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TRADEBOOK LLC
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October 6, 2014

Via email: rule-comments@sec.gov

U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090
Attention: Mr. Brent J. Fields, Secretary

COMMENT LETTER AND PETITION FOR DISAPPROVAL

Re: **Response to NYSE Letter, Securities Exchange Act Release No. 72548 (July 7, 2014), 79 FR 40183 (July 11, 2014) (SR-NYSE-2014-32) ("Notice") and Securities Exchange Act Release No. 72547 (July 7, 2014), 79 FR 40169 (July 11, 2014) (SR-NYSEMKT-2014-56)**

Dear Mr. Fields:

Bloomberg Tradebook LLC ("Tradebook")[1] appreciates the opportunity to respond to New York Stock Exchange LLC's ("Exchange" or "NYSE") response letter[2] to the Securities and Exchange Commission ("Commission") regarding the Tradebook Comment Letter to the above-captioned Notice.[3] For the reasons set forth in the Tradebook Comment Letter and in this response to the NYSE Letter, Tradebook asserts that the Notice to make the Add Liquidity Only ("ALO") modifier available for limit orders and make the day time-in-force condition available for

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[1]   Bloomberg Tradebook LLC is a registered broker-dealer, operates an Alternative Trading System (ATS) registered with the SEC, is a member of FINRA, Inc., and is a wholly-owned subsidiary of Bloomberg L.P.

[2]   Letter from Martha Redding, Chief Counsel, New York Stock Exchange, LLC to Kevin M. O'Neill, Deputy Secretary, U.S. Securities and Exchange Commission, dated September 30, 2014 ("NYSE Letter").

[3]   Letter from Raymond M. Tierney III, President and Chief Executive Officer, and Gary Stone, Chief Strategy Officer, Bloomberg Tradebook LLC, to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission, dated September 22, 2014 ("Tradebook Comment Letter"). Additionally, NYSE's affiliated exchange, NYSE MKT LLC, submitted a virtually identical rule proposal on the same day as the Notice. See Securities Exchange Act Release No. 72547 (July 7, 2014), 79 FR 40169 (July 11, 2014) (SR-NYSEMKT-2014-56). The Commission extended its time to act on the Notice and the related NYSE MKT proposal to October 9, 2014. Following the Exchange's approach in having the NYSE Letter address both proposals, the Tradebook Comment Letter and this response are intended to contest both the Notice and related NYSE MKT proposal. The Tradebook Comment Letter has been attached hereto as an appendix.

Intermarket Sweep Orders ("Day ISO") is inconsistent with Section 6(b)(5) of the Securities Exchange Act of 1934 ("Exchange Act"). Tradebook therefore respectfully requests that the Commission disapprove the Notice and ensure that no exchange is improperly utilizing the Day ISO order type. This is a novel issue for the Commission, a matter of first impression, so the Commission should require that the necessary rule changes be filed so that they are subject to the notice and comment process and Commission review.

A. Day ISO is a Regulation NMS Concern

As a preliminary matter, Tradebook would like to emphasize the point that the Day ISO and Day ISO ALO are Regulation NMS concerns. At this point in time, the Exchange seeks to delay Commission review and analysis of the Tradebook Comment Letter regarding the order type because it claims that Tradebook "raises general questions regarding current equity market structure" but that the Exchange would "welcome discussion regarding current equity market structure in the appropriate forum." Day ISO is not a market structure issue – simply put, this order type(s) violates provisions of Regulation NMS. Thus, Commission review of the Notice is the appropriate forum to make a determination in this regard. Consistent with its mission to maintain fair, orderly, and efficient markets, the Commission should without delay appropriately address violations of Regulation NMS and enforce these marketplace rules of the road.

In fact, in 2004, Tradebook advocated against many parts of Rules 610 and 611.[4] As an example of a market structure proposal, if Tradebook now requested a lift on the locked and crossed markets ban, then the Exchange would be correct in that we would be raising a broad market structure issue. However, at this point in time, Tradebook is merely requesting that the Regulation NMS rules implemented by the Commission are being followed.

Further, consistent with the Tradebook Comment Letter, Tradebook requests that the Commission revisit its Regulation NMS Guidance with respect to this order type.[5] The Regulation NMS Guidance was issued before the practical implications of the workings of Regulation NMS could be assessed. Thus, the Notice presents the Commission with an opportunity to evaluate Regulation NMS market practices in light of the operation of the market.

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[4]   Regulation NMS, Exchange Act Release No. 34-51808 (June 9, 2005), 70 Fed. Reg. 37496 (June 29, 2005) ("Adopting Release") at 41, 43 (n. 61, 62, 64). During the comment process for Regulation NMS, Tradebook in 2004 provided statistics to show that locked and crossed markets and problems with order protection were infrequent events, and therefore, Rules 610 and 611 were not necessary.

[5]   See Commission Division of Trading and Markets, Responses to Frequently Asked Questions Concerning Rule 611 and Rule 610 of Regulation NMS, April 4, 2008 Update, available at: http://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm#sec3 ("Regulation NMS Guidance").

