CITADEL | Securities

March 15, 2017

Mr. Eduardo A. Aleman
Assistant Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549–1090

Re: Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Rule 104 Regarding Designated Market Makers Trading Ten Minutes Prior to the Close of Trading (Release No. 34-80044; File No. SR-NYSE-2016-71)

Dear Mr. Aleman:

Citadel Securities ("Citadel")[1] appreciates the opportunity to comment on the Securities and Exchange Commission's (the "Commission") order instituting proceedings[2] to determine whether to approve or disapprove the proposed rule change by the New York Stock Exchange LLC ("NYSE"). This rule change would eliminate the prohibition against Designated Market Makers ("DMMs") establishing, during the last ten minutes of trading before the close, a new high (low) price for the day on NYSE in a security in which the DMM has a long (short) position (the "NYSE Rule").[3] Citadel supports the Proposal primarily because the NYSE Rule is no longer necessary due to changes in equity market structure that have occurred since the adoption of the rule in 2006.

I. The NYSE Rule No Longer Serves Its Intended Purpose

The NYSE Rule was designed to prevent specialists from exercising undue influence over the price of a security by prohibiting certain specialist transactions during the last ten minutes of trading before the close.[4] At the time the NYSE Rule was adopted, specialists enjoyed significant benefits compared to other market participants, including (a) trade-through protection for manual quotations[5] and (b) an order-by-order advance "look" at incoming orders. Trade-through

[1] Citadel Securities is a leading global market maker across a broad array of fixed income and equity securities. In partnering with us, our clients, including asset managers, banks, broker-dealers, hedge funds, government agencies and public pension programs, are better positioned to meet their investment goals. On an average day, Citadel accounts for approximately 15 percent of U.S. listed equity volume, 19 percent of U.S. listed equity option volume, and more than 35 percent of all retail U.S. listed equity volume.

[2] Securities Exchange Act Release No. 80044, 82 FR 11388 (February 22, 2017) ("**Order Instituting Proceedings**").

[3] Securities Exchange Act Release No. 79284, 82 FR 11252 (November 17, 2016) (the "**Proposal**").

[4] Securities Exchange Act Release No. 54860, 71 FR 71221, 71229 (December 8, 2006).

[5] *See* NYSE Information Memo Number 07-62, Elimination of ITS (Intermarket Trading System) (June 29, 2007). Trade-through protection of manual quotations meant that, unless an exception applied, market participants would have to route orders to NYSE specialists to determine if a better priced quotation was available there before executing on an away market.

protection drove significant order flow to NYSE specialists, while the advance look provided them with "an informational advantage over other market participants which, if unchecked, could permit them to adjust their trading interest to the disadvantage of orders residing on the book."[6] In addition, at that time, NYSE specialists maintained a dominant position in the trading of NYSE-listed securities. For example, NYSE executed approximately 79.1% of the consolidated volume in NYSE-listed stocks in January 2005.[7] Together, the dominant position of, and structural benefits enjoyed by, NYSE specialists warranted imposing prescriptive limitations on their trading activities, particularly at certain critical pricing points during the day (such as the pre-closing period).

Significant changes in equity market structure since the adoption of the NYSE Rule in 2006 merit its removal. NYSE specialists have been replaced by DMMs, which do not have the same structural advantages that specialists once did, such as the order-by-order advance "look". In addition, DMMs do not have the same dominant position in the trading of NYSE-listed securities. NYSE market share of consolidated volume in NYSE-listed stocks decreased from 79.1% to 25.1% between January 2005 and October 2009.[8] This trend has continued, as evidenced by the fact that, for the month of February 2017, the NYSE market share for NYSE-listed (Tape A) stocks was approximately 24% (including auctions) and 19% (excluding opening/closing/reopening auctions).[9] Market data for this same period of time, covering common stocks for which NYSE is the primary exchange and Citadel Securities is the DMM, shows that, on a share-weighted basis, NYSE market share during the last ten minutes of trading (before the closing auction) was approximately 27%.

