

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-78801; File No. SR-NYSEARCA-2016-123)

September 9, 2016

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Proposed Rule Change Amending Rule 7.46 Relating to the Tick Size Pilot Program

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the “Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that, on August 25, 2016, NYSE Arca, Inc. (the “Exchange” or “NYSE Arca”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I, II, and III 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 7.46 to (1) describe system functionality requirements necessary to implement the Plan to Implement a Tick Size Pilot Program submitted to the Commission pursuant to Rule 608 of Regulation NMS<sup>4</sup> under the Act (the “Plan”) and (2) clarify the operation of certain exceptions to the Trade-at Prohibition<sup>5</sup> on Pilot Securities in the third test group.. The proposed rule change is available on the Exchange’s website at

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<sup>1</sup> 15 U.S.C.78s(b)(1).

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

<sup>4</sup> 17 CFR 242.608.

<sup>5</sup> Rule 7.6(e)(4)(A) defines the “Trade-at Prohibition” to mean the prohibition against executions by a Trading Center of a sell order for a Pilot Security at the price of a Protected Bid or the execution of a buy order for a Pilot Security at the price of a Protected Offer during regular trading hours.

[www.nyse.com](http://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 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 Exchange proposes to amend Rule 7.46 to (1) describe system functionality requirements necessary to implement the Plan<sup>6</sup> and (2) clarify the operation of certain exceptions to the Trade-at Prohibition<sup>7</sup> on Pilot Securities in the third test group (“Test Group Three”).<sup>8</sup>

The Plan is designed to study and assess the impact of increment conventions on the liquidity and trading of the common stocks of small capitalization companies. The Exchange proposes to amend Rule 7.46, which has been adopted on a two-year pilot period that coincides with the pilot period for the Plan, which is currently scheduled to begin on October 3, 2016.

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<sup>6</sup> See Securities and Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27513 (File No. 4-657) (“Tick Plan Approval Order”). See, also, Securities and Exchange Act Release No. 76382 (November 6, 2015) (File No. 4-657), 80 FR 70284 (File No. 4-657) (November 13, 2015), which extended the pilot period commencement date from May 6, 2015 to October 3, 2016. The Plan was submitted to the Commission pursuant to Rule 608 of Regulation NMS. 17 CFR 242.608.

<sup>7</sup> Unless otherwise specified, capitalized terms used in this rule filing are based on the defined terms of the Plan.

<sup>8</sup> See *infra* notes 14-17 and accompanying text for a description of Test Group Three.

## Background

On August 25, 2014, NYSE Group, Inc., on behalf of Bats BZX Exchange, Inc. (f/k/a BATS Exchange, Inc.), Bats BYX Exchange, Inc. (f/k/a BATS Y-Exchange, Inc.), Chicago Stock Exchange, Inc., Bats EDGA Exchange, Inc. (f/k/a EDGA Exchange, Inc.), Bats EDGX Exchange, Inc. (f/k/a EDGX Exchange, Inc.), Financial Industry Regulatory Authority, Inc. (“FINRA”), NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, the Nasdaq Stock Market LLC, New York Stock Exchange LLC, NYSE MKT LLC, and the Exchange (collectively “Participants”), filed with the Commission, pursuant to Section 11A of the Act<sup>9</sup> and Rule 608 of Regulation NMS thereunder, the Plan to Implement a Tick Size Pilot Program.<sup>10</sup> The Participants filed the Plan to comply with an order issued by the Commission on June 24, 2014 (the “June 2014 Order”).<sup>11</sup> The Plan was published for comment in the Federal Register on November 7, 2014,<sup>12</sup> and approved by the Commission, as modified, on May 6, 2015.<sup>13</sup>

The Plan is designed to allow the Commission, market participants, and the public to study and assess the impact of increment conventions on the liquidity and trading of the common stocks of small capitalization companies. The Tick Size Pilot Program will enable the Commission to assess whether wider tick sizes would enhance the market quality of Pilot Securities for the benefit of issuers and investors. Each Participant is required to comply with,

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<sup>9</sup> 15 U.S.C. 78k-1.

<sup>10</sup> See Letter from Brendon J. Weiss, Vice President, Intercontinental Exchange, Inc., to Secretary, Commission, dated August 25, 2014.