B. The Exchange's Competition Argument is Not Applicable

Tradebook agrees with NYSE's assertions that, "Because all other securities exchanges offer the order types the Exchange proposes, Commission disapproval of only NYSE's order type would be ineffective in addressing Tradebook's concerns because the order types would continue to be available on all securities exchanges, except the Exchange." Therefore, as noted in the Tradebook Comment Letter, Tradebook respectfully requests that the SEC provide guidance to the market – to all participants that currently employ the functionality – addressing the fact that this is not an acceptable order type. This is also consistent with the Exchange's request that these issues can only be addressed at a national level so that if any changes result, they would be applied uniformly across all trading venues.

The crux of the Exchange's argument for approval is that NYSE would be at a competitive disadvantage if the Notice were not approved. For example, the Exchange states, "Disapproval of the Exchange's proposal, therefore, would impose a different standard to the Exchange's Proposal than to its competitors, which would impose a burden on competition that is not necessary or appropriate in furtherance of the Act." However, this argument is not persuasive. The order type(s) should only be approved if the Commission finds it consistent with Regulation NMS. As stated in the Tradebook Comment Letter, "The unapproved use of the order type by other exchanges does not provide supporting evidence that the order type is proper."[6] Likewise, the unapproved use of the order type by other exchanges should not be the premise of a competition argument. Tradebook appreciates that NYSE is the only exchange to file with the Commission the necessary rule change for the Day ISO order type. Tradebook and NYSE both note that other exchanges' rules do not bother to address the existence or handling of the Day ISO, yet they utilize the order type anyway. The failure of other exchanges to obey the rules of the road does not argue for the Commission to waive the rules of the road. It argues for the Commission to enforce the rules of the road. That will protect the public and ensure exchanges that follow the rules are not disadvantaged.

In fact, the Commission in no uncertain terms stated the following in its Regulation NMS Guidance: "Regulation NMS neither requires a trading center to cancel immediately the unexecuted portion of an ISO nor prohibits it from doing so. To assure an immediate cancellation and response, order routers should use the IOC designation. Trading centers, in turn, will have the option of adopting rules requiring that the unexecuted portion of ISOs be immediately canceled. If, however, a trading center chooses *not* to cancel the portion of ISOs that cannot be executed immediately, **its rules will need to address appropriately** the

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[6]   See Tradebook Comment Letter. The Notice provides: "The rules of Nasdaq, BATS, BATS-Y, EDGA, and EDGX do not expressly provide that their versions of ISOs can be day, however, nor do their rules prohibit this functionality. In practice, Nasdaq, BATS, BATS-Y EDGA, and EDGX all accept ISOs with a day time- in-force condition."

subsequent handling of the unexecuted portions. For example, such rules would need to comply with the relevant SRO rule on the display of locking or crossing quotations (see FAQ 5.01 below). In addition, any subsequent execution would not qualify for the original ISO exception created by the initial routing of the ISO. The exception will expire after the ISO exhausts the liquidity that is immediately available at the trading center. Consequently, a subsequent execution of the remaining balance of an ISO must independently comply with Rule 611 (*e.g.*, by not trading through a protected quotation or newly qualifying for a Rule 611 exception)."[7] Tradebook respectfully requests that the Commission ensure the Regulation NMS Guidance is not selectively ignored by the other exchanges. All of the exchanges operating in the marketplace should be doing so pursuant to the rules and guidance.

Further, the Commission has *not* found the same order types when proposed by other exchanges to be consistent with the Exchange Act. The only precedence NYSE states for this proposition is NYSE Arca Equities, Inc.'s 2006 proposal ("Arca 2006 Proposal"),[8] a proposal that does not propose the same order type(s) as those proposed in the Notice,[9] and even more importantly, a proposal that was adopted and approved before Regulation NMS even went into effect.[10] Thus, this is a novel issue for the Commission, a matter of first impression. The Notice presents the Commission with the unique opportunity to assess this order type, particularly in light of the serious concerns that are highlighted in the Tradebook Comment Letter. Neither the Exchange nor the Commission had the opportunity to review these concerns because the Arca 2006 Proposal was approved and implemented prior to the start of Regulation NMS.

C. The Display of Liquidity Should be Encouraged

Tradebook supports the Exchange's position that the Commission should encourage the display of liquidity. This is precisely why the Day ISO order type(s) must be abrogated. Exchanges should encourage the use of and elevate the position of Reserve. As noted in the Tradebook Comment Letter, "Reserve orders were created so that large orders could be represented in the market without moving the market, which can happen with large display sizes. Reserve orders are display in waiting, adding to the market depth and contributing to market stability while controlling for potential adverse market movement that can occur from large display." Reserve

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[7]   Regulation NMS Guidance 3.01.

[8]   Securities Exchange Act Release No. 34-54549 (Sept. 29, 2006); File No. SR-NYSEArca-2006-59; 71 Fed. Reg. 59179 (Oct. 6, 2006).

[9]   At the time of the NYSE Arca Proposal, the greater concern was the interaction of manual quotes within an electronic market. The Proposal notes that greater concern: "Post No Preference (PNP) Orders and PNP Directed Orders will never route away and will be posted in the NYSE Arca book if partially executed on the exchange. PNP Orders may lock, cross or trade-through a Manual Quotation without a requirement to route." Securities Exchange Act Release No. 34-54549 (Sept. 29, 2006); File No. SR-NYSEArca-2006-59; 71 Fed. Reg. 59179 (Oct. 6, 2006) at 59180.

[10]   This proposal was approved before the trading phase on February 5, 2007 started.

