



March 11, 2013

By Electronic Mail (rule-comments@sec.gov)

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Re: File Numbers SR-NYSE-2013-08; SR-NYSEMKT-2013-07; SR-BYX-2013-008;
and SR-NASDAQ-2013-031

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates the opportunity to respond to the request for comment by the U.S. Securities and Exchange Commission (“Commission”) on the above-referenced proposed rule changes filed by the New York Stock Exchange LLC (“NYSE”), NYSE MKT LLC (“NYSE MKT”), BATS-Y-Exchange, Inc. (“BYX”), and the Nasdaq Stock Market LLC (“NASDAQ” and together with NYSE, NYSE MKT, and BYX, the “Exchanges”) under Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Exchange Act”). NYSE, NYSE MKT, BYX, and NASDAQ propose to amend the attestation requirement of NYSE Rule 107C, NYSE MKT Rule 107C, BYX Rule 11.24, and NASDAQ Rule 4780 respectively, to allow participants to attest that “substantially all” orders submitted to the “Retail Liquidity Program” (“RLP” or the “Programs”) will qualify as “Retail Orders.”² In this context, we bring to the Commission’s attention that SIFMA member firms represent the majority of retail order flow executed in the United States today.

¹ SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA’s mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (“GFMA”). For more information, visit www.sifma.org.

² See Securities Exchange Act Release No. 68747 (January 28, 2013), 78 FR 7824 (February 4, 2013) (“NYSE RLP Amendment Proposal”); see also Securities Exchange Act Release No. 68746 (January 28, 2013), 78 FR 7842 (February 4, 2013) (“NYSE MKT RLP Amendment Proposal”); see also Securities Exchange Act Release No. 68975 (February 25, 2013) (“BYX RLP Amendment Proposal”); see also Securities Exchange Act Release 69039 (March 5, 2013) (“NASDAQ RLP Amendment Proposal”).

I. Introduction

As originally approved by the Commission, the Programs are intended to attract additional retail order flow to the Exchanges while also providing price improvement through sub-penny pricing. The Programs each create a new class of market participants: Retail Member Organizations (“RMOs”). In order to qualify as an RMO, a participant is required to submit an attestation to the Exchange that “any” order flow submitted would qualify as a “Retail Order.”³ These Programs were approved on a pilot basis by the Commission staff acting pursuant to delegated authority.⁴

Among the issues that the Commission had to consider in approving the RLPs was the definition of “Retail Member Organization.” In order to qualify as an RMO and participate in the Program, an Exchange member organization “must conduct a retail business or handle retail orders on behalf of another broker-dealer.” Furthermore, the Exchanges asserted that they would “require a Retail Member Organization to have written policies and procedures in place to assure that *only* bona fide retail orders are designated as such.”⁵

The original scope of what qualified as a “Retail Order” eligible for participation in the proposed Programs received a great deal of consideration by the Commission and commenters. As the Commission is aware, at the time these rule proposals were submitted for approval, SIFMA raised a number of issues regarding the Programs’ definition of “Retail Order.”⁶ For example, to qualify as a Retail Order, in addition to the requirement that orders be agency orders from a natural person submitted to the Exchanges by an RMO that are not modified, the orders cannot “originate from a trading algorithm or any computerized methodology.” As SIFMA noted in prior letters, this definition may be over- or under-inclusive, thus potentially discriminating against some retail orders depending on how they are submitted.

3 NYSE Rule 107C(b); NYSE MKT Rule 107C(b); BYX Rule 11.24(b)(2)(C); NASDAQ Rule 4780(b)(2)(C).

4 *See* Securities Exchange Act Release No. 67347 (July 3, 2012), 77 FR 40673 (July 10, 2012) (“NYSE RLP Approval”); *see also* Securities Exchange Act Release No. 67347 (July 3, 2012), 77 FR 40673 (July 10, 2012) (“NYSE MKT RLP Approval”); *see also* Securities Exchange Act Release No. 68303 (November 27, 2012), 77 FR 71652 (December 3, 2012) (“BYX RLP Approval”); *see also* Securities Exchange Act Release No. 68937 (February 15, 2013), 78 FR 12397 (February 22, 2013) (“NASDAQ RLP Approval”).