<sup>11</sup> See Securities Exchange Act Release No. 72460 (June 24, 2014), 79 FR 36840 (June 30, 2014).

<sup>12</sup> See Securities and Exchange Act Release No. 73511 (November 3, 2014), 79 FR 66423 (File No. 4-657) (Tick Plan Filing).

<sup>13</sup> See Tick Plan Approval Order, supra note 6. See, also, Securities Exchange Act Release No. 77277 (March 3, 2016), 81 FR 12162 (March 8, 2016) (File No. 4-657), which amended the Plan to add National Stock Exchange, Inc. as a Participant.

and to enforce compliance by its member organizations, as applicable, with the provisions of the Plan.

The Tick Size Pilot Program will include stocks of companies 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. The Tick Size Pilot Program will consist of a control group of approximately 1400 Pilot Securities and three test groups with 400 Pilot Securities in each selected by a stratified sampling.<sup>14</sup>

During the pilot, Pilot Securities in the control group will be quoted at the current tick size increment of \$0.01 per share and will trade at the currently permitted increments. Pilot Securities in the first test group (“Test Group One”) will be quoted in \$0.05 minimum increments but will continue to trade at any price increment that is currently permitted.<sup>15</sup> Pilot Securities in the second test group (“Test Group Two”) will be quoted in \$0.05 minimum increments and will trade at \$0.05 minimum increments subject to a midpoint exception, a retail investor exception, and a negotiated trade exception.<sup>16</sup> Pilot Securities in Test Group Three will be subject to the same terms as Test Group Two and also will be subject to the “Trade-at” requirement to prevent price matching by a person not displaying at a price of a Trading Center’s “Best Protected Bid or “Best Protected Offer,” unless an enumerated exception applies.<sup>17</sup> In addition to the exceptions provided under Test Group Two, an exception for Block Size orders

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<sup>14</sup> See Section V of the Plan for identification of Pilot Securities, including criteria for selection and grouping.

<sup>15</sup> See Section VI(B) of the Plan. Pilot Securities in Test Group One will be subject to a midpoint exception and a retail investor exception.

<sup>16</sup> See Section VI(C) of the Plan.

<sup>17</sup> See Section VI(D) of the Plan.

and exceptions that closely resemble those under Rule 611 of Regulation NMS (“Rule 611”)<sup>18</sup> will apply to the Trade-at requirement.

The Plan requires the Exchange to establish, maintain, and enforce written policies and procedures that are reasonably designed to comply with applicable quoting and trading requirements specified in the Plan. Accordingly, the Exchange adopted paragraphs (a) and (c)-(e) of Rule 7.46 to require ETP Holders to comply with the quoting and trading provisions of the Plan.<sup>19</sup> The Exchange also adopted paragraph (b) of Rule 7.46 to require ETP Holders to comply with the data collection provisions under Appendix B and C of the Plan.<sup>20</sup>

#### Trade-at Intermarket Sweep Orders

The Plan defines a Trade-at Intermarket Sweep Order (“ISO”) as a limit order for a Pilot Security that, when routed to a Trading Center, is identified as an ISO, and simultaneous with the routing of the limit order identified as an ISO, 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) for the Pilot Security with a price that is equal to the limit price of the limit order identified as an ISO. These additional routed orders also must be marked as ISOs.<sup>21</sup>

The Exchange clarified the use of an ISO in connection with the “Trade-at” requirement in Test Group Three by adopting a comprehensive definition of “Trade-at ISO” under Rule

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<sup>18</sup> 17 CFR 242.611.

<sup>19</sup> See Securities Exchange Act Release No. 77947 (May 31, 2016), 81 FR 36361 (June 6, 2016) (SR-NYSEArca-2016-76) (“Quoting & Trading Rules Proposal”).

<sup>20</sup> See Securities Exchange Act Release No. 77484 (March 31, 2016), 81 FR 20024 (April 6, 2016) (SR-NYSEArca-2016-52).

<sup>21</sup> See Plan, Section I(MM).