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is a resting "display-in-waiting" order in the marketplace. Consistent with encouraging display, other orders should yield to their standing in the marketplace.

As stated in the Tradebook Comment Letter, the rules and guidance do not obfuscate the Exchanges' (as SROs) requirement to ensure that the Day ISO does not systematically cause Regulation NMS Rule 610 violations. NYSE Arca appears to be one of the exchanges that stands it ground on Reserve replenishment. The Tradebook System has, since 2007, displayed orders in the NYSE Arca system and this is the behavior we appear to experience. Thus, because the NYSE Arca system appears to work in this manner, the NYSE system accepting Day ISOs would be systematically violating Rule 610.

D. The ISO Exemption to Rule 610(d) – The Exchange Must Check the Market Prior to Posting

As noted in the Tradebook Comment Letter, the Adopting Release stated that only a SRO may "ship and post" – a procedure where the SRO attempts to execute against a relevant displayed quotation while simultaneously posting a quotation that could lock or cross such a quotation.[11] The Commission was quite clear that only SROs could "ship and post" because compliance with Rule 610 is solely an SRO responsibility due to the fact that the SRO is the only entity in the national market that can post a protected quote. The Regulation NMS Guidance is consistent with that view:

> "Question 5.02: ISO Exception to SRO Lock/Cross Rules
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> The SRO rules addressing locking and crossing quotations include an ISO exception under which market participants are permitted to "ship-and-post." Do the routing requirements for this exception vary in any respect from the routing requirements for other uses of ISOs?
>
> Answer: Yes, the ISO exception from the SRO lock/cross rules varies from other ISO exceptions with respect to the scope of protected quotations to which ISOs must be routed. For example, Rule 611(b)(6) requires that ISOs be routed to execute against all protected quotations with better prices than the price of the excepted trade-through transaction. The ISO exception to the SRO lock/cross rules, in contrast, requires that ISOs be routed to execute against all protected quotations with a price that is equal to the display price (i.e., those protected quotations that would be locked by the displayed quotation), as well as all protected quotations with prices that are better than the display

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[11] Adopting Release at 206.

price (i.e., those protected quotations that would be crossed by the displayed quotation)."[12]

The staff reference to "market participants" is referring to the other SROs because "members" sending orders cannot possibly predict at the time of sending the future state of the market and whether the order will result in a locked or crossed market. Also, consistent with this guidance, the exchange as the market participant can offer to check the market for the member, but it would be inappropriate to abrogate that obligation to the member.

The Adopting Release noted: "SRO rules can include so-called 'ship and post' procedures that require a market participant to attempt to execute against a relevant displayed quotation while posting a quotation that could lock or cross such a quotation. Finally, Rule 610(d)(2) requires that each SRO's rules be reasonably designed to enable the reconciliation of locked or crossed quotations in an NMS stock. Such rules must require the market participant responsible for displaying the locking or crossing quotation to take reasonable action to resolve the locked or crossed market."[13] The ISO does not absolve the Exchange from the responsibility of checking the market prior to posting.

E. The Exchange Has Not Demonstrated that the Order Type Meets Statutory Standards

The Notice must be consistent with Section 6(b)[14] of the Exchange Act and, in particular, further the objectives of Section 6(b)(5)[15] of the Exchange Act. A proposed rule change must be

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[12]   Regulation NMS Guidance 5.02.

[13]   Footnote 457 of the Adopting Release states: "The Commission notes that the requirement in Rule 610(d)(1) that an SRO establish, maintain, and enforce rules that require its members reasonably to avoid engaging in certain activity relating to locking and crossing of displayed quotations may appear to be similar to the language contained in Section 8(d)(i) of the existing ITS Plan that '[t]he Participants also agree that 'locked markets' in System securities should be avoided.' The Commission emphasizes, however, that the intent and meaning of Rule 610(d) is more strict and comprehensive than the ITS Plan provision. In particular, as noted above, Rule 610(d) requires SROs to restrict their members' ability to engage in locking and crossing activity. The Commission therefore believes that most existing SRO rules established to implement the locked and crossed provision of the ITS Plan likely would not be sufficient to comply with Rule 610(d)." Furthermore, the footnote in Regulation NMS and Rule 610(d)(2) require each SRO to have rules that are reasonably designed to enable reconciliation of the locked or crossed quotes in a NMS stock. It is clear that the exchange must take steps to resolve the lock/cross condition and the Day ISO and Day ISO ALO do nothing to resolve this condition. The example provided confirms this.

[14]   15 U.S.C. § 78f(b).

[15]   15 U.S.C. § 78(f)(b)(5). "The rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market

designed to 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, to protect investors and the public interest. As stated in the Tradebook Comment Letter and herein, adding a day time-in-force condition to ISOs adds impediments to a free and open market and national market system. The Day ISO is a distortion of the original ISO order type and is inconsistent with the definition of an ISO under Regulation NMS.[16] By "considering" that the "protected quotes that existed at the time of arrival of the Day ISO as cleared when it posts any remainder of a Day ISO to the Exchange's book" the Day ISO directly violates Regulation NMS's prohibition on locking and crossing quotations. The treatment of Reserve makes violations in Rule 610 systemic. Furthermore, the Exchange's attempts to absolve itself of its own responsibilities and obligations with respect to locked and crossed markets go against Section 6(b)(5) of the Exchange Act.

