



July 26, 2016

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

RE: SR-BatsBYX-2016-17, SR-BatsBZX-2016-29, SR-BatsEDGA-2016-15, SR-BatsEDGX-2016-26

Dear Ms. Murphy:

Bats Global Markets, Inc. (“Bats”) submits this letter in connection with the above-referenced proposed rule changes in which Bats BYX Exchange, Inc. (“BYX”), Bats BZX Exchange, Inc. (“BZX”), Bats EDGA Exchange, Inc. (“EDGA”), and Bats EDGX Exchange, Inc. (“EDGX”) (collectively, the “Exchanges”) proposed to amend their rules to describe system and functionality changes necessary to implement the Regulation NMS Plan to Implement a Tick Size Pilot Program (“Plan” or “Pilot”).¹ The above proposals were published for public comment on July 14, 2016.² Bats believes it must submit a comment letter for its own proposal because in the Releases, the Commission Staff stated its concern that the proposed rule changes may not be consistent with the Act and the Staff included provocative statements as part of its solicitation of comments that misrepresents the intent of the proposed rule changes in what appears to be an attempt by Commission staff to bias prospective commenters against the proposed rules changes. Bats disagrees with the Commission Staff’s statements and submits this letter to correct the record.

The Commission Staff asserts that the proposals to not accept Market Pegged Orders, Discretionary Orders, Supplemental Peg Orders, and certain types of Mid-Point Peg Orders, in some or all Test Groups of Pilot Securities “appear designed to permit the Exchange to avoid the costs of modifying [certain] . . . order types to comply with the Plan.” By contrast, the Commission Staff asserts that the proposals by the Exchanges to accept with modifications Market Pegged Orders, Non-Displayed Orders, and certain orders subject to the Display-Price Sliding process, evidence that the Exchanges are willing to incur costs to make programming modifications for Pilot Securities where doing so will increase opportunities for executions. The clear implication of these statements, of course, is that Commission Staff believe the Exchanges are willing to incur costs associated with modifications to its system where it may result in

¹ See Securities Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27513 (May 13, 2015) (“Approval Order”).

² See Securities Exchange Act Release Nos. 78333 (July 14, 2016) (SR-BatsBYX-2016-17); 78334 (July 14, 2016) (SR-BatsBZX-2016-29); 78330 (July 14, 2016) (SR-BatsEDGA-2016-15); and 78331 (July 14, 2016) (SR-BatsEDGX-2016-26) (the “Releases”).

greater execution opportunities, but unwilling to do so when that is not the case. This belief suffers from the fundamental defect of being completely false and unsupported by the record.

At the outset, Bats wishes to make clear that the proposed changes are all reasonably designed to comply with the Pilot. Nothing about the proposed changes would cause Bats to be out of compliance with any aspect of the Pilot. What is at issue here is Bats' proposal to not accept certain order types in the Pilot that are already lightly used in the securities subject to the Pilot and that would require significant modifications to Bats systems' to support the quoting and trading requirements of the Pilot that Bats believes would create an unacceptable level of systemic risk to the Bats matching engine. After undergoing a lengthy review of the systems changes required to support the order type functionality at issue, Bats engaged in several discussions with Commission Staff leading up to the filing of these proposed rule changes in which Bats technologists repeatedly expressed concerns about the systemic risks of supporting this order type functionality in Pilot Securities. Bats reiterated these concerns in the current rule proposals. Not once in the several conversations with Commission Staff or in the rule proposals has Bats ever expressed concerns about the costs of implementation. For Commission Staff to suggest otherwise in its provocative solicitation of comments is, frankly, disingenuous and not supported by the record.

The Commission Staff is concerned that the proposed rule changes to eliminate certain order types in certain Pilot Securities could "have a disparate impact on different Test Groups and the Control Group" and "could bias the results of the Pilot and undermine the value of the data generated in informing future policy decisions". In short, the Commission Staff and its economists want to ensure that the data is pure. As a result, the Commission Staff is balancing the purity of data in the Pilot against the complexity of the market to implement the Pilot. Unfortunately and ironically, the Commission Staff has chosen that purity of data is more important than system risk and market complexity.

The Commission Staff's statements fail to recognize the complexity of the numerous system changes necessary to comply with the Plan and the systemic risk created by such complexity. In determining the scope of these proposed changes, Bats carefully weighed the impact on the Pilot, system complexity, and the usage of such order types in Pilot Securities. The proposed changes are designed to directly comply with the Plan and to assist Bats in meeting its regulatory obligations pursuant to the Plan. The Exchanges also determined that the proposed changes are necessary to ensure continued system resiliency in accordance with the requirements of Regulation SCI.³ Certain of these changes are also intended to reduce risk in the system by eliminating unnecessary complexity, and Bats has submitted data to the Commission Staff demonstrating the infrequent usage of the order types at issue in the universe of securities from which the Pilot Securities will be chosen, as well as in some cases the limited ability of these order types to even execute under the Pilot's Trade-at Prohibition. The rule proposals thoroughly discuss the impact on system complexity, limited execution scenarios, and Bats