7.46(a)(1)(D).<sup>22</sup> The Exchange now proposes to further clarify that, when a Trade-at ISO is routed to a Trading Center, when simultaneously routing additional limit orders 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, such additional limit orders can be routed as either Trade-at ISOs or ISOs. Therefore, the Exchange is proposing to distinguish Trade-at from ISOs by adding the phrase “or Intermarket Sweep Orders” to the end of Rule 7.46(a)(1)(D)(ii), so that any such additional routed orders sent to execute against the Trade-at ISO limit order would need to be marked as either Trade-at ISOs or ISOs, as applicable.

Likewise, the Exchange is proposing to amend Rule 7.46(e)(4)(C)(x) to add the phrase “or Intermarket Sweep Orders” into the Trade-at ISO exemption to the Trade-at Prohibition, to clarify that a Trading Center can simultaneously route Trade-at ISOs or ISOs to execute against the full displayed size of the Protected Quotation that was traded at.

#### Block Size Exemption to Trade-at

The Plan defines Block Size as an order (1) of at least 5,000 shares or (2) for a quantity of stock having a market value of at least \$100,000. The Block Size exception to the Trade-at Prohibition permits a Trading Center to immediately execute a Block Size order against displayed and undisplayed liquidity at a price equal to the National Best Bid or National Best

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<sup>22</sup> Rule 7.46(a)(1)(D) defines Trade-at Intermarket Sweep Order to mean a limit order for a Pilot Security that meets the following requirements:

- (i) When routed to a Trading Center, the limit order is identified as a Trade-at Intermarket Sweep Order; and
- (ii) Simultaneously with the routing of the limit order identified as a Trade-at Intermarket Sweep Order, one or more additional limit orders, as necessary, are routed to execute against the full 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, for the Pilot Security with a price that is better than or equal to the limit price of the limit order identified as a Trade-at Intermarket Sweep Order. These additional routed orders also must be marked as Trade-at Intermarket Sweep Orders.

Offer, as applicable, without satisfying all Protected Quotations at the National Best Bid or National Best Offer, as applicable.<sup>23</sup>

The Exchange is proposing to amend Rule 7.46(e)(4)(C)(iii) to clarify how the Block Size exception to the Trade-at Prohibition would operate under the requirements of the Plan. The Exchange proposes to delete subparagraph (C) of Rule 7.46(e)(4)(C)(iii), which state that, to qualify for the Block Size exception, the order may not be executed on multiple Trading Centers. By deleting this requirement, the Block Size exception to the Trade At Prohibition would apply to an order received by a market that has sufficiently liquidity to execute such Block Size, irrespective of whether the receiving market routes a portion of the Block Size order to another Trading Center to comply with Rule 611 or Regulation NMS. Any routed interest that returns unexecuted may be immediately executed under the same Block Size exception, provided such interest remains marketable.

#### Proposed Amendments to Rule 7.46 for Tick-Pilot Specific System Changes

The Exchange proposes to add paragraph (f) of Rule 7.46 to describe changes to system functionality necessary to implement the Plan. Paragraph (f) of Rule 7.46 would set forth the Exchange's specific procedures for handling, executing, re-pricing and displaying of certain order types and order type instructions applicable to Pilot Securities in Test Groups One, Two, and Three.

In determining the scope of these proposed changes to implement the Plan, the Exchange reviewed its order types and identified which orders and instructions would be inconsistent with the Plan and propose to modify the operation of such order types so they will comply with the Plan, or, to the extent inconsistent with the Plan, eliminate them. These proposed changes are

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<sup>23</sup> See Plan, Section VI(D).

designed to comply with the Plan and to allow the Exchange to meet its regulatory obligations under the Plan.

As part of this review, the Exchange identified order types that were designed to comply with the requirements of Regulation NMS. Among other things, Regulation NMS requires a trading center to have policies and procedures to reasonably avoid displaying quotations that lock or cross any protected quotation<sup>24</sup> and to prevent trade-throughs in NMS stocks that do not fall within an exception enumerated in Rule 611(b) to Regulation NMS.<sup>25</sup> As such, under Regulation NMS, an exchange may rank undisplayed orders at the price of a protected quotation on an away market and execute such non-displayed orders at the price of a protected quotation on an away market. By contrast, in Test Group Three, an undisplayed order may not trade at the price of a protected quotation on an away market. Accordingly, as described below, in order to comply with the Plan for Test Group Three securities, the Exchange is proposing to modify the behavior of specified orders that are currently permitted to trade undisplayed at the price of the PBBO or NBBO.