F. The Commission Should Disapprove the Rule Change

Rather than conduct a comprehensive review to streamline order types, the Exchange has created this new order type – one that does not support fair, orderly, and efficient markets. In an effort to reduce the complexity in our market structure, a goal espoused by the Chair in her recent speech, Tradebook believes that the simplest solution is for the Commission to disapprove the rule change and provide guidance to the SROs and ATSs regarding this order type.
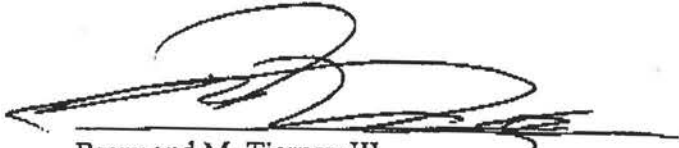
Conclusion

For the foregoing reasons, the Commission should disapprove the Notice under Section 19(b)(2) because disapproval is necessary or appropriate in the public interest, for the protection of investors, and in furtherance of the purposes of the Exchange Act and Regulation NMS.
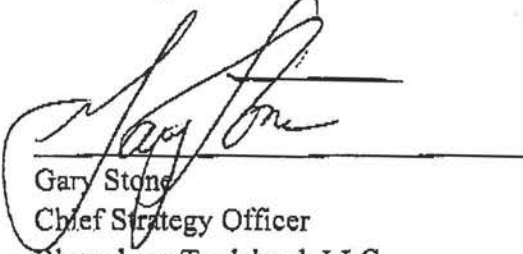
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If you have any questions or you would like to discuss these matters further, please do not hesitate to contact us.

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system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this chapter or the administration of the exchange."

[16]   17 C.F.R. § 242.600(b)(3). See Tradebook Comment Letter.

Raymond M. Tierney III
President and Chief Executive Officer
Bloomberg Tradebook LLC

Gary Stone
Chief Strategy Officer
Bloomberg Tradebook LLC

APPENDIX

Bloomberg
TRADEBOOK LLC
Member of FINRA/SIPC/NFA

<u>September 22, 2014</u>

<u>Via email: rule-comments@sec.gov</u>

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

COMMENT LETTER AND PETITION FOR DISAPPROVAL

Re: <u>Notice of Filing of Proposed Rule Change Amending Rule 13 to Make the Add Liquidity Only Modifier Available for Additional Limit Orders and Make the Day Time-in-Force Condition Available for Intermarket Sweep Orders, File No. SR-NYSE-2014-32</u>

Dear Secretary Fields:

Bloomberg Tradebook LLC ("Tradebook")[1] appreciates the opportunity to comment on the above-captioned notice ("Notice"), under which the New York Stock Exchange LLC ("Exchange") proposes to amend Exchange Rule 13, Orders and Modifiers.[2] According to the Notice, the Exchange is proposing to make the add liquidity only modifier ("ALO Modifier") available for additional limit orders and make the day time-in-force condition available for intermarket sweep orders ("ISOs").

The U.S. Securities and Exchange Commission ("Commission") shall by order approve or disapprove such proposed rule change, or institute proceedings to determine whether the proposed rule change should be disapproved in accordance with Section 19(b)(2) of the Securities Exchange Act of 1934, as amended (the "Exchange Act").[3] For the reasons set forth

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[1]   Bloomberg Tradebook LLC is a registered broker-dealer, operates an Alternative Trading System (ATS) registered with the SEC, is a member of FINRA, Inc., and is a wholly-owned subsidiary of Bloomberg L.P.

[2]   Notice of Filing of Proposed Rule Change Amending Rule 13 to Make the Add Liquidity Only Modifier Available for Additional Limit Orders and Make the Day Time-in-Force Condition Available for Intermarket Sweep Orders ("Notice"), Release No. 34-72548 (July 7, 2014); File No. SR-NYSE-2014-32; 79 Fed. Reg. 40183.

[3]   See 15 U.S.C. § 78s(b)(2).

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below, and because the Exchange's request is inconsistent with Regulation NMS, we respectfully petition the Commission to disapprove the Notice.

A. Background

An ISO is currently defined in Exchange Rule 13 as a limit order designated for automatic execution that meets the following requirements: (i) it is identified as an ISO in the manner prescribed by the Exchange; and (ii) simultaneously with the routing of an ISO to the Exchange, one or more additional limit orders, as necessary, are routed to execute against the full displayed size of any protected bid, in the case of a limit order to sell, or the full displayed size of any protected offer, in the case of a limit order to buy and these additional orders are identified as ISOs. This definition is based on the definition of ISO set forth in Regulation NMS Rule 600(b)(30).[4]

The Exchange stated in the Notice that currently it immediately and automatically executes an ISO upon arrival and the portion not so executed will be immediately and automatically canceled.[5] Accordingly, the Exchange treats all ISOs with an immediate-or-cancel ("IOC") time-in-force condition. Tradebook believes that the Exchange's current Rule 13 is consistent with the Commission's stated ISO behavior outlined in the Regulation NMS final rule. However, the Exchange notes that other equities exchanges currently do not limit their ISOs to an IOC time-in-force condition. Thus, the Exchange now seeks to amend Rule 13 governing ISOs to make available an ISO order with a day time-in-force condition. As proposed, an ISO designated Day ("Day ISO"), if marketable upon arrival, would be immediately and automatically executed against all of the liquidity in the Exchange's display and reserve queues up to its full size in accordance with and to the extent provided by Exchange Rules 1000 – 1004.[6]

The Exchange remarked the following in connection with the Day ISO, "The Exchange further proposes to provide that the remaining unexecuted portion of a Day ISO would be posted to the Exchange's book at its limit price and may lock or cross a protection quotation that was displayed at the time of arrival of the Day ISO. The Exchange believes this proposed rule text is consistent with Regulation NMS and the rules of other exchanges because the member organization that sent the Day ISO to the Exchange has an existing obligation (pursuant to paragraph (a)(ii) governing ISOs in Rule 13) to simultaneously route ISOs to trade with the full size of protected quotations on other markets. Accordingly, the Exchange would *consider*[7] any

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[4]   17 C.F.R. § 242.600(b)(30).

