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November 3, 2017

VIA E-MAIL

Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C., 20549-1090

Re: Securities Exchange Act Release No. 80683 (May 16, 2017), 82 FR 23320 (May 22, 2017) (SR-BatsBZX-2017-34) (the "BZX Proposal")

Dear Mr. Fields:

NYSE Group, on behalf of New York Stock Exchange LLC ("NYSE"), NYSE Arca, Inc. ("NYSE Arca"), and NYSE American LLC ("NYSE American"), appreciates the opportunity to provide additional comments to the Securities and Exchange Commission ("Commission") on the above-referenced proposed rule change by Bats BZX Exchange, Inc. ("BZX") to add a "BZX Market Close."

NYSE Group previously commented on the BZX Proposal and explained why it believes it is not consistent with the Securities Exchange Act of 1934, as amended ("Exchange Act") and the Commission's rules thereunder.<sup>1</sup> As the NYSE Group explained in its letters, the primary listing exchanges are required to support the technology and regulatory costs associated with running a closing auction and establishing an official closing price; to approve the use of this price by another exchange, which bears none of the costs or risks associated with the closing auction process, would be an unfair burden on competition.<sup>2</sup>

BZX seems to believe that repeatedly stating false assumptions somehow makes them true. This letter supplements NYSE Group's earlier comment letters with additional data and responds to certain points raised by BZX in its most recent response to comment letters.<sup>3</sup>

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<sup>1</sup> See Letters from Elizabeth K. King, General Counsel and Corporate Secretary, NYSE, to Brent J. Fields, Secretary, Commission, dated June 13, 2017 and August 9, 2017.

<sup>2</sup> 15 U.S.C. 78f(b)(8).

<sup>3</sup> See Letter from Joanne Moffic-Silver, Executive Vice President, General Counsel, and Corporate Secretary, Bats Global Markets, a CBOE Company, to Brent J. Fields, Secretary, Commission, dated October 11, 2017. See also Letter from Joanne Moffic-Silver, Executive Vice President, General Counsel, and Corporate Secretary, Bats Global Markets, Inc., to Brent J. Fields, Secretary, Commission, dated August 2, 2017.

### **A. BZX Failed to Provide Any Meaningful Data In Support of its Proposal**

In the Order instituting proceedings to determine whether to approve or disapprove the BZX Proposal (the “Order”), the Commission solicited comments on a number of the issues that NYSE Group and other commenters raised about the BZX Proposal.<sup>4</sup> Importantly, in soliciting comments, the Commission requested data, analyses, or studies. For example, the Commission requested “[w]hat analyses of available data could provide information about relationships between information disseminated during closing auctions, trading strategies in closing auctions, and closing prices.” In connection with trading volume that is already on venues other than the primary listing exchanges, the Commission asked “[h]ow does that volume impact the closing auction process on each of the primary listing exchanges.” Likewise, the Commission asked “[w]ould the proposal affect the existing level of fragmentation in the market? If so, how?”

Tellingly, BZX has not responded to these questions with any data. Instead, BZX structures its letter as a response to each of the comments that the Commission has solicited, but then populates its responses with repetition of its unsubstantiated assertions. For example, in response to the Commission’s question regarding the impact of the BZX Proposal on price discovery, BZX resorts to reiterating its claim that its proposal would avoid any impact on price discovery. BZX fails to respond to the Commission’s request for “analyses of available data” to support this claim.

In NYSE Group’s first letter, it provided data<sup>5</sup> and real-world examples of how the BZX Proposal would have an impact on the validity and integrity of the closing price and specifically how the closing price would be different if the market orders intended for the close were directed away from the primary listing exchange. That data regarding the potential negative impact on closing prices of the BZX Proposal cannot be ignored and BZX has provided no data that refutes it.

Likewise, in response to the Commission’s question regarding the effect the proposal would have on market complexity and/or operational risk, BZX simply says it would not have an impact because market participants would not be required to send their orders to BZX. However, the relevant question regarding complexity to the market is not whether it is optional to send market orders to the Bats Market Close, but rather, how the mere existence of the Bats Market Close, and the expected similar offerings of other exchanges, would increase complexity and thus operational risk across the market.