5 NYSE RLP Approval at 6,7 (Emphasis added.); *see also* NYSE MKT Approval at 7. Similarly, the BYX RLP Approval states that RMOs must have “written policies and procedures reasonably designed to assure that it will only designate orders as Retail Orders if all the requirements of a Retail Order are met.” (BYX RLP Approval at 6). *See also* NASDAQ RLP Approval at 7.

6 *See* Letters from Ann Vlcek Managing Director and Associate General Counsel, SIFMA to Elizabeth M. Murphy, Secretary, Commission dated December 7, 2011 and March 23, 2012, and Letter from Theodore Lazo, Managing Director and Associate General Counsel, SIFMA to Elizabeth M. Murphy, Secretary, Commission dated September 26, 2012.

In instituting disapproval proceedings for NYSE’s original proposal, the Commission found that the broad scope of the Exchanges’ proposed definition of “Retail Order” was problematic for a number of reasons. For example, the Commission noted that the proposed definition included “not only orders that originate from a natural person, but also broker-dealer proprietary orders that liquidate positions acquired from internalizing orders that originate from natural persons.”⁷ Because of this, the Commission found that “under these circumstances it is unclear whether the benefit of the sub-penny price improvement ultimately would reach the retail investors.” Further, the Commission found that the definition raised concerns as to whether the Proposals would “promote just and equitable principles of trade...[and] be in the public interest and consistent with the protection of investors.”⁸

In order to address the various concerns raised regarding the definition of “Retail Order,” the Exchanges narrowed the definition to an agency order that originates from a natural person and not a trading algorithm or any other computerized methodology.⁹ Retail Orders must be submitted by RMOs approved by the Exchanges, and RMOs must maintain written policies and procedures designed to ensure that only orders qualifying for the program are designated as Retail Orders.¹⁰ Based on these limitations, the Commission approved the Programs with the understanding that the standards for defining “Retail Orders” would be “sufficiently tailored to provide the benefits of potential price improvement *only to bona fide retail order flow* originating from natural persons.”¹¹

7 Securities Exchange Act Release No. 66346 (February 7, 2012), 77 FR 7628 (February 13, 2012).

8 *Id.*

9 The Exchanges now define a “retail order” as “an agency order that originates from a natural person and is submitted to the Exchange by a Retail Member Organization, provided that no change is made to the terms of the order with respect to price or side of market and the order does not originate from a trading algorithm or any other computerized methodology.” NYSE Rule 107C(a)(3); NYSE MKT Rule 107C(a)(3); BYX Rule 11.24(a)(2); NASDAQ Rule 4780(a)(2).

10 NYSE RLP Approval at 29; NYSE MKT RLP Approval at 29; BYX RLP Approval at 16; NASDAQ RLP Approval at 14.

11 NYSE RLP Approval at 28; NYSE MKT RLP Approval at 28; BYX RLP Approval at 16; NASDAQ RLP Approval at 13 (emphasis added).

II. The Exchanges Are Proposing a Change that Would Likely Undermine the Rationale for the Programs and the Corresponding Exemptions.¹²

The Exchanges now propose to broaden the definition of “Retail Orders” well beyond the scope that justified the original approval of the Programs and that resulted from significant discussion between the Commission, commenters, and the Exchanges. Specifically, the Exchanges seek to amend the attestation requirement to allow an RMO to attest that “substantially all” orders submitted to the RLP will qualify as a “Retail Order,” weakening the requirement from an attestation that “any order” submitted qualifies for participation in the Program. To the extent the amendments now proposed by the Exchanges expand the Programs’ reach beyond a retail audience, SIFMA strongly believes that the Commission should reevaluate the important market structure issues considered in determining to initially approve the Programs and the corresponding exemptions required for the Programs to operate and with regard to whether to extend the approval of the Programs in their current form beyond the one-year pilot period.