[5]   See paragraph (b) governing ISOs in Exchange Rule 13.

[6]   Notice at 10.

[7]   Tradebook's emphasis on the word "consider" is added because as we explain later, the Exchange is making an assumption that we believe is contra to the compliance of Rule 610.

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protected quotes that existed at the time of arrival of the Day ISO as cleared when it posts any remainder of a Day ISO to the Exchange's book."

The Exchange would then allow the ALO Modifier to set new price levels on the Day ISO ("Day ISO ALO") when posting locking and crossing quotations: "Because Day ISOs would not route, which is similar to the proposed ALO Modifier functionality, the Exchange proposes to re-price and re-display resting Day ISOs in a manner consistent with the proposed re-pricing and re-displaying functionality described above for limit orders designated ALO. As proposed, if, after posting, a Day ISO would lock or cross a protected quotation, the Exchange would re-price and re-display the order consistent with proposed paragraph (b) for ALO Modifiers in Rule 13."

B. Distortion of the Intermarket Sweep Order (ISO) Order Type

The ISO was originally introduced as a solution to data latency issues and prevention of an "indefinite loop scenario" that such issues could cause. In every instance in the Regulation NMS adopting release ("Adopting Release"), the Commission clearly referred to an ISO as an aggressive order – created for efficient sweeping.[8] This was a simple market structure and implementation concept. The Commission noted that ISOs are aggressive orders to increase execution speed and reliability because they would allow market participants to simultaneously and immediately sweep through multiple price levels. Specifically, the Commission stated that the ISO "allows market participants to access multiple price levels simultaneously at different trading centers – a particularly important function now that trading in penny increments has dispersed liquidity across multiple price levels. The intermarket sweep exception enables trading centers that receive sweep orders to execute those orders immediately, without waiting for better-priced quotations in other markets to be updated."[9]

Implied in the Adopting Release and the definition of ISO[10] is the fact that the ISO was never intended to have a day time-in-force condition. Rather, the Commission contemplated that ISOs would be aggressive orders filled immediately as IOC. In fact, the Commission went even further in stating that the ISO would be advantageous to liquidity providers enabling participants to "…compete on both price and size through use of the intermarket sweep order exception,[11]

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[8]   Regulation NMS Adopting Release ("Adopting Release"), Exchange Act Release No. 34-51808 (June 9, 2005), 70 Fed. Reg. 37496 (June 29, 2005) at 35.

[9]   Id.

[10]   17 C.F.R. § 242.600(b)(30).

[11]   17 C.F.R. § 242.611(b)(5).

which will allow them to *execute immediately* a large transaction at prices outside the best prices by routing orders to execute against the displayed size of better-priced quotations."[12]

History shows that IOC is the correct interpretation of the ISO order type. However, with the ISO IOC order type, an issue arose for the exchanges. The exchanges desired to keep residual unfilled order balances on their books because it was less beneficial for exchanges to have to compete with other market centers for the second order. Thus, the sender would have to send two orders: (1) ISO IOC; and then (2) a Day Limit Order. In the implementation phase of Regulation NMS, the exchanges requested that Commission staff allow an ISO that is not canceled when not executed immediately. For that reason, the Commission staff issued guidance on Regulation NMS Rules 610 and 611 ("Guidance") whereby staff noted that Regulation NMS does not require trading centers to cancel any portion of an ISO that cannot be executed immediately.[13] With this Guidance, staff sought to address issues occurring when ISOs were too large for execution, issues with message traffic, and posting residual unfilled balances after sweeping. However, Day ISO complicates the market structure because of the Day ISO's interaction with Regulation NMS Rule 610 (set forth in Section C below).

Additionally, what Commission staff did not contemplate was the further corruption of the ISO order type into the Exchange's requested Day ISO ALO order type – an ISO that is no longer an aggressive order and that no longer sweeps. At the time of implementation of Regulation NMS and the Guidance, the Commission did not anticipate that the ISO would be used as a Day ISO ALO to have a day time-in-force condition and set a new price level. The Day ISO ALO order type is not for sweeping or taking liquidity – it is a complete distortion of the intended use of the ISO order type and warrants meaningful Commission review. In light of the original purpose of the ISO order type and the resulting complications arising from Day ISO and Day ISO ALO (explained herein), Tradebook respectfully requests that the Commission revisit this Guidance and not permit these order types.