As described in greater detail below, the Exchange is also proposing to reject specified orders in Pilot Securities in Test Group Three because the operation of such order types are, by their terms, inconsistent with the requirements of the Trade At Prohibition.

#### Proposed Rule 7.46(f)(1) – Trade-at Intermarket Sweep Orders

Proposed Rule 7.46(f)(1) would describe the handling of Trade-at Intermarket Sweep Orders (“TA ISO”) on the Exchange. As described above, the requirements for an ETP Holder that enters a TA ISO are specified in Rule 7.46(a)(1)(D)(ii) and differ from the requirements for

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<sup>24</sup> See 17 CFR 242.610(d).

<sup>25</sup> See 17 CFR 242.611(b).



an ETP Holder that enters an IOC ISO (as specified in Rule 7.31P(e)(3)(A)). However, the Exchange will handle a TA ISO the same way it handles an IOC ISO in all securities.

As proposed in Rule 7.46(f)(1)(A), the Exchange would accept TA ISOs in all securities. Further, TA ISOs must be designated as IOC, may be designated with a “No Midpoint Execution” modifier, may not be designated with a minimum trade size, and do not route. These requirements are based on existing IOC functionality, as specified in Rule 7.31P(b)(2) governing IOC Modifiers, and IOC ISO functionality, as specified in Rule 7.31P(e)(3)(B).

In addition, proposed Rule 7.46(f)(1)(B) would provide that a TA ISO would be immediately traded with contra-side displayed and non-displayed interest in the NYSE Arca Book up to its full size and limit price and the quantity and the quantity not so traded will be immediately and automatically cancelled. This proposed rule text is based on current Rule 7.31P(e)(3)(B).

Proposed Rule 7.46(f)(2) – Pilot Securities in Test Groups One, Two, and Three

Proposed Rule 7.46(f)(2) would describe the procedures for handling, executing, re-pricing and displaying of certain order types and order type instructions applicable to Pilot Securities in Test Groups One, Two and Three.

- Proposed Rule 7.46(f)(2)(A) would provide that references in Exchange rules to the minimum price variation (“MPV”), as defined in Rule 7.6, would instead mean the quoting MPV specified in paragraphs (c), (d), and (e) of this Rule. This proposed rule text promotes transparency in Exchange rules to be clear that if a rule specifies that an order will be priced based off of the MPV, for Pilot Securities in Test Groups One, Two, and Three, the applicable MPV will be the

quoting MPV required by the Plan.<sup>26</sup> For example, Rule 7.31P(e)(1) provides that if an Arca Only Order is marketable against Exchange interest or would lock or cross a protected quotation in violation of Rule 610(d) of Regulation NMS, the order to buy (sell) will be re-priced as provided for in Rule 7.31P(e)(1)(A)(i)-(iv), including being assigned a display price one MPV below (above) the PBO (PBB). For Pilot Securities in Test Groups One, Two, and Three, the applicable MPV would be \$0.05.

Proposed Rule 7.46(f)(2)(A) would further provide that references to truncating to the MPV in Exchange rules would instead mean rounding down to the applicable quoting MPV for Pilot Securities in Test Groups One, Two and Three. For example, if a value would come to a \$0.09 price, it would be rounded down to a \$0.05 increment, which is the nearest quoting MPV for Pilot Securities in Test Groups One, Two, and Three.

- Proposed Rule 7.46(f)(2)(B) would provide that Mid-Point Liquidity Orders (“MPL Orders”)<sup>27</sup> must be entered with a limit price in a \$0.05 pricing increment. While MPL Orders in all Test Groups would be eligible to trade at the midpoint of the PBBO, which may not be in a \$0.05 pricing increment, the Exchange proposes that the limit price specified for such orders must be in the quoting MPV for Test Groups One, Two, and Three.

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<sup>26</sup> See, e.g., Rules 7.31P(a)(1)(B)(i) and (ii), 7.35P(a)(10)(A) and (B), and 7.31P(e).