As detailed above, the majority of trading in NYSE-listed securities now occurs away from DMMs, reducing concerns regarding undue influence over the price of these securities, both during the day and near the close. In addition, DMM trading in NYSE-listed securities occurs without the advance "look" that was once provided to specialists. Instead, DMM algorithms, which are responsible for most DMM trading activity today, operate on a level playing field with other market participants, including during the final ten minutes of trading before the closing auction.

In the Order Instituting Proceedings, the Commission emphasizes the need to maintain "an appropriate balance between the benefits and obligations of being a DMM."[10] However, it is important to note that the benefit that was the primary genesis for this specific NYSE Rule – the advance "look" at incoming orders – has long been removed. The removal of this benefit led the Commission to conclude that it was not necessary to impose the negative obligations of specialists on the activities of DMMs.[11] Whereas specialists were generally only permitted to trade for their

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[6] Securities Exchange Act Release No. 58845, 73 FR 64379, 64388 (October 29, 2008) (the "**New Market Model Pilot**").

[7] Securities Exchange Act Release No. 61358, 79 FR 3593, 3595 (January 21, 2010).

[8] *Id.*

[9] *See* Bats, Market Share Charts, *available at* https://www.bats.com/us/equities/market_statistics/venue/market/all_market/.

[10] Order Instituting Proceedings at 11389.

[11] *See* New Market Model Pilot at 64382.

own account when reasonably necessary to maintain a fair and orderly market, DMMs are not subject to this restriction.[12] Similarly, we recommend that the Commission approve the Proposal to remove a restriction on DMMs that is unrelated to a specific benefit and no longer serves its intended purpose.

II. Marking the Close and Market Manipulation Are Prohibited

In the context of evaluating this Proposal, it is important to note that existing NYSE and Commission rules prohibit all market participants, including DMMs, from engaging in market manipulation, including around the close. In addition, DMMs have specific obligations relating to fair and orderly trading, including:[13]

- NYSE Rule 104(a) - engaging in a course of dealing for their own account to assist in the maintenance of a fair and orderly market insofar as reasonable practicable;
- NYSE Rule 104(f)(ii) - acting as reasonably necessary to ensure appropriate depth and to maintain reasonable price variations between transactions, and to prevent unexpected variations in trading;
- NYSE Rule 123D(a) - opening and re-openings must be fair and orderly, reflecting the DMM's professional assessment of market conditions at the time; and
- NYSE Rule 104(h) - obligations to re-enter the market when reaching across to execute against available interest.

These rules are reasonably designed to prevent DMMs from inappropriately influencing or manipulating the close in light of DMMs' responsibility for closing auctions. Since the majority of trading in NYSE-listed securities now takes place away from NYSE, and DMMs do not benefit from the advance "look" at incoming orders that specialists once did, the additional prohibition contained in the NYSE Rule is no longer necessary.

III. The NYSE Rule Creates an Uneven Playing Field in the Current Market Structure

The NYSE Rule only prohibits certain trading activity on a single exchange. However, in the current equity market structure, trading activity and price formation occurs across all of the trading centers that are active in the relevant security, impacting the closing price of that security. Further, as discussed above, the majority of trading activity in NYSE-listed securities now occurs away from NYSE.

As a result, the NYSE Rule disadvantages both DMMs and NYSE and serves as an undue burden on competition during the last ten minutes of trading before the close. Unlike other market participants, DMMs are restricted from setting a new high (or low) price during these ten minutes,

[12] *See* New Market Model Pilot at 64380.

[13] *See* the Proposal.

which can affect their ability to provide competitive quotations. This can hinder price discovery and negatively impact the liquidity available to investors on NYSE. In addition, trading activity may migrate to other venues where participants are not subject to this same artificial restriction.

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For the foregoing reasons, Citadel believes that the Proposal should be approved. We appreciate the opportunity to provide comments on the Proposal. Please feel free to call the undersigned at [redacted] with any questions regarding these comments.

Respectfully,

/s/ Stephen John Berger

Managing Director, Government and Regulatory Policy