size Affect Stock Prices? Evidence from the Tick Size Pilot Announcement of the Test Groups and the Control Group*, Salil Pachare and Ilia Rainer (November 2018). Available at https://www.sec.gov/files/dera_wp_does_the_tick_size_affect_stock_prices.pdf

Footnote 13 of the DERA study further specifies that:

> In a robustness check, we also conduct our analysis for stocks with pre-Pilot quoted spreads smaller than $0.03 and find that our results remain robust.

Given the certainty of the spread increase in the Tick Pilot, this lack of price impact is telling. When considering potential harm to issuers, the price of their stock is the primary measure – if liquidity diminishes, or expected returns of the stock decline, this would be reflected in the value of the stock – and no such statistically significant decline in value was found. As the increase to spreads did not elicit an impact on the selected stocks in the Tick Pilot, this calls into question NYSE's allegation that a potential increase to spreads will somehow harm stock prices in the TFP.

Acceptance of and Reliance on Event Studies

The Supreme Court in *Basic v. Levinson*, 485 U.S. 224 (1988) approved the use of event studies to determine causation in the case of 10b-5 claims. Since *Basic*, many refinements to the Court's usage of event studies have occurred, which have generally advanced its usage for differing circumstances. As more recently described in *Bricklayers v. Credit Suisse*, 752 F.3d 82 (1st Cir. 2014):

> The usual — it is fair to say "preferred" — method of proving loss causation in a securities fraud case is through an event study, in which an expert determines the extent to which the changes in the price of a security result from events such as disclosure of negative information about a company, and the extent to which those changes result from other factors.

Given the Court's and the Commission's reliance on event studies, the Commission's consideration of DERA's Tick Pilot analysis as part of its evaluation of the TFP is warranted.

DERA's Multi-Firm Event Study

In fact, event studies that are routinely relied on to determine causation in 10b-5 cases—serious matters that involve substantial penalties and findings of fraud—are applied in the context of an event evaluating impact on a single firm's share price. From a statistical standpoint, the testing of an event that impacts multiple firms (holding all else constant) would increase confidence in the test as the risk of idiosyncrasies in a single firm event study could be identified.

In fact, prior to its application in 10b-5 matters, academics originally designed the event study methodology "to measure the effect of a single event across multiple firms, the effects of multiple events at a single firm, or the effects of multiple events at multiple firms."[2]

Here, DERA applied the study to a single event whose impact could be measured across multiple firms.[3] In this regard, the added confidence of the multi-firm study should increase the value of the DERA analysis relative to single-firm studies applied in 10b-5 matters.

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[2] The Logic and Limits of Event Studies in Securities Fraud Litigation, Fisch, Gelbach and Klick, Penn Law: Legal Scholarship Repository (2018) at p. 557. Available at https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2656&context=faculty_scholarship

[3] See id.

The Short Duration of Event Studies

Finally, it is worth noting that event studies, by their design, depend on the price adjustments that result from a specific informational event. The studies are typically short in duration because markets rapidly incorporate new information.[4] NYSE fully understands the rapid pace by which information is reflected in stock prices – hence their criticism of the test for "spanning three trading days" is disingenuous.

DERA's analysis is directly informative to the Commission's evaluation of investor protection, efficiency, competition and capital formation in the Tick Pilot, and in the anticipated TFP,[5] and I applaud DERA for efficiently and creatively applying data generated from one pilot study to aid in analyzing a future pilot.

Sincerely,

J.W. Verret

cc: Honorable Jay Clayton, Chairman
Honorable Kara M. Stein, Commissioner
Honorable Robert J. Jackson, Jr., Commissioner
Honorable Hester M. Peirce, Commissioner
Honorable Elad L. Roisman, Commissioner
Brett Redfearn, Director, Division of Trading and Markets

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[4] *See* Lessons from Financial Economics: Materiality, Reliance, and Extending the Reach of Basic v. Levinson, Jonathan R. Macey, Geoffrey P. Miller, Mark L. Mitchell, Jeffry M. Netter. Available at https://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?referer=&httpsredir=1&article=2684&context=fss_papers

[5] *See* Business Roundtable v. SEC, 647 F 3d 1144 (2011).