<sup>27</sup> An MPL Order is a Limit order priced at the midpoint of the PBBO and not displayed. An order designated as an MPL Order will not route or trade-through a Protected Quotation. MPL Orders shall have a minimum order entry size of one share and such orders, if entered without a limit price or with a FOK modifier, are rejected. As described in Rules 7.46(c), (d)(1) and (e)(1), orders priced to trade at the midpoint of the PBBO, i.e., MPL Orders, may be ranked in increments less than \$0.05.

#### Proposed Rule 7.46(f)(3) – Pilot Securities in Test Groups One and Two

Proposed Rule 7.46(f)(3) would describe the procedures for handling, executing, re-pricing and displaying of certain order types and order type instructions applicable to Pilot Securities in Test Groups One and Two.

- A Market Pegged Order to buy (sell), as set forth in Rule 7.31P(h)(1)(C), may include an offset value that will set the working price below (above) the PBO (PBB) by the specified offset, which may be specified up to two decimals.

Proposed Rule 7.46(f)(3) would provide that an offset included with a Market Pegged Order in Pilot Securities in Test Groups One and Two must be in pricing increments of \$0.05.

#### Proposed Rule 7.46(f)(4) – Pilot Securities in Test Groups Two and Three

Proposed Rule 7.46(f)(4) would describe the procedures for handling, executing, re-pricing and displaying of certain order types and order type instructions applicable to Pilot Securities in Test Groups Two and Three.

- A Retail Price Improvement Order, as set forth in Rule 7.44P(a)(4), consists of non-displayed interest in NYSE Arca-listed securities and UTP Securities, excluding NYSE-listed (Tape A) securities, that would trade at prices better than the PBB or PBO by at least \$0.001 and that is identified as such. Consistent with the requirements of the Plan, which requires a minimum of \$0.005 price improvement in retail programs in Test Groups Two and Three instead of the \$0.001 price improvement specified in Rule 7.44P, proposed Rule 7.46(f)(4) would provide that Retail Price Improvement Orders in Pilot Securities in Test Groups Two and Three must be entered in pricing increments of \$0.005.

### Proposed Rule 7.46(f)(5) – Pilot Securities in Test Group Three

Proposed Rule 7.46(f)(5) would describe the procedures for handling, executing, re-pricing and displaying certain order types and order type instructions applicable to Pilot Securities in Test Group Three. The proposed changes to order behavior for Pilot Securities in Test Group Three are designed to comply with the Trade-at Prohibition by changing the ranking and working price of orders that trade at non-displayed prices unless the execution is eligible for an exception.

- Proposed Rule 7.46(f)(5)(A)(i)-(iv) would provide for the priority of resting orders at each price point for Pilot Securities in Test Group Three. Rule 7.36P(e) sets forth the priority of orders for all other securities, including that Priority 1 – Market Orders always have first priority. In addition, protected quotations are not included in the ranking in Rule 7.36P(e) because at a price point, the Exchange may trade with all displayed and non-displayed interest before routing to a protected quotation. In order to meet the requirements of the Trade-at Prohibition, the Exchange proposes to revise the priority of resting orders, as follows:
  - First priority would be given to Priority 2 – Display Orders, which are non-marketable Limit Orders with a displayed working price. This is consistent with the Trade-at Prohibition, whose objective is to promote the display of liquidity and generally to prevent any Trading Center that is not quoting from price-matching protected quotations.
  - Second priority would be given to protected quotations of Away Markets. This would be a new priority category that would be applicable only to

Pilot Securities in Test Group Three and would reflect the requirement in the Trade-at Prohibition to trade with protected quotations on Away Markets before trading with any undisplayed interest at a price.

- Third priority would be given to Priority 3 – Market Orders, which are unexecuted Market Orders. Because unexecuted Market Orders are not displayed, such orders would have priority behind protected quotations at the same price on Away Markets. Ranking unexecuted Market Orders next is consistent with the current ranking process, pursuant to which Market Orders are ranked ahead of non-displayed Limit Orders.
- Fourth priority would be given to Priority 3 – Non-Display Orders, which are non-marketable Limit Orders for which the working price is not displayed, including reserve interest of Reserve Orders. This proposed ranking is consistent with the ranking set forth in Rule 7.36P(e). As described below, because the Exchange would not be offering Tracking Orders in Pilot Securities in Test Group Three, proposed Rule 7.46(f)(5)(A) would not need to reference Priority 4 – Tracking Orders.
- Proposed Rule 7.46(f)(5)(B) would provide that orders would not be routed to Away Markets that are not displaying protected quotations. As defined in Rule 1.1(ffP), the term “Away Market” includes alternative trading systems and other broker-dealers with which NYSE Arca Marketplace maintains an electronic linkage and which provides instantaneous responses to orders routed from the NYSE Arca Marketplace. However, because such markets do not display protected quotations, the Exchange will not route orders in Pilot Securities in Test

Group Three to such Away Markets.