A. The Commission’s Approval of the RLP Proposals was Predicated on the Understanding that Programs Would be Limited to Retail Orders

SIFMA believes that the proposed amendments weakening the standard to allow some non-retail orders represents a material and problematic departure from the Programs originally considered by the Commission. The Exchanges’ requirement that RMOs attest that “any order” submitted to the RLP qualify as a “Retail Order” allowed the Commission to conclude that this strict standard “should help ensure that *only* retail order flow is submitted into the Program and thereby promote just and equitable principles of trade and protect investors and the public interest, while also providing an objective process through which members may become Retail Member Organizations or Retail Liquidity Providers.”¹³ In approving the Programs, the Commission determined that the possible benefit to retail order execution warranted exemptions from NMS rules governing fair access and subpenny pricing. To the extent that the Programs are

12 The Commission granted each Exchange a limited exemption from the Sub-Penny Rule to operate its RLP. See NYSE RLP Approval 32-35; NYSE MKT RLP Approval 32-35; BYX RLP Approval 20-23; NASDAQ RLP Approval 16-19. The Exchanges also requested that the staff of the Commission not recommend enforcement action under the Quote Rule relating to the kind of information disseminated through the Retail Liquidity Identifier. These requests were granted by the Commission. See Letter from David Shillman, Associate Director, Division of Trading and Markets, to Janet McGinness, Senior Vice President-Legal and Corporate Secretary, Office of the General Counsel, NYSE Euronext, dated July 3, 2012; see also Letter from David Shillman, Associate Director, Division of Trading and Markets, to Eric Swanson, Senior Vice President and General Counsel, BATS, dated November 27, 2012; see also Letter from David Shillman, Associate Director, Division of Trading and Markets, to Jeffrey Davis, Vice President and Deputy General Counsel, The NASDAQ Stock Market LLC, dated February 15, 2013.

13 NYSE RLP Approval at 29; NYSE MKT RLP Approval at 29. BYX RLP Approval at 16; NASDAQ RLP Approval at 14 (emphasis added).

not limited to retail order flow, the rationale for those exemptions appears to be undermined and must be reevaluated.

B. The Exchanges Have Not Provided Evidence to Support the Assertion that the Proposed Amendments Will Increase Retail Investor Access to the Programs

As justification for the proposed amendments, the Exchanges state that “certain significant retail brokers” are prevented from participating in the Program “due to operational constraints” and claim that weakening the attestation requirement will expand the access retail investors have to the Programs.¹⁴ However, the Exchanges have not provided sufficient explanation of why these brokers are unable to isolate retail orders from non-retail orders. Furthermore, it is unclear why, if RMOs cannot isolate all retail order flow they can, under the proposed standard, attest that “substantially all” of the order flow meets the retail standard. The Commission should require additional explanation and an analysis of the costs and benefits to RMOs of implementing the necessary technology to identify orders as retail. SIFMA further requests that the comment period be extended to allow for a discussion of firm capabilities in complying with the proposed amendment.

The Exchanges’ claim that a strict definition of “Retail Orders” prevents some retail brokers from participating in the Programs is undermined by examples of situations in which broker dealers must strictly comply with definitions of “customers.” For example, many exchanges have developed fee structures in which the rates charged distinguish between public and professional customers, a standard comparable to retail versus non-retail customers.¹⁵ The rules for these exchanges provide for different fees depending upon the type of customer submitting the order, and these rules have been strictly enforced.¹⁶ The Exchanges have not provided explanation for why broker-dealers are able to distinguish public from professional orders for options routing purposes, but not to determine qualifications to participate in the Programs.