BZX does not dispute the value to market participants of knowing the volume of paired shares that would participate in the Bats Market Close. This is why BZX proposes to include such information in the Bats Auction Feed. But the need to subscribe to and ingest information from

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<sup>4</sup> See Securities Exchange Act Release No. 81437 (August 18, 2017), 82 FR 40202 (August 24, 2017) (SR-BatsBZX-2017-34).

<sup>5</sup> Specifically, for the first six months of 2017, NYSE Group identified 130 instances on NYSE Arca when the official closing price of a security was based on paired-off MOC order volume and, therefore, would have been different if all paired-off MOC order volume were to be removed from the primary listing exchange.

multiple data feeds to ascertain the volume in the close is itself is an unnecessary complexity. As the NYSE Group previously noted, while sophisticated market participants with large investments in technology would be able to adapt to this structure, it would place other market participants, which may not subscribe to multiple proprietary data feeds, at a disadvantage. The complexity would be further compounded when additional exchanges offer similar functionality because even sophisticated market participants would have to stitch the market back together.

## **B. Fragmentation at the Close Leads to Increased Volatility**

The only data that BZX offered in its latest comment letter is how much closing volume already occurs in off-exchange venues. BZX illustrates how, in 2017, there has been an increase in off-exchange matching of orders at the official closing prices of the primary listing exchanges. NYSE Group does not dispute this trend. In some ways, these existing off-exchange crossing mechanisms function similarly to the BZX Proposal. Specifically, broker-dealers that offer this off-exchange service receive orders from their customers that want to trade at the closing price and do not route to the primary listing exchange market orders that pair off or with which the broker-dealer chooses to trade against as principal. As with the BZX Proposal, the broker-dealers guarantee their customers the closing price in advance of the close, but unlike the BZX Proposal, frequently trade as principal with their customers' orders.

Regardless of whether it is an agency or principal trade, after the primary listing exchange establishes the closing price, these broker-dealers report the trades resulting from paired-off orders to a trade reporting facility ("TRF") at the closing price established by the exchange. As described below, such off-exchange matching of orders at the official closing prices of the primary listing exchanges already has a negative impact on the validity and integrity of price discovery in the closing auctions. However, unlike the BZX Proposal, the Commission is not required to find that such off-exchange broker-dealer activities are consistent with the Exchange Act and, thus, this existing fragmentation does not support a finding that BZX's Proposal, which would contribute further to the fragmentation at the close, is consistent with the Exchange Act.

Moreover, while BZX provides data on the volume of off-exchange matching of orders at the official closing prices of the primary listing exchange, it does not analyze the negative impact of that existing fragmentation on volatility leading into the close and on closing prices. In this regard, NYSE Group reviewed closing auctions with large imbalances and segmented those auctions based on the share of total volume at the official closing price that has been reported to a TRF. The data show that for those securities with low closing volume (i.e., 1,000 shares or less reported at the official closing price on and off-exchange), volatility in the last 10 minutes of trading leading into the close is 52% higher when more than 75% of a security's closing share volume is reported to a TRF than when less than 25% of a security's closing share volume is reported to a TRF.

NYSE Group's data also show that the move of closing auction volume off-exchange impacts the closing price. Specifically, the official closing price is more than twice as far away from the last consolidated sale price for securities with 1,000 shares or less reported at the official closing price when more than 75% of a security's share volume is reported to a TRF. To take account for last-sale price anomalies, NYSE Group also looked at the VWAP leading in to the close, and similarly found that for securities with 1,000 shares or less reported at the official

closing price, the closing price is nearly twice as far away from the market VWAP of the last two minutes of trading leading into the close.