- Proposed Rule 7.46(f)(5)(C) would provide that the display price of Limit Orders to buy (sell) repriced under Rule 7.31P(a)(2)(C) would be the same as provided for in that rule, but the working price of such orders would be the same as the display price. Rule 7.31P(a)(2)(C) specifies re-pricing of displayed Limit Orders to prevent the Exchange from locking or crossing the PBBO. Under such re-pricing, the Exchange assigns a display price one MPV below (above) the contra-side PBO (PBB), and a working price equal to the contra-side PBBO. As proposed, in Test Group Three, to avoid ranking orders undisplayed at the price of a protected quotation, the Exchange proposes to assign a working price equal to the re-priced display price under Rule 7.31P(a)(2)(C).
- Proposed Rule 7.46(f)(5)(D) would apply to Reserve Orders in Pilot Securities in Test Group Three, and would provide that if a Reserve Order to buy (sell) is displayed at a price that is locked or crossed by a protected offer (bid), the portion of the Reserve Order that is not displayed would be assigned a working price of \$0.05 below (above) the protected offer (bid), but if routable, would route to a protected offer (bid) based on the limit price of the order. A Reserve Order is defined in Rule 7.31P(d)(1) as a Limit or Inside Limit Order with a quantity of the size displayed and with a reserve quantity of the size ("reserve interest") that is not displayed. The displayed quantity of a Reserve Order is ranked Priority 2 - Display Orders and the reserve interest is ranked Priority 3 - Non-Display Orders. Both the display quantity and the reserve interest of an arriving marketable Reserve Order are eligible to trade with resting interest in the NYSE Arca Book

or route to Away Markets.

- Proposed Rule 7.46(f)(5)(E) would provide that if the limit price of a resting Limit Non-Displayed Order to buy (sell) is equal to or higher (lower) than the PBO (PBB), it would have a working price \$0.05 below (above) the PBO (PBB). Under Rule 7.31P(d)(2)(A), if the limit price of a Limit Non-Displayed Order to buy (sell) is equal to the PBO (PBB), it will be assigned a working price equal to the limit price, i.e., the same price as the PBO (PBB). To avoid ranking non-displayed orders at the price of the PBBO, the Exchange proposes that for Pilot Securities in Test Group Three, a Limit Non-Displayed Order would be assigned a working price one MPV off of the PBBO.
- Proposed Rule 7.46(f)(5)(F) relates to orders in Pilot Securities in Test Group Three with instructions not to route, as defined in Rule 7.31P(e).<sup>28</sup> As proposed in Rule 7.46(f)(5)(F)(i), on arrival, orders with instructions not to route would trade with resting orders in the NYSE Arca Book consistent with the terms of the order and the Trade-at Prohibition. Because an ETP Holder that enters a Day ISO to buy (sell) must simultaneously route one or more limit orders to execute against the full displayed size of any protected offer (bid), an ETP Holder entering a Day ISO would have met the obligations specified in Rule 7.46(e)(4)(C)(ix).

Accordingly, proposed Rule 7.46(f)(5)(F)(i)(A) would provide that on arrival,

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<sup>28</sup> The proposed rule would be applicable to Arca Only Orders, ALO Orders and Intermarket Sweep Orders. An Arca Only Order is a Limit Order that does not route. See Rule 7.31P(e)(1). An ALO Order is an Arca Only Order that, with some exceptions, will not remove liquidity from the NYSE Arca Book and must have a minimum on one displayed round lot. See Rule 7.31P(e)(2). An Intermarket Sweep Order is a Limit Order that does not route and meets the requirements of Rule 600(b)(30) of Regulation NMS. See Rule 7.31P(e)(3).

