

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-80073; File No. SR-NYSEMKT-2017-08)

February 21, 2017

Self-Regulatory Organizations; NYSE MKT LLC; Notice of Filing of Proposed Rule Change to Amend Rule 925.1NY Regarding Market Maker Quotations, Including to Adopt a Market Maker Light Only Quotation

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934 (the “Act”)² and Rule 19b-4 thereunder,³ notice is hereby given that on February 10, 2017, NYSE MKT LLC (the “Exchange” or “NYSE MKT”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Rule 925.1NY regarding Market Maker Quotations, including to adopt a Market Maker Light Only Quotation. The proposed rule change is available on the Exchange’s website at www.nyse.com, at the principal office of the Exchange, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places

¹ 15 U.S.C.78s(b)(1).

² 15 U.S.C. 78a.

³ 17 CFR 240.19b-4.

specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to modify Rule 925.1NY regarding Market Maker Quotations. Rule 925.1NY(a) provides that a Market Maker may enter quotes in the option issues included in its appointment. The Exchange proposes to amend Rule 925.1NY(a) to define Market Maker quotes, add a new quote type, and specify how such quotes would be processed when a series is open for trading.

Defining Market Maker Quotes and adopting Market Maker Light Only Quotes

First, the Exchange proposes to define Market Maker quotes to provide that “[t]he term ‘quote’ or ‘quotation’ means a bid or offer entered by a Market Maker that updates the Market Maker’s previous bid or offer, if any.”⁴ This proposed definition, which would add clarity, transparency, and internal consistency to Exchange rules, is identical or substantially identical to the way quotes are defined on at least two other options exchanges.⁵ Consistent with this change, the Exchange also proposes to modify the current definition of “Quote with Size” to include a cross reference to the proposed definition of quotation, which would add clarity and transparency to Exchange rules.⁶

⁴ See proposed Rule 925.1NY(a)(1).

⁵ See, e.g., International Securities Exchange Rule 100(42). See also BOX Options Exchange LLC Rule 100(a)(55) (providing that “[t]he term ‘quote’ or ‘quotation’ means a bid or offer entered by a Market Maker as a firm order that updates the Market Maker’s previous bid or offer, if any”).

⁶ See proposed Rule 900.2NY(65) (providing that “the term ‘Quote with Size’ means a quotation (as defined in Rule 925.1NY (a)(1)) to buy or sell a specific number of option

Second, the Exchange proposes to add a Market Maker Light Only Quotation (“MMLO”) to provide Market Makers the option to designate incoming quotes to trade solely with displayed interest on the Consolidated Book.⁷ This proposed change would allow Market Makers to designate quotes as MMLO to prevent such quotes from trading with undisplayed liquidity upon arrival. Once an MMLO is added to the Consolidated Book, the MMLO designation no longer applies and any unexecuted portion could trade with displayed and undisplayed interest. The Exchange believes that this functionality would give Market Makers greater control over the circumstances in which their quotes interact with contra-side trading interest on the Exchange. This increase in control is desirable from the perspective of Market Makers because it is difficult for them to account for undisplayed liquidity in their quoting models.⁸ Because the options market is quote driven, Market Makers are vital to the price discovery process, the Exchange believes that the proposed MMLO would provide Market Makers with a greater level of determinism, in terms of managing their exposure, and thus may encourage more aggressive liquidity provision, resulting in more trading opportunities and tighter spreads. Accordingly, the Exchange believes that the proposal would improve overall market quality and enhance competition on the Exchange to the benefit to all market participants.^{9, 10} The Exchange also

contracts at a specific price that a Market Maker has submitted to the System through an electronic interface”).

⁷ See proposed Rule 925.1NY(a)(2).

⁸ The Exchange understands that, while a Market Maker’s quoting algorithm can take into account displayed liquidity in the marketplace, the algorithm may not be able to accurately account for the risk of interacting with undisplayed liquidity.

⁹ The Exchange notes that the concept of allowing market participants, including Market Makers, to avoid trading with undisplayed liquidity is available on other options exchanges. See e.g., NYSE Arca, Inc. (“Arca”) Rule 6.62(v) (defining PNP-Light Orders as non-routable orders that are only eligible to execute against displayed liquidity).