³ See Securities Exchange Act Release No. 73639 (November 19, 2014), 79 FR 72251 (December 5, 2014) ("Regulation SCI Approval Order").

provided statistics evidencing current limited usage of the order types it proposes to modify or eliminate.⁴

The Commission Staff's statements that such changes could bias the results of the Pilot is based on nothing other than mere conjecture, and on their face appear to be completely unfounded, again based on the data submitted by the Exchanges demonstrating the limited usage of these order types in the securities at issue. And, importantly, not once in Bats' discussions with Commission Staff did the Staff involve a Commission technologist who may have better understood the systemic risk described by Bats' technologists. In addition, Section IV of the Plan simply requires the Exchange to adopt procedures that are **reasonably designed** to comply with the requirement of the Plan, as these proposed rule changes are intended to enable Bats to do, while protecting exchange systems from complexity that arises from implementing the Pilot with respect to a limited number of infrequently used features.

But, there is a more fundamental question at stake in these proposed rule changes and the Commission Staff's clearly evidenced bias to disapprove them: to what extent does the Commission Staff have the authority to dictate the order types an exchange can choose to discontinue? It is indisputable that an exchange has the discretion to discontinue order types out of concern for system complexity or for any other reason in the absence of the Pilot. In fact, in 2014 the Commission Staff found that eliminating order types to reduce systems complexity was consistent with Section 6(b)(5) of the Act.⁵ The Commission Staff's provocative solicitation of comments in the current case suggests it may now believe the opposite, which in turn suggests there are no limiting principles to Section 6(b)(5) of the Act and that it can instead be read to suit any outcome the Commission Staff desires.

During our discussions with Commission Staff, Bats attempted to accommodate the Staff's concerns about potential data biases to the Pilot and Bats agreed not to propose certain other changes that also would have reduced systems complexity. Bats attempted to accommodate these concerns, not because Bats believed that the Pilot would be biased if we didn't, nor because we believed Commission Staff had the statutory authority to dictate the order types offered in the Pilot, but because Bats was attempting to work cooperatively with its regulator. In fact, in the original proposal, Bats had planned not to accept Non-Displayed orders in Pilot Securities subject to the Trade-at prohibition. Bats ultimately capitulated to the

⁴ The Releases describe the complexity of the proposed changes and provided detailed descriptions of the limited execution scenarios created by the Plan. *Supra* note 2. The Releases include the following statistics: during March 2016, the alternative pegging functionality of Mid-Point Peg Orders, Market Pegged Orders, and Supplemental Peg Orders accounted for 0.01%, 0.02%, and 0.01%, respectively, of volume in eligible Pilot Securities on the BYX, BZX, EDGA and EDGX combined. Discretionary Orders accounted for 0.00% of volume in eligible Pilot Securities on the BYX, BZX, EDGA and EDGX combined. *Id.*

⁵ *See* Securities Exchange Act Release No. 72942 (August 28, 2014), 79 FR 52784 (September 4, 2014) (SR-NYSEArca-2014-75) (evidencing the Commission Staff's view that Section 6(b)(5) of the Exchange Act includes no limiting principles with regard to the elimination of order types or a reduction in system complexity).

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Commission Staff and agreed to accept Non-Displayed orders with the modifications outlined in the rule proposals – a fact the Commission Staff not only now conveniently ignores, but instead turns on its head in the Releases as evidence that the Exchanges are willing to incur the costs of making those changes because it will increase execution opportunities.

The remaining changes that make up the substance of the current proposals reflect those that Bats' technologists have concluded present the greatest risk to its systems and, as has been demonstrated to the Staff, are virtually unused today in the universe of securities that will be the subject of the Pilot. If the Commission Staff wanted to dictate order types that should be supported as part of the Pilot, it could have engaged in full Commission rule-making to achieve that end rather than implementing the Pilot as a National Market System Plan under Rule 608 of Regulation NMS. It did not do so, and the Exchanges do not believe the Commission Staff have the authority under the Act to deny the proposed rule changes, which the Exchanges believe promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, protect investors and the public interest in accordance with Section 6(b)(5) by reducing system complexity and enhancing system resiliency, while not adversely affecting the data collected under the Plan.

Bats supports the Pilot and its goal of assisting the Commission, market participants, and the public in studying and assessing the impact of different quoting and trading increments on the liquidity and trading of stocks of small capitalization companies. Bats appreciates the opportunity to submit this comment letter and looks forward to working constructively with Commission Staff on completing the remaining steps necessary to implement the Pilot, including the proposed rule changes.

Please feel free to contact me if you have any questions related this matter.

Sincerely,



Eric Swanson
General Counsel

cc: Steve Luparello, Director, Division of Trading and Markets