C. Day ISO Violates Regulation NMS Rule 610(d)

Regulation NMS Rule 610 governs access to quotations and subpart (d) states that "[e]ach national securities exchange and national securities association shall establish, maintain, and enforce written rules that: (1) [r]equire its members reasonably to avoid: (i) [d]isplaying quotations that lock or cross any protected quotation in an NMS stock; and (ii) [d]isplaying manual quotations that lock or cross any quotation in an NMS stock disseminated pursuant to an

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[12]   Adopting Release at 425.

[13]   Division of Trading and Markets' Responses to Frequently Asked Questions Concerning Rule 611 and Rule 610 of Regulation NMS (April 4, 2008 Update) found at http://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm#sec3 (last accessed September 19, 2014).

effective national market system plan; (2) [a]re reasonably designed to assure the reconciliation of locked or crossed quotations in an NMS stock; and (3) [p]rohibit its members from engaging in a pattern or practice of displaying quotations that lock or cross any protected quotation in an NMS stock disseminated pursuant to an effective national market system plan, other than displaying quotations that lock or cross any protected or other quotation as permitted by an exception contained in its rules..."

In the Adopting Release, the Commission explained that Regulation NMS Rule 610(d) was designed to promote and balance order and price competition in a market structure where various market venues competed with each other. The Commission has long been concerned that the practice of self-regulatory organizations (SROs) displaying quotations that lock and cross detract from market efficiency and can be a sign of an inefficient market structure. Further, the Commission has also been concerned that pricing rationality is disrupted by locked and crossed markets. Rule 610 obligates SROs to take all reasonable efforts to reduce the incidence of such disruptions. The Commission specifically stated the following in the Adopting Release about locked and crossed quotations: "The basic principle underlying the NMS is to promote fair competition among markets, but within a system that also promotes interaction between all of the buyers and sellers in a particular NMS stock. Allowing...locking and crossing quotations is inconsistent with this principle."

1. The Exchange Attempts to Abrogate its Locked and Crossed Markets Obligations

The Day ISO and Day ISO ALO order types are inconsistent with the basic principles underlying Regulation NMS and violate Commission policy behind the prohibition on locking and crossing quotations. In the Adopting Release the Commission noted that "...Rule 610(d) requires members to 'reasonably avoid' locking and crossing and prohibits a 'pattern or practice' of locking or crossing quotations where this can be reasonably avoided. As set forth above, Rule 610(d)(2) requires that each SRO's rules be reasonably designed to enable the reconciliation of locked or crossed quotations in an NMS stock. Such rules must require the market participant responsible for displaying the locking or crossing quotation to take reasonable action to resolve the locked or crossed market."[14] It is clear from Regulation NMS that because only SROs can display in the national market structure Rule 610 compliance is solely (and can only be) an SRO obligation. Thus, Regulation NMS prohibits an SRO from *considering* a protected quote that existed at the time of arrival of the Day ISO as cleared.

The Exchange attempts to utilize the Day ISO and Day ISO ALO order types even though they clearly violate Rule 610's prohibitions on locked and crossed markets. The Regulation NMS

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[14]   Adopting Release at 207.

Rule 610(d) obligation to not post locking and crossing quotations rests with SROs – in this case the Exchange because the Exchange posts the quotation. As set forth in the Notice, the Exchange asserts that the Day ISO and Day ISO ALO may lock and cross a protected quotation. However, instead of avoiding use of an order type that violates Regulation NMS 610 and Commission principles of fair and orderly markets, the Exchange improperly attempts to transfer its obligations to not post locking and crossing quotations to the sender of the order, even though a locked or crossed market can only be determined when the order is *received* by the Exchange and the Exchange posts the display. The sender of the order cannot possibly predict at the time of sending the future state of the market and whether the order will result in a locked or crossed market. Essentially, the Exchange contends that it does not have to check the market prior to posting because the sending broker already did. However, the Exchange *must* check the market prior to posting. This is the only way the Exchange can reasonably be assured that it is not locking or crossing the market when it received the order. It is unreasonable for the Exchange to abrogate this responsibility to another party. Accordingly, the Exchange should not be permitted to transfer its responsibility and rely exclusively on the sending broker to make this determination, particularly since it is impossible for the sending broker to know exactly where the market will be when the order is received and it is the Exchange that posts the quote. We respectfully request that the Commission revisit its Guidance[15] to reiterate that the Exchange is required to check a quote before posting.

The Adopting Release also noted that only a SRO may "ship and post" – a procedure where the SRO attempts to execute against a relevant displayed quotation while simultaneously posting a quotation that could lock or cross such a quotation.[16] The Commission was quite clear that only SROs could "ship and post" because compliance with Rule 610 is solely an SRO responsibility due to the fact that the SRO is the only entity in the national market structure that can post a protected quote. The foregoing reflects the Commission's intention that the SRO's obligations include monitoring, seeking to avoid, and resolving locking and crossing quotation issues. Instead, with the proposed rule change, the Exchange is improperly allowing a non-SRO to engage in a ship and post procedure and transferring to the sending broker all responsibilities with respect to locking and crossing quotations and disclaims all of its own responsibilities and obligations.

2. The Exchange's Treatment of Reserve Creates a Systematic Violation of Rule 610

Day ISO and Day ISO ALO orders unfairly enable the sender of the order to gain immediate protected status. It is the Reserve order that should be given the benefit of special consideration.

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[15]   See supra note 13.

[16]   Adopting Release at 206.