14 NYSE RLP Amendment Proposal at 1; NYSE MKT RLP Amendment Proposal at 1; BYX RLP Amendment Proposal at 1; NASDAQ Amendment Proposal at 1. NYSE, NYSE MKT, and BYX explain in their proposals that the “categorical nature of the current attestation language is preventing certain Members with retail customers from participating in the Program,” and that “limitations in order management systems...make it infeasible...to isolate 100% of Retail Orders.” (NYSE RLP Amendment Proposal at 3; NYSE MKT RLP Amendment Proposal at 3; BYX RLP Amendment Proposal 4). The NASDAQ RLP Amendment Proposal does not include this limited explanation of why certain Exchange Members are unable to participate in the RLP Program.

15 *See, e.g.*, NYSE Amex Options Fee Schedule (available at http://www.nyse.com/pdfs/NYSE_Amex_Options_Fee_Schedule_CLEAN4.01.pdf); *see also*, BATS BZX Exchange Fee Schedule March 1, 2013 (available at http://cdn.batstrading.com/resources/regulation/rule_book/BZX_Fee_Schedule.pdf).

16 *See, e.g.*, NYSE Amex Rules 16, 324, 956NY(a) and NYSE MKT LLC Hearing Board Decision 12-NYSEMKT-6 (September 20, 2012).

C. The Proposed Amendments Create an Unworkably Vague Standard that Will Encourage an Increasingly Expansive Definition of Qualifying Order Flow

In addition to being a significant divergence from the original proposals, SIFMA is concerned that the “substantially all” standard proposed by the Exchanges is so vague that it could allow a material amount of non-retail order flow to qualify for the Programs. The Exchanges state that they are proposing a “de minimis relaxation” of the attestation requirement, but have not provided any guidance on what quantity or percentage of order flow may be non-retail. The already-present incentives to increase market share by loosening the standards of what constitutes retail order flow are exacerbated by the further weakening of the standards governing the percentage of order flow that must be retail in order to qualify for the RLP. SIFMA requests that, should the Commission approve the proposed amendment, it first establish a bright-line rule to define what constitutes “substantially all” retail order flow.¹⁷ In any event, the Commission should extend the comment period so that the industry may comment on appropriate minimums is necessary to prevent the proposed “relaxation” of the standard from opening the floodgates to non-retail order flow.

D. The Proposed Amendment May Increase Monitoring and Recordkeeping Inaccuracies

The Exchanges have asserted that they will monitor order flow from RMOs in order to verify that such order flow meets the characteristics of retail orders.¹⁸ However, this monitoring and recordkeeping may become exponentially more difficult when the Exchanges must not only identify non-retail order flow, but additionally determine whether such order flow is at a level beyond the permissible “de minimis” level. The difficulty of this process may increase the likelihood of unfair discrimination among members in the approval and disqualification process for participation in the RLP. The Commission should require the Exchanges to comply with rigorous monitoring, recordkeeping, and reporting obligations to ensure that the Programs are being administered on a consistent, non-discriminatory basis.

17 For example, a “de minimis” transaction has been defined in connection with a distribution of securities as “less than 2%.” 17 C.F.R. 242.101(b)(7).

18 See Letter to the Commission from Janet McGinnis, Senior Vice President, Legal & Corporate Secretary, Legal & Government Affairs, NYSE Euronext, dated January 3, 2012.

Ms. Elizabeth M. Murphy, Securities and Exchange Commission
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As noted in our prior letters, SIFMA supports and encourages the Exchanges to provide innovative products to investors. However, SIFMA believes that the implications of the proposals must be thoroughly considered before the amendments are approved to ensure the continued, proper functioning of our marketplace. SIFMA therefore urges a careful examination of how the proposed amendments impact the efficacy of the RLPs in achieving the stated policy goals.

SIFMA greatly appreciates the Commission's consideration of the issues discussed above in connection with the Exchanges' proposed amendment. SIFMA would be pleased to discuss these comments in greater detail with the Commission and the Staff. If you have any questions, please call me (at 202-962-7383 or tlazo@sifma.org) or Timothy Cummings (at 212-313-1239 or tcummings@sifma.org).

Sincerely,



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SIFMA

cc: Elisse B. Walter, Chairman
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