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By Electronic Mail

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F. Street, N.E.
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Re: *Proposed Rule Change by BATS Exchange, Inc., as Amended by Amendment No. 1, to Replace Current Rule 20.6 (Obvious Error) with New Rule 20.6 (Nullification and Adjustment of Options Transactions including Obvious Errors); Release No. 34-73884; File No. SR-BATS-2014-067*

I. INTRODUCTION

Goldman Sachs & Co. ("Goldman Sachs") appreciates the opportunity to comment on the proposed rule change filed by BATS Exchange, Inc. ("BATS" or "Exchange")[1] regarding the adjustment and nullification of equity options transactions that occur on the Exchange (the "Proposed Rule"). The Proposed Rule would replace BATS Rule 20.6 entitled "Obvious Error," with new Rule 20.6, entitled "Nullification and Adjustment of Options Transactions including Obvious Errors." [2]

We agree it is essential to manage and mitigate the consequences of obviously erroneous transactions. In that regard, we support the goal and much of the substance of the Proposed Rule. We also believe that ensuring predictability in the case of substantial, widespread error – defined in the Proposed Rule as a Significant Market Event ("SME")

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1 *See* Securities Exchange Act Release No. 73884 (December 18, 2014), 79 FR 77557 (December 24, 2014) (SR-BATS-2014-067), http://www.gpo.gov/fdsys/pkg/FR-2014-12-24/pdf/2014-30127.pdf.

2 BATS filed Amendment No. 1 on December 17, 2014, which amended and replaced the Proposed Rule in its entirety. The SEC published notice of the Proposed Rule, as amended, in the Federal Register to solicit comments from interested persons.

remain the best solution and are the most important priority. We therefore hope the Securities and Exchange Commission ("Commission") will continue to work with national securities exchanges and other market participants to consider ways to prevent erroneous options transactions before they occur, such as through the use of a framework like the limit up/limit down ("LULD") plan that is already in place for the equities markets. That reform, among others, has served to enhance confidence in our markets by mitigating the negative effects of disruptive trading incidents.

II. IN THE CASE OF A SIGNIFICANT MARKET EVENT ALL OBVIOUS ERROR TRADES SHOULD BE NULLIFIED

The definition of an SME in the Proposed Rule would establish a set of predetermined criteria under which options trades in a widespread market event would be reviewed by BATS as potentially erroneous. Specifically, Proposed Rule 20.6(e) would establish that a market event constitutes an SME if the transactions that are potentially erroneous on the Exchange and all other options exchanges with affected transactions result in a worst-case adjustment penalty, as computed under the rule, of $30 million or more.[3] Options trades on the Exchange and other affected options exchanges during a market event would also constitute an SME if, more broadly and in the aggregate, the potentially erroneous transactions satisfy certain percentage thresholds in relationship to four criteria: (1) a worst-case adjustment penalty of at least $30 million; (2) the transactions that are potentially erroneous involve over 500,000 options contracts; (3) the transactions that are potentially erroneous have a notional value of more than $100 million; and (4) there are more than 10,000 transactions that are potentially erroneous. We generally support the proposed approach for determining whether an SME exists. However, amendments to the Proposed Rule can and should be made to ensure that if an SME occurs BATS and other impacted exchanges will immediately nullify all affected trades.

The current Proposed Rule provides that unless the parties to a trade that is determined to be an obvious error during an SME agree to adjust the trade to a different price or nullify it, the trade would go through a process of evaluation and adjustment using parameters fixed by the Proposed Rule.[4] Moreover, if BATS, in consultation with other affected options exchanges, determines that timely adjustments are not feasible, because of the extraordinary nature of the

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3 *See* Proposed Rule 20.6(e)(1)(A). The worst-case adjustment penalty is computed as the sum, across all potentially erroneous trades, of: (i) $.30 (i.e., the largest transaction adjustment value listed in Proposed Rule 20.6(e)(3)(A)); multiplied by (ii) the contract multiplier for each traded contract; multiplied by (iii) the number of contracts for each trade; multiplied by (iv) the appropriate size adjustment modifier for each trade, if any, as defined in Proposed Rule 20.6(e)(3)(A).