Day ISOs would be eligible for the exception set forth in Rule 7.46(e)(4)(C)(ix). Additionally, proposed Rule 7.46(f)(5)(F)(i)(B) would provide that an IOC ISO to buy (sell) would not trade with orders to sell (buy) ranked Priority 1 – Market Orders or Priority 3 – Non-Display Orders that are the same price as a protected offer (bid) unless the limit price of such IOC ISO is higher (lower) than the price of the protected offer (bid). As such, an arriving IOC ISO would be permitted to trade with undisplayed orders resting on the NYSE Arca Book only if the limit price of the arriving IOC ISO order is better than the PBBO. This would be permitted under the Trade-at Prohibition because to enter an IOC ISO to buy (sell) at a price higher (lower) than PBO (PBB), the entering firm would have been required to simultaneously route limit orders to execute against the full displayed size of the PBO (PBB).

- Proposed Rule 7.46(f)(5)(F)(ii) would provide that when an Arca Only Order or ALO Orders is being added to the NYSE Arca Book, such orders to buy (sell) with a limit price equal to or above (below) the PBO (PBB) would be assigned a display price and working price one MPV below (above) the PBO (PBB). Currently, Rule 7.31P(e)(1)(A)(i) provides that an Arca Only Order to buy (sell) is priced with a working price of the PBO (PBB) and a display price one MPV below (above) the PBO (PBB). For Pilot Securities in Test Group Three, to avoid assigning a working price that is equal to the PBBO and that differs from a display price, the Exchange proposes that the working price of an Arca Only would be the same as the display price.
- Proposed Rule 7.46(f)(5)(iii) would provide that once an Arca Only Order or



ALO Order to buy (sell) is resting on the NYSE Arca Book, such orders would not be eligible to trade with later-arriving orders to sell (buy) ranked Priority 2 – Display Orders priced equal to the PBO (PBB). The proposed rule further provides that a later-arriving order to buy (sell) that is eligible to trade with the PBO (PBB) may trade before such resting order. This proposed rule text makes clear that once an Arca Only is assigned a working price, it will not be repriced if the PBBO does not change. In such case, a later-arriving order that is on the same side of the market as the resting Arca Only Order and is eligible to trade with the PBBO may trade ahead of the resting Arca Only Order. For example, assume that the Exchange receives an Arca Only Order to buy (“A”) priced at \$10.15 and the PBO is \$10.10 and the Exchange Best Offer is \$10.15. On arrival, pursuant to proposed Rule 7.46(f)(5)(ii), Order A would be assigned both a working and display price of \$10.05, i.e., one MPV below the PBO of \$10.10. Assume now the Exchange receives a sell order priced at \$10.10. The Exchange publishes this offer because it matches the price of the away PBO. Assume next that the Exchange receives another Arca Only Order to buy (“B”) priced at \$10.15. On arrival, Order B will trade consistent with the terms of the order and the Trade-at Prohibition, and therefore may trade with the Exchange’s displayed offer at \$10.10. In such case, even though Order A was received before Order B, Order A would not be repriced to trade with the Exchange offer at \$10.10. Any remaining quantity of Order B would be added to the NYSE Arca Book at \$10.05, i.e., one MPV below the away market PBO. At this point, consistent with Rule 7.36P(f)(1), Order B would be assigned a working time after Order A’s working

time, and therefore, for any subsequent executions at that price point, Order A would trade before Order B.

- Proposed Rule 7.46(f)(5)(G) would provide that the only orders eligible for the exception set forth in Rule 7.46(e)(4)(C)(iii) would be Limit IOC Cross Orders that meet the Block Size definition under the Plan. A Limit IOC Cross Order is defined in Rule 7.31P(g)(1) as a two-sided order with instructions to match the buy-side with the identified sell-side at a specified price and that does not route and will cancel at the time of entry if the cross price is not between the BBO or would trade through the PBBO. Rule 7.46(e)(4)(iii), described in more detail above, sets forth the Block Size exception to the Trade-At Prohibition. The Exchange believes that orders that meet the Block Size definition and that are entered as a Limit IOC Cross Order would meet this exception because such orders are required to trade in full at price or be rejected, e.g., if at the same price as the BBO. Currently, the Limit IOC Cross Order is designed to comply with Rule 611(b) of Regulation NMS in that it is permitted to trade at the PBBO, provided it does not trade at the Exchange BBO. For Pilot Securities in Test Group Three, a Limit IOC Cross Order that meets the Block Size definition would therefore operate no differently than Limit IOC Cross Orders of any size in any other security. However, because Limit IOC Cross Orders that do not meet the Block Size definition would not be eligible to trade at the PBBO, the Exchange proposes to provide that a Limit IOC Cross Order that is at the same price as the PBBO but does not meet the Plan's Block Size definition would be rejected.