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Reserve orders were created so that large orders could be represented in the market without moving the market, which can happen with large display sizes. Reserve orders are display in waiting, adding to the market depth and contributing to market stability while controlling for potential adverse market movement that can occur from large display. Rule 611 protects displayed quotes. The Commission should abolish Day ISOs to protect, incentivize and elevate the status of Reserve Orders, and expand its Guidance[17] to reflect this.

The Day ISO's lack of respect for Reserve creates a systematic violation of Regulation NMS Rule 610, which the Exchange is supposed to prevent (and have policies to prevent). Day ISOs *assume* that there is no Reserve behind the displayed quote. The Commission through Rule 611 acknowledges the value of displayed liquidity by expressly protecting an SRO's top of file only displayed orders. Under current regulations, the replenishment from Reserve from an order that executed versus display technically never leaves the quote. It is treated as a quote update. In fact, most exchanges automatically replenish the display without checking whether they will lock or cross other protected quotes. The exchanges stand their ground with Reserve replenishment because the replenishment is instantaneous. Isn't it ironic that the same exchanges that permit Day ISOs and the equivalent of a Day ISO ALO treat Reserve replenishment in this manner? By behaving this way and knowing that other SROs behave similarly, they cannot be in conformance with the "reasonableness" standards of Rule 610. This is what leads to the systematic violation of Rule 610 and why the exchange must check the quote prior to posting the display of a Day ISO. It is improper for the Exchange to take the ISO flag and not check the quote prior to posting.

The Commission never provided guidance on the treatment of Reserve. When an order takes liquidity, does the SRO replenish immediately at the same level or must the SRO check the quote prior to replenishing? Both standards are operating in the market.

> For example, consider a market that is 10 - 11. At Exchange A there is an offer for 10,300 shares at 11. 300 shares are displayed with 10,000 shares in Reserve. Only the 300 is protected. Also at 11, Exchange B has an order for 200 shares – all 200 shares are displayed and, of course, under Rule 611, protected. Assume a member sends two Day ISO orders to lift both 11 offers. To be compliant with Rule 611, the sender sends one order for 300 shares to Exchange B and 400 shares to Exchange A. Because there are two standards of how Reserve is replenished there are two possible scenarios:
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> Scenario 1: Assume that the Exchange A automatically redisplays - the 400 shares at Exchange A executes. Exchange A immediately redisplays at 300 shares at 11. At Exchange B, if the Exchange does not check the quote, the Day ISO will lock the market with 100 shares at 11.

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[17]   See supra note 13.

Scenario 2: Assume that Exchange A checks the quote prior to redisplaying - the 400 shares at Exchange A executes. But if Exchange B updates the quote first and Exchange A checks the quote prior to replenishing Reserve, then Exchange A will redisplay at 12 yielding to the Day ISO, which has taken 200 shares at 11 and become 11 bid for 100 shares.

This is another negative consequence of the Day ISO order type. In every encounter where an away exchange could have Reserve, exchanges' treatment of the Day ISO will systematically violate Rule 610 and lock or cross the market.

The Commission has the opportunity to elevate the importance of Reserve in the market. Reserve is very important because it enables large orders to have a display but reduce signaling risk. Reserve also provides depth to the market and with such depth comes more stability. By providing guidance that Reserve can "stand its ground" by redisplaying and forcing all other orders to check the quote and yield, the Commission will give Reserve orders the benefit it deserves.

D. Day ISO: a New and Unapproved Order Type

1. Proliferation of Order Types

Tradebook would like to take this opportunity to support Chair White's recent remarks: "I am asking the exchanges to conduct a comprehensive review of their order types and how they operate in practice. As part of this review, I expect that the exchanges will consider appropriate rule changes to help clarify the nature of their order types and how they interact with each other, and how they support fair, orderly, and efficient markets."[18] The proliferation of order types is of great concern. From Chair White's request, the public is learning more about the existence of these (and other) order types and how orders interact with each other. This is what makes it possible for the Commission's denial of the Rule 13 changes to have universal application to all SROs.

2. Other Exchanges' Utilization of Day ISO Without Commission Approval

In seeking approval for this new order type, the Exchange filed the Notice pursuant to Section 19(b)(1)[19] of the Securities Exchange Act of 1934[20] and Rule 19b-4 thereunder.[21] The Notice

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[18]   "Enhancing Our Equity Market Structure" by Chair Mary Jo White, Sandler O'Neill & Partners, L.P. Global Exchange and Brokerage Conference, New York, N.Y. (June 5, 2014).

[19]   15 U.S.C. § 78s(b)(1).

[20]   15 U.S.C. § 78a.

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states that "Currently, the Exchange immediately and automatically executes an ISO upon arrival and the portion not so executed will be immediately and automatically cancelled. Accordingly, the Exchange treats all ISOs with an immediate-or-cancel time-in-force condition. Other equities exchanges do not limit their ISOs to an immediate-or-cancel time-in-force condition." In fact, the Exchange states that "The rules of Nasdaq, BATS, BATS-Y, EDGA, and EDGX do not expressly provide that their versions of ISOs can be day, however, nor do their rules prohibit this functionality. In practice, Nasdaq, BATS, BATS-Y, EDGA, and EDGX all accept ISOs with a day time-in-force condition."

In the case of the ISO, the Exchange's notice to amend Rule 13 notes that other exchanges do not expressly provide for this "functionality" in their rules, but they go ahead and utilize it anyway.[22] By doing so, the other exchanges appear to completely absolve themselves of the Commission's required rule change and review process. The unapproved use of the order type by other exchanges does not provide supporting evidence that the order type is proper.