¹⁰ The Exchange notes that another options exchange – Arca – previously offered (and later eliminated) a Post No Preference Light Only Quotation (“PNPLO”), which, like the

notes that other options exchanges have recently adopted quote types designed to strengthen market making.¹¹

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Specifying the Treatment of Market Maker Quotes, including MMLOs

The Exchange also proposes to modify and add detail regarding how Market Maker quotes, including MMLOs, would be processed when a series is open for trading. As discussed below, the Exchange's proposal to modify the processing of Market Maker quotations aligns with the NMS plan for Options Order Protection And Locked/Crossed Market Plan ("Plan"), to which the Exchange is a party.¹²

MMLO, allowed Market Makers to designate certain quotations to only interact with displayed liquidity. The Commission approved the PNPLO, in part, on grounds that market participants, including Market Makers, could achieve functionality similar to the PNPLO through use of the PNP-Light Order and that the PNPLO offer similar functionality for use by Market Makers when quoting. See Securities Exchange Act Release Nos. 67252 (June 25, 2012), 77 FR 38879 (June 29, 2012) (SR-NYSEArca-2012-05) (order approving adoption of PNPLO, applicable to Penny Pilot issues only); 68339 (December 3, 2012), 77 FR 73109 (December 7, 2012) (SR-NYSEArca-2012-130) (immediately effective filing extending the PNPLO to non-Penny Pilot issues). The PNPLO was eliminated approximately one year after it was adopted because the functionality was not implemented in the time period contemplated. See Securities Exchange Act Release No. 34-69641 (May 28, 2013), 78 FR 33134 (June 3, 2013) (SR-NYSEArca-2013-51) (immediately effective filing deleting reference to the PNPLO from Rule 6.62(cc)).

¹¹ The Exchange notes that BOX recently added functionality to only accept quotes that add liquidity. See Securities Exchange Act Release Nos. 79311 (October 3 [sic], 2016), 81 FR 83322 (November 15 [sic], 2016) (SR-BOX-2016-45) (order approving change to only accept liquidity-adding quotes); 78946 (September 27, 2016), 81 FR 68069 (October 3, 2016) (notice). See also BOX IM-8050-3 (providing that "[i]f an incoming quote is marketable against the BOX Book and will execute against a resting order or quote, it will be rejected").

¹² See Plan, dated April 14, 2009, available here, http://www.optionsclearing.com/components/docs/clearing/services/options_order_protection_plan.pdf. See also Securities Exchange Act Release No. 60405 (July 30, 2009), 74 FR 39362 (August 6, 2009) (File No. 4-546) (order approving the Plan). Consistent with the Plan, the rules of the Exchange include prohibitions against trade-throughs and a

The Exchange proposes to change the treatment of incoming quotations, including the conditions under which quotes would be cancelled or rejected. Specifically, as proposed, an incoming quotation would only trade against contra-side interest in the Consolidated Book at prices that would not trade through interest on another Market Center.¹³ Any untraded size of an incoming quote would be added to the Consolidated Book, unless it locks or crosses interest on another Market Center or if the quote is an MMLO and locks or crosses undisplayed interest.¹⁴ The proposed rule would state that when such quantity of an incoming quote is cancelled (as opposed to being rejected outright), the Exchange would also cancel the Market Maker's current quote on the opposite side of the market. In other words, both sides of the Market Maker's quote residing on the Consolidated Book would be cancelled, which allows a Market Maker to refresh both its bid and offer simultaneously.

In addition, as proposed, an incoming quotation would be rejected if it locks or crosses interest on another Market Center and if it cannot trade with interest in the Consolidated Book at prices that do not trade through another Market Center.¹⁵ An incoming quotation designated as MMLO would be rejected if it locks or crosses undisplayed interest and cannot trade with displayed interest in the Consolidated Book at prices that do not trade through another Market Center.¹⁶ The proposed rule would specify that when an incoming quote is rejected outright (as opposed to being cancelled after a partial fill), the Exchange would also cancel the Market

pattern or practice of displaying certain quotations that lock or cross away markets. See, e.g., Rules 991NY, 992NY. See also infra note 20.

¹³ See proposed 925.1NY(a)(3)(A). See Rule 900.2NY(36) (defining Market Center as “a national securities exchange that has qualified for participation in the Options Clearing Corporation pursuant to the provisions of the rules of the Options Clearing Corporation”).

¹⁴ See proposed Rule 925.1NY(a)(3)(B)(i).

