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November 7, 2016

<u>VIA E-MAIL</u>

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

Re: <u>SR-NYSE-2016-62, SR-NYSEMKT-2016-83, and SR-NYSE-Arca-2016-123</u>

Dear Mr. Fields:

New York Stock Exchange LLC ("NYSE"), NYSE MKT LLC ("NYSE MKT"), and NYSE Arca, Inc. ("NYSE Arca," together with NYSE and NYSE MKT, the "Exchanges") are submitting this comment letter for the public file regarding the above-referenced proposed rule changes, which were approved by the Commission on October 3, 2016[1] and September 30, 2016.[2] These proposed changes to the Exchanges' rules were filed to comply with the Tick Size Pilot Program (the "Plan"),[3] which began on October 3, 2016.

The Plan requires the Exchanges to establish, maintain, and enforce written policies and procedures that are *reasonably designed to comply* with applicable quoting and trading requirements of the Plan (emphasis added).[4] However, in its approval order of the NYSE and NYSE MKT proposals, the Commission stated that "any proposed changes targeted at

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[1]   See Securities Exchange Act Release Nos. 79030 (Oct. 3, 2016), 81 FR 69878 (Oct. 7, 2016) (SR-NYSE-2016-62) (Notice of Filing of Partial Amendment No. 2 and Order Granting Accelerated Approval) ("NYSE Approval Order") and 79029 (Oct. 3, 2016), 81 FR 69874 (Oct. 7, 2016) (SR-NYSEMKT-2016-83) (Notice of Filing of Partial Amendment No. 2 and Order Granting Accelerated Approval) ("NYSE MKT Approval Order").

[2]   See Securities Exchange Act Release No. 79017 (September 30, 2016), 81 FR 69562 (October 6, 2016) (SR-NYSEArca-2016-123) (Notice of Filing of Partial Amendment No. 1 and Order Granting Accelerated Approval) ("NYSE Arca Approval Order").

[3]   Securities Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27513 (May 13, 2015) ("Tick Plan Approval Order"). The pilot includes stocks of small capitalization companies, defined as those with $3 billion or less in market capitalization, an average daily trading volume of one million shares or less, and a volume weighted average price of at least $2.00 for every trading day ("Pilot Securities"). All Pilot Securities have been assigned to either a control group or one of three test groups. Pilot Securities in Test Group Three are subject to a Trade-at requirement, which prohibits price matching by a market participant that is not displaying at a price of a Trading Center's best protected bid or offer, subject to certain exceptions.

[4]   See Section IV of the Plan.

particular Test Groups during the Pilot Period *should be necessary for compliance* with the Plan" (emphasis added).[5] This new standard established by the Commission in the approval order has the effect of limiting the Exchanges' ability to adapt to market structure changes, and is not articulated in the Exchange Act or the Plan. In addition, no comment was solicited before this new standard was applied.

Discussion

On August 25, 2016, the Exchanges filed their proposed rule changes to set forth the Exchanges' specific procedures for handling, executing, re-pricing, and displaying certain order types and order type instructions applicable to Pilot Securities. Consistent with the Plan, the Exchanges' proposals were reasonably designed to comply with applicable quoting and trading requirements of the Plan. Commission staff, however, stated that the Commission would not approve the NYSE and NYSE MKT proposals because certain of the proposed changes -- those relating to the operation of d-Quotes in Pilot Securities in Test Group Three -- did not meet the non-public standard being applied of "necessary for compliance with the Plan."

A d-Quote is an order available only to Floor brokers that has discretionary instructions as to size or price, or both. To comply with the Trade-at requirement applicable to Pilot Securities in Test Group Three, NYSE and NYSE MKT proposed that a d-Quote would not exercise discretion if the price of a same-side protected quote is equal to or better than the displayed price of the d-Quote. The staff, however, expressed its view that there were three scenarios in which d-Quotes in Pilot Securities in Test Group Three *should* exercise discretion, rather than not exercising discretion, as proposed by the NYSE and NYSE MKT.

As an alternative to making the specific, discrete changes to Test Group Three, Commission staff stated that NYSE and NYSE MKT could instead apply its proposed d-Quote functionality across *all* Pilot Securities, even though not all Pilot Securities are subject to the Trade-requirement for which the changes were designed.