NYSEArca, in 2006, appears to be the only SRO that filed with the Commission, through a Post No Preference ("PNP") rule change, an order type that expressly permitted an ISO with a day time-in-force condition.[23] However, contrary to what the Exchange suggests, PNP does not expressly permit Day ISO or Day ISO ALO and is not an equivalent order type.[24] The Exchange's current notice to amend Rule 13 provides the Commission with a unique opportunity to review and reevaluate that approval in the context of today's market structure and create uniform compliance with Rule 610.

E. The Exchange Has Not Demonstrated that the Order Type Meets Statutory Standards

The Notice must be consistent with Section 6(b)[25] of the Exchange Act and, in particular, further the objectives of Section 6(b)(5)[26] of the Exchange Act. A proposed rule change must be

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[21]   17 C.F.R. § 240.19b-4.

[22]   Please note that the Exchange refers to Day ISO as a "functionality," perhaps in an effort to downplay the fact that it is a significant departure from the original ISO order type and that Day ISO is, in point of fact, a completely new order type.

[23]   Securities Exchange Act Release No. 34-54549 (Sept. 29, 2006); File No. SR-NYSEArca-2006-59; 71 Fed. Reg. 59179 (Oct. 6, 2006).

[24]   For example, the PNP order type is completely different from the Day ISO ALO order type the Exchange requests in the Notice.

[25]   15 U.S.C. § 78f(b).

designed to 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, to protect investors and the public interest. Adding a day time-in-force condition to ISOs adds impediments to a free and open market and national market system. The Day ISO is a distortion of the original ISO order type and is inconsistent with the definition of an ISO under Regulation NMS.[27] By "considering" that the "protected quotes that existed at the time of arrival of the Day ISO as cleared when it posts any remainder of a Day ISO to the Exchange's book" the Day ISO directly violates Regulation NMS's prohibition on locking and crossing quotations. The treatment of Reserve makes violations of Rule 610 systemic. Furthermore, the Exchange's attempts to absolve itself of its own responsibilities and obligations with respect to locked and crossed markets go against Section 6(b)(5) of the Exchange Act.

F. The Commission Should Disapprove the Rule Change

Rather than conduct a comprehensive review to streamline order types, the Exchange has created this new order type – one that does not support fair, orderly, and efficient markets. In an effort to reduce the complexity in our market structure, a goal espoused by the Chair in her recent speech, Tradebook believes that the simplest solution is for the Commission to disapprove the rule change and in the disapproval text provide guidance to the SROs and ATSs that the default time-in-force for an ISO order type is IOC, as the Exchange's current Rule 13 accurately stipulates.

Tradebook acknowledges that this comment letter will be received by the Commission after the deadline. We considered filing this letter under the still open 2010 Concept Release on Market Structure but decided to file it under this Notice even though the comment period deadline has passed. Tradebook will be making our views known through our Market Structure and Thought Leadership initiative.[28]

The Commission, in its discretion, may accept and include in the public record written comments received by the Commission after the closing date.[29] We understand that no comments were

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[26]   15 U.S.C. § 78(f)(b)(5). "The rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this chapter or the administration of the exchange."

[27]   17 C.F.R. § 242.600(b)(3).

[28]   Please refer to "The 'Book" at www.bloombergtradebook.com.

[29]   17 C.F.R. § 202.6(b).

received by the deadline and that on August 21, 2014 the Commission extended from 45 days to 90 days[30] the time period under which it shall either approve the rule change, disapprove the rule change, or institute proceedings to determine whether the proposed rule change should be disapproved.[31] The Commission stated the following, "The Commission finds that it is appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider the proposed rule change." Accordingly, Tradebook respectfully requests that the Commission consider this comment letter as the Commission continues to evaluate the proposed rule change and also include this letter in the public record.

Conclusion

For the foregoing reasons, the Commission should disapprove the Notice under Section 19(b)(2) because disapproval is necessary or appropriate in the public interest, for the protection of investors, and in furtherance of the purposes of the Exchange Act and Regulation NMS.
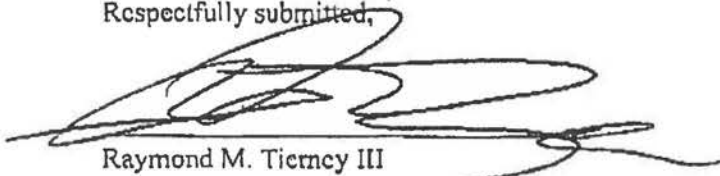
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If you have any questions or you would like to discuss these matters further, please do not hesitate to contact us.

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[30]   The Commission designated October 9, 2014 as the date by which the Commission should act.

[31]   See Section 19(b)(2) of the Securities Exchange Act of 1934, 15 U.S.C. § 78s(b)(2). Notice of Designation of a Longer Period for Commission Action on Proposed Rule Change Amending Rule 13 to Make the Add Liquidity Only Modifier Available for Additional Limit Orders and Make the Day Time-In-Force Condition Available for Intermarket Sweep Orders; Release No. 34-72893 (August 21, 2014); File No. SR-NYSE-2014-32; 79 Fed. Reg. 51208 (August 27, 2014).

Respectfully submitted,

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