¹⁵ See proposed Rule 925.1NY(a)(3)(C)(i).

¹⁶ See proposed Rule 925.1NY(a)(3)(C)(ii).

Maker's current quote on the same side of the market.¹⁷ Such treatment recognizes that the Market Maker attempted (unsuccessfully) to update its bid or offer price and allows the Market Maker to refresh that side of its quote.

In addition, when a series is open for trading, a quote will trade only against interest in the Consolidated Book and will not route. The Exchange does not route Market Maker quotations because such quotes are designed to meet the Market Maker's obligation to have displayed quotations on the Exchange. The Exchange proposes to specify this functionality in Exchange rules.¹⁸

The Exchange believes that processing Market Maker quotations, as described in the proposed rules, aligns with the Plan.¹⁹ The Plan obligates the participating exchanges to provide order protection, including addressing locked and crossed markets and the potential for trade-throughs in certain options classes.²⁰ The Plan establishes various obligations for participating exchanges, including that Market Makers should "reasonably avoid displaying, and shall not engage in a pattern or practice of displaying, any quotations that lock or cross" the best bid or offer on another Market Center.²¹ The Plan further obligates participating exchanges to conduct surveillance of their respective markets on a regular basis to ascertain the effectiveness of the policies and procedures to prevent trade-throughs and to take prompt action to remedy

¹⁷ See proposed Rule 925.1NY (a)(3)(C).

¹⁸ See proposed Rule 925.1NY(a)(3), (D).

¹⁹ See Plan, supra note 12.

²⁰ See e.g., Securities Exchange Act Release No. 60526 (August 18, 2009), 74 FR 43185 (August 26, 2009) (SR-NYSEAmex-2009-19) (adopting and updating Exchange rules to implement the Plan).

²¹ See Plan at Section 6(c), supra note 12.

deficiencies in such policies and procedures.²² Because Market Maker quotations do not route, and incoming quotes, or portions thereof, would reject or cancel if such quotes locked or crossed away markets, the Exchange believes the proposal is consistent with the requirements of the Plan. In addition, the proposed processing of quotes is consistent with the Plan because it avoids trading-through better prices on other exchange and locking or crossing markets. In addition, the Exchange believes this proposal would assist Market Makers in maintaining a fair and orderly market, as it would encourage Market Makers to provide greater liquidity.

The Exchange notes that this proposal does not relieve a Market Maker of its continuous quoting, or firm quote, obligations pursuant to Rules 925.1NY and 970NY, respectively. Further, the Exchange notes that Market Makers would still be able to send orders in (and out of) classes to which they are appointed, as orders are not affected by this proposal.

Implementation

The Exchange will announce the implementation of the proposed rule change by Trader Update, which implementation will be no later than 30 days after the approval of this rule change.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Securities Exchange Act of 1934 (the “Act”),²³ in general, and furthers the objectives of Section 6(b)(5) of the Act,²⁴ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect

²² See Plan at Section 5(a), *supra* note 12.

²³ 15 U.S.C. 78f(b).

²⁴ 15 U.S.C. 78f(b)(5).

the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The proposal to add the definition of Market Maker quotes would provide clarity and transparency to Exchange rules to the benefit of investors as the additional clarity would promote just and equitable principles of trade and remove impediments to, and perfect the mechanism of, a free and open market and a national market system. The proposed rule amendments would also provide internal consistency within Exchange rules and operate to protect investors and the investing public by making the Exchange rules easier to navigate and comprehend. Because the proposed definition of quotes is identical or substantially identical to definitions provided on other options exchanges, the proposal presents no new or novel issues.²⁵

The proposal to offer to Market Makers the ability to designate quotes as MMLO would remove impediments to and perfect the mechanism of a free and open market and a national market system because it would provide Market Makers with increased control over interactions with contra-side liquidity. Specifically, the proposal would improve market making on the Exchange because it would prevent incoming Market Maker quotes from trading with resting undisplayed interest, which interest is difficult to take into account in quoting models.