Though the NYSE and NYSE MKT did not believe that it was appropriate to make changes to its proposed rules, it was effectively required to do so. The absence of a Commission approval of rules to implement the Plan prior to the scheduled implementation on October 3, 2016 would have resulted in NYSE and NYSE MKT either violating their obligation to comply with the terms of the Plan[6] or violating Section 19(b) of the Act by applying rules that had not been approved. Accordingly, NYSE and NYSE MKT filed amendments to apply the d-Quote changes designed for compliance with the Trade-at requirement to 2,200 securities not subject to the Trade-at requirement.

In addition, Commission staff applied the "necessary for compliance with the Plan" standard to the proposed rule changes filed by NYSE Arca. NYSE Arca filed proposed rule changes that were reasonably designed to comply with applicable quoting and trading requirements of the Plan. Commission staff, however, stated that the Commission would not approve NYSE Arca's

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[5]   See NYSE Approval Order, supra note 1 at 69880 and NYSE MKT Approval Order, supra note 1 at 69876.

[6]   Rule 608(c) of Regulation NMS.

proposal because its proposed changes to the functionality of its Market Pegged Orders in Test Group Three Securities were not "necessary for compliance with the Plan." Accordingly, NYSE Arca amended its proposal to prohibit the use of Market Pegged Orders in all Pilot Securities, even though the operation of Market Pegged Orders did not conflict with the requirements governing Pilot Securities in the control group or Test Groups One or Two.[7]

Finally, we also note that, to receive Commission approval in a timely manner, Bats BYX Exchange, Inc., Bats BZX Exchange, Inc., Bats EDGA Exchange, Inc., and Bats EDGX Exchange, Inc. ("Bats Exchanges") similarly modified their original proposed rule changes describing system and functionality necessary to implement the Plan.[8] The Bats Exchanges initially proposed to eliminate certain order types only in Test Group Three Securities because of the Trade-at requirement applicable to those Pilot securities. The Commission's publication of these exchanges' proposals for comment did not express concern that they failed to meet the standard in the Plan of being reasonably designed to comply with applicable quoting and trading requirements of the Plan. Instead, the Commission stated that eliminating certain order types only in Test Group Three 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." This concern is not a basis under the Exchange Act or the Plan for objecting to these exchanges' proposals. Nevertheless, to meet the implementation deadline in the Plan and avoid non-compliance, the Bats Exchanges amended their respective proposals and eliminated certain order types across all Pilot Securities, even though only Test Group Three Securities are subject to a Trade-at requirement.

Conclusion

The Exchanges are concerned that there was no public notice or comment process regarding the standard that exchanges were required to meet to implement the Plan. The Exchanges developed technology changes to implement the Plan and were informed of the "new" standard only after filing proposed rule changes.[9] The Exchanges were then required to agree to last-minute changes to the operation of order types. Importantly, this new standard has not been applied to trading centers that are not registered exchanges and therefore do not need to file proposed rule changes before changing order behavior. Finally, the Exchanges believe that the

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[7]   See NYSE Arca Approval Order, supra note 2 at 69562 n. 9 (describing the NYSE Arca Partial Amendment No. 1, which was filed September 27, 2016).

[8]   See Letter from Eric Swanson, EVP, General Counsel and Secretary, Bats Global Markets, Inc. to Brent J. Fields, Secretary, Securities and Exchange Commission, dated September 9, 2016

[9]   The Exchanges, together with BATS Global Market and Nasdaq, Inc., submitted a comment letter on the proposals of the ten exchanges represented by these markets in which the concern was expressed that the lack of clarity at that late date jeopardized not only the integrity of the scheduled industry-wide tests, but also the ability of exchanges to meet the October 3, 2016 implementation date. See Letter from Eric Swanson, EVP, General Counsel and Secretary, Bats Global Markets, Thomas A. Wittman, EVP, Global Head of Equities, Nasdaq, Inc., and Elizabeth K. King, General Counsel and Corporate Secretary, New York Stock Exchange, to Brent J. Fields, Secretary, Securities and Exchange Commission, dated September 9, 2016, and available here: https://www.sec.gov/comments/sr-batsbyx-2016-17/batsbyx201617-2.pdf ("September 9, 2016 Comment Letter").

changes they were required to make are illogical and will not improve, and may diminish, the quality of the Pilot data.

Sincerely,

Elizabeth K. King

cc: Hon. Mary Jo White, Chair
        Hon. Kara Stein, Commissioner
        Hon. Michael Piwowar, Commissioner