4 An exception would permit the obvious error to be nullified if at least one party is a "customer" and the adjustment results in an execution price compared to the customer's limit price that would be higher for purchases or lower for sales. The term customer is defined to exclude a broker-dealer and any person or entity that is not a securities broker-dealer but who places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s).

SME, BATS would retain discretion to evaluate whether to nullify or adjust some or all trades that are determined to have arisen from the SME, regardless of whether they qualify as obvious errors.[5]

Calibration of the SME criteria to substantial and uncommon errors is a compelling reason why all affected transactions should be nullified immediately when an SME has occurred. Giving market participants certainty in that outcome during such a disruption would allow affected parties to immediately and definitively cap their related risks, and it would promote timely and final remediation of the event. By contrast, the proposed structure injects unnecessary delay and higher risk of residual economic harm to affected market participants. As a result, the efficacy of the Proposed Rule's improvements will be diminished if objective metrics clearly support that an event as severe as a SME has occurred and BATS and other affected options exchanges then take additional time to evaluate trades. During that period of uncertainty, market participants will not know their actual risk exposures, and we believe that such a lack of certainty risks increasing the severity of a market disruption. Therefore, the more appropriate solution is to immediately nullify all trades affected by the SME.

III. PREVENTION OF ERRONEOUS TRADES CONTINUES TO BE THE MOST OPTIMAL SOLUTION

The Proposed Rule represents a significant improvement in mitigating the impact of obviously erroneous transactions, and we encourage the Commission and the national securities exchanges to continue working toward what we believe will be an even more robust improvement: the establishment of pre-trade controls preventing erroneous trades before they happen. Since the "Flash Crash" market events of May 6, 2010, Goldman Sachs has consistently advocated for market structure reforms that we believe would improve the safety and integrity of the U.S. securities markets and for mechanisms designed to provide the ultimate safeguard, the prevention of erroneous trades.[6] An improved safety net of controls designed to reduce the frequency and magnitude of market disruptions could incorporate many tools, including a LULD

5 *See* Proposed Rule 20.6(e)(4).

6 *See* Goldman Sachs & Co. June 25, 2010 Letter to E. Murphy re: Concept Release on Equity Market Structure, http://www.sec.gov/comments/s7-02-10/s70210-243.pdf. ("[p]reventing erroneous trades before they occur with solutions such as price collars and short pauses to attract liquidity before a price decline escalates (i.e., a limit down model) would help to mitigate [concerns related to obvious errors]"); Joseph M. Mecane et. al. September 28, 2012 Letter to E. Murphy re: Technology and Trading Roundtable, http://www.sec.gov/comments/4-652/4652-17.pdf (recommending that exchange rules on clearly erroneous transactions be modified to better fit into a LULD framework and that "the clearly-erroneous execution rules must remain metric-based, and any movement to discretion around clearly erroneous determinations would lead to lack of certainty that would increase the likelihood and severity of market disruptions"); Gary Cohn, The Responsible Way to Rein in Super-Fast Trading, *The Wall Street Journal*, March 20, 2014 (advocating a stronger safety net of controls to reduce the frequency and magnitude of market disruptions).

solution for the listed options market and market-wide requirements that exchanges implement robust kill switches designed to detect and minimize severe trading system malfunctions. Without such pre-trade controls, today's markets will continue to operate with levels of speed and complexity that are unsupported by commensurate safeguards.

IV. CONCLUSION

We continue to believe that the primary emphasis in handling obvious error trades should be on stopping them before they occur. At the same time, we recognize that even with very robust pre-trade risk controls there will always be some risk that erroneous transactions and market disruptions will occur from time to time. We therefore applaud the Proposed Rule as a complement to the importance of continued efforts in the area of pre-trade risk controls and support the efforts of BATS to harmonize exchange rules regarding the adjustment and nullification of erroneous options transactions.

As explained, we also firmly believe it is important to modify the Proposed Rule to eliminate discretion in the event of an SME and rather dictate the prompt nullification of all SME related options transactions. With this change, the Proposed Rule will significantly improve the ability of market participants to understand and manage their risk exposures on an ongoing basis and will avoid unnecessary delays and uncertainty that potentially would exacerbate a market disruption.

Sincerely,

Paul M. Russo
Managing Director
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