The same degradation in quality of the official closing price also occurs in closes with larger volumes, i.e., 10,000 shares or more reported at the official closing price on exchanges and TRFs, when more than 75% of the total closing volume prints to the TRF. The following chart illustrates these points:

Closing Auctions of 1,000 Shares or Less, Jan Sep 2017*	75% or More Printed at TRF	25% or Less Printed at TRF	Difference
Closing Price Slippage from Last Sale	33.3 bp	16.21 bp	105.6%
Closing Price Slippage from 2-Minute Market VWAP	31.5 bp	16.0 bp	96.5%
Ratio of last 10 minute trading range to regular hours trading range	38.6%	23.8%	62.1%
Trading range in the last 10 minutes.	37.9 bp	30.5 bp	24.3%

  

Closing Auctions of 10,000 Shares or More, Jan Sep 2017*	75% or More Printed at TRF	25% or Less Printed at TRF	Difference
Closing Price Slippage from Last Sale	8.2 bp	6.5 bp	25.5%
Closing Price Slippage from 2-Minute Market VWAP	8.8 bp	7.6 bp	15.0%
Ratio of last 10 minute trading range to regular hours trading range	19.8%	16.1%	23.4%
Trading range in the last 10 minutes	38.3 bp	34.0 bp	12.7%

*\*Auctions with imbalances of 50% of paired shares as of 3:50 PM*

The NYSE Group's data illustrate the actual impact of existing fragmentation on the close. Given the negative impact of existing fragmentation on closing prices, the BZX Proposal is not consistent with the Exchange Act because it would not remove impediments to and perfect the mechanism of a free and open market and a national market system. Rather, the proposal would add impediments to the mechanism of a free and open market by contributing to volatility and price dislocation at the close, thus harming investors and the public, which includes the issuers whose stock prices would be negatively impacted by any further increase in fragmentation.

### **C. NYSE Arca Closing Auctions Are Not Designed To Compete with the Primary Listing Exchange Closing Auctions**

The Commission requested comment on whether the BZX Proposal would have a positive, negative, or neutral impact on competition. The Commission also asked for information regarding the current costs associated with a primary listing market developing and operating a closing auction, how the fixed costs associated with developing closing auctions compare to the variable costs of conducting closing auctions, to what extent those costs are passed on to market participants, and whether the BZX Proposal would impact the current fees charged by the primary listing markets for participation in their closing auctions.

In its previous comment letters, NYSE Group explained why the BZX Proposal would impose an unfair burden on competition because BZX would be selling an official closing price established by the primary listing exchanges without being required to support the technology and regulatory costs associated with running a closing auction and establishing an official closing

price. NYSE Group does not segregate the costs associated with building, testing, monitoring, or maintaining its closing auction process. Nor does NYSE Group distinguish the concept of “fixed” costs for developing auctions from “variable” costs for conducting its auction processes. However, the vast majority of costs are fixed costs associated with the development, testing, and maintenance of the closing auction and its interactions with other exchange functions. These costs do not vary based on the volume of orders sent to the closing auction.

Moreover, for the reasons enumerated in the NYSE Group’s prior comment letter, operating auctions is the most technologically complicated function of an exchange and therefore a significant portion of NYSE Group resources are spent on these functions, including the testing efforts associated with these complex functions. Simply put, these are costs that BZX would not have to bear. As NYSE Group previously explained, BZX would be able to offer the closing prices to its members at a lower fee than those offered by the primary listing exchanges because BZX does not have to expend the resources described in NYSE Group’s second comment letter to build, test, monitor, or maintain any of the complex systems involved in determining those closing prices. Thus, contrary to what BZX asserts, BZX would not be competing “based on execution quality, depth of liquidity, novelty and usefulness of innovative products, comprehensive platforms, as well as resilient technology.” Rather, BZX would be “competing” by selling what is already available, but at a price point at which the primary listing exchanges cannot realistically compete.

With respect to the Commission’s specific question regarding whether the BZX Proposal would have an impact on the current fees that are charged, it is premature to determine whether and how NYSE Group exchanges would revise fees in response to the BZX Proposal. As NYSE Group explained in its prior comment letters, NYSE already offers a tiered pricing schedule. What is clear, however, is that the BZX Proposal would not alter in any way the costs the NYSE Group exchanges bear to operate auctions. Because costs would not be changing, if one or more NYSE Group exchange were to reduce fees associated with the closing auction, which BZX claims is the stated goal of its proposal, there are likely to be other impacts on the overall fee structure of the exchange.