Accordingly, the Exchange believes that the proposed MMLO designation would provide Market Makers with a greater level of determinism, in terms of managing their exposure, and would encourage more aggressive liquidity provision, resulting in more trading opportunities for market participants and tighter spreads. Accordingly, the Exchange believes that the proposal would

²⁵ See supra note 5.

improve overall market quality and improve competition on the Exchange, to the benefit of all market participants.²⁶

Because market participants that enter undisplayed interest (e.g., PNP-Blind Orders)²⁷ are opting not to have their interest displayed, the Exchange believes it is consistent with the Act for Market Makers to choose to designate their quotes not to trade with such undisplayed interest.²⁸ For the forgoing reasons, the Exchange believes that the proposal to offer to Market Makers the option to designate their quotes as MMLO is not unfairly discriminatory. The Exchange also believes that such offering would protect investors and the public interest because it may contribute to more aggressive quoting by Market Makers, which should increase the quality of the Exchange's market and benefit investors.

The proposal to add detail and amend the treatment of Market Maker quotes is consistent with, and facilitates the Exchange meeting its obligations under the Plan and, thus, would remove impediments to, and perfect the mechanism of, a free and open market and a national market system. The Exchange believes the proposed processing of quotes is consistent with the Plan because it avoids trading through better prices on other exchanges and is designed to avoid locking and crossing markets. By preventing Market Makers from locking or crossing trading interest on away Market Centers, the proposal would prevent fraudulent and manipulative acts and practices and would promote just and equitable principles of trade to the benefit of all market

²⁶ Moreover, the Exchange notes that the concept of allowing market participants, including Market Makers, to avoid trading with undisplayed liquidity is available on other options exchanges. See supra note 9.

²⁷ See Rule 900.3NY(x) (providing that a PNP (Post No Preference) Blind Order is a Limit Order to buy or sell that is to be executed in whole or in part on the Exchange, and the portion not so executed is to be ranked in the Consolidated Book, without routing any portion of the order to another Market Center).

²⁸ In this regard, the Exchange notes that undisplayed liquidity is not afforded trade-through protection under Section 5 of the Plan. See Plan, supra note 12.

participants. The Exchange also believes the proposal regarding how the Exchange processes quotes in the event that an incoming quote is rejected, or a portion thereof is cancelled, would promote just and equitable principles of trade. Specifically, the proposed rules would enable Market Makers to simultaneously update both sides of their resting quote when one side of the quote received a partial fill but was subsequently cancelled and, where one side of a quote is rejected and not booked, to leave undisturbed that opposite-side interest because it remains valid. The Exchange believes this proposed handling of quotes would assist Market Makers in maintaining a fair and orderly market as it would encourage Market Makers to provide greater volumes of liquidity, which would add value to market making on the Exchange.

The Exchange believes that the entire proposal is just, equitable and not unfairly discriminatory, as it would apply to all Market Makers on the Exchange. Further, the proposal would protect investors and the public interest by providing a more robust market, including because the proposal may contribute to more aggressive quoting by Market Makers. The Exchange believes that the proposal would lead to enhanced liquidity on the Exchange, which in turn will benefit and protect investors and the public interest through the potential for greater volume of orders and executions on the Exchange.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange believes the proposal adds value to market making on the Exchange. The Exchange does not believe the proposal would impose a burden on competition among the options exchanges because of vigorous competition for order flow among the options exchanges. In this highly competitive market, market participants can easily and readily direct order flow to

competing venues. The proposal does not impose an undue burden on intramarket competition because the proposed change would apply to all Market Makers on the Exchange. The proposal is structured to offer the same enhancement to all Market Makers, regardless of size, and would not impose a competitive burden on any participant.

The proposed MMLO, which provides Market Makers with enhanced determinism over their quotes, may contribute to more aggressive quoting by Market Makers, resulting in more trading opportunities and tighter spreads. To the extent this purpose is achieved, the MMLO would enhance the market making function on the Exchange, which would improve overall market quality and improve competition on the Exchange to the benefit of all market participants.

The Exchange believes the proposal is pro-competitive because when an exchange offers enhanced functionality that distinguishes it from other exchanges and participants find it useful, it has been the Exchange's experience that competing exchanges will move to adopt similar functionality. Thus, the Exchange believes that this type of competition amongst exchanges is beneficial to the market place as a whole as it can result in enhanced processes, functionality, and technologies.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

No written comments were solicited or received with respect to the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NYSEMKT-2017-08 on the subject line.

Paper comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEMKT-2017-08. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m.

and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSEMKT-2017-08 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁹

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²⁹ 17 CFR 200.30-3(a)(12).