Instead of responding to the Commission’s question or NYSE Group’s previous comment regarding the burden on competition, BZX reiterated its argument that because NYSE Arca runs a closing auction in non-primary securities, BZX should similarly be approved to sell the official closing price of the primary listing exchange. This statement is based on the false equivalence BZX makes between the NYSE Arca closing auction process and the BZX Proposal. Both the NYSE Arca and Nasdaq closing auctions for non-primary securities are independent, price-discovery auction events. This is a distinction understood by NYSE’s issuers contrary to inflammatory assumptions made by BZX. Neither the NYSE Arca nor the Nasdaq closing auctions for non-primary securities use the official closing price established by the primary market as BZX proposes and, thus, do not impose an undue burden on competition by re-selling the primary listing exchange’s official closing price at a lower cost without making the same investment to create that price. NYSE Arca’s and Nasdaq’s closing auctions for non-primary securities create their own closing prices, which are only used as the official closing price in the event that the primary market does not have an official closing price.

BZX also claims that the NYSE Arca closing auction for non-primary symbols contributes to fragmentation at the close. However, the data do not support this claim. For the period January

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1, 2017 through October 13, 2017, as detailed in the Appendix, closing auctions in NYSE-listed and Nasdaq-listed securities on NYSE Arca represent just 0.05% of the notional value traded in the primary auctions at NYSE and Nasdaq.

Consistent with the purpose of its non-primary closing auctions – i.e., to serve as a back-up facility – NYSE Arca actively discourages order flow sent to NYSE Arca for non-primary auctions. NYSE Arca staff monitor order flow directed for such auctions and on multiple occasions, have reached out to ETP Holders that have entered large auction orders and advised them to cancel such orders and redirect them to the primary listing exchange.

As noted in NYSE Group's earlier comment letters, NYSE Arca began offering closing auctions in non-primary securities in August 2016 to provide an alternative to market participants in the event that NYSE, NYSE American, Nasdaq, or BZX is unable to conduct a closing auction in some or all of their listed securities. NYSE Arca does not otherwise have a business interest in running closing auctions in non-primary securities. The resiliency function the NYSE Arca non-primary auctions serve outweighs the modest negative impact of fragmentation given their limited use.

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For the foregoing reasons and the reasons set forth in its earlier comment letters, as well as the dozens of opposing comment letters from concerned listed companies, investors, and index providers, NYSE Group respectfully requests that the Commission disapprove the BZX Proposal.

Sincerely,



Elizabeth K. King

cc: Hon. Jay Clayton, Chairman  
Hon. Michael Piwowar, Commissioner  
Hon. Kara Stein, Commissioner  
Brett Redfearn, Director, Division of Trading and Markets  
Gary Goldsholle, Deputy Director, Division of Trading and Markets  
David Shillman, Associate Director, Division of Trading and Markets

**Appendix**

Notional Value Traded in NYSE Arca Non Primary Auctions						
Month	Notional Value Traded in NYSE Arca's Non Primary Auctions	Notional Value Traded in Primary Auctions	Avg Daily Notional Arca	Avg Daily Notional Primary	Arca % of Primary	Notional
Jan-17	\$145,249,286	\$302,385,186,809	\$7,262,464	\$15,119,259,340		0.05%
Feb-17	\$125,975,225	\$287,004,895,292	\$6,630,275	\$15,105,520,805		0.04%
Mar-17	\$140,126,223	\$409,965,375,695	\$6,092,444	\$17,824,581,552		0.03%
Apr-17	\$128,316,018	\$280,430,739,259	\$6,753,475	\$14,759,512,593		0.05%
May-17	\$148,058,047	\$341,506,456,641	\$6,729,911	\$15,523,020,756		0.04%
Jun-17	\$239,669,141	\$477,445,343,689	\$10,894,052	\$21,702,061,077		0.05%
Jul-17	\$119,677,288	\$326,000,174,235	\$5,983,864	\$16,300,008,712		0.04%
Aug-17	\$181,391,857	\$340,726,785,283	\$7,886,602	\$14,814,208,056		0.05%
Sep-17	\$279,775,810	\$414,158,105,400	\$13,988,790	\$20,707,905,270		0.07%
Oct-17	\$116,345,418	\$154,969,667,642	\$11,634,542	\$15,496,966,764		0.08%
Total Through 10/13	\$1,624,584,313	\$3,334,592,729,947	\$8,204,971	\$16,841,377,424		0.05%