- Proposed Rule 7.46(f)(5)(H) would provide that Market Pegged Orders and Tracking Orders would be rejected. The Exchange proposes to reject these order types for Pilot Securities in Test Group Three because they are designed in compliance with Rule 611 to be non-displayed orders that price match protected quotations, which would be prohibited under the Trade-at Prohibition.

As described in Rule 7.31P(d)(4), a Tracking Order is an order that is not displayed, does not route, and will trade only with an order that is eligible to trade. The working price of a Tracking Order is the same-side PBBO. As further described in Rule 7.31P(d)(4)(A), a Tracking Order does not trade on arrival and is triggered to trade by a contra-side order that has (i) exhausted all other interest eligible to trade at the Exchange, (ii) has a remaining quantity equal to or less than the size of the resting Trading Order, and (iii) would otherwise route to an Away Market. As such, the Tracking Order is designed in compliance with Rule 611 to be resting non-displayed interest, priced at the PBBO, and that would be triggered to trade only by an order that would otherwise route and in so doing, price-matches Away Market protected quotations.

Similarly, as described in Rule 7.31P(h)(1), once resting on the NYSE Arca Book, a Market Pegged Order is a non-displayed order with a working price pegged to the contra-side PBBO. As such, the Market Pegged Order is designed to be in compliance with Rule 611 to price match protected quotations. As discussed above, unlike Rule 611(b) of Regulation NMS, the Trade-At Prohibition applicable for Pilot Securities in Test Group Three prevents a trading center that was not quoting from price-matching protected quotations. Because both

Tracking Orders and Market Pegged Orders are designed as non-displayed resting orders that price-match protected quotations, which would not be permitted in Test Group Three, these order types are inconsistent with the Plan. Therefore, the Exchange proposes not to make these order types available in Test Group Three. As proposed, Tracking Orders or Market Pegged Orders entered in Test Group Three Pilot Securities would be rejected. The Exchange believes that rejecting such orders in Pilot Securities for Test Group Three would promote transparency in the Exchange's rule book that the Tracking Order and Market Pegged Order functionality would not be available under the Trade-at Prohibition.

#### Proposed Amendments to Other Exchange Rules

The Exchange also proposes amendments to Rule 7.11P, which governs the Limit Up/Limit Down ("LULD") price controls pursuant to the NMS Plan to Address Extraordinary Market Volatility ("LULD Plan"),<sup>29</sup> Rule 7.31P(a)(2)(B) governing Limit Order Price Protection, and Rule 7.35P(a)(8) governing the definition of Indicative Match Price. These proposed rule changes are designed to facilitate compliance with the Plan and would be applicable across all securities that trade at the Exchange, regardless of the applicable MPV.

In particular, the Exchange proposes to add a new subsection (9) to Rule 7.11P(a) that would specify that, after the Exchange opens or reopens an Exchange-listed security but before receiving Price Bands from the SIP under the LULD Plan, the Exchange will calculate Price Bands based on the first Reference Price provided to the SIP and, if such Price Bands are not in the MPV for the security, round such Price Bands to the nearest price at the applicable MPV. The Exchange would apply this standard rounding calculation regardless of the MPV of the

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<sup>29</sup> See Securities Exchange Act Release No. 67091 (May 31, 2012), 77 FR 33498 (June 6, 2012) (File No. 4-631).

security. As described above, pursuant to proposed Rule 7.46(f)(2)(A), references to MPV in Exchange rules instead mean the quoting MPV specified in Rules 7.46(c), (d), and (e).

The Exchange also proposes to amend Rule 7.31P(a)(2)(B), which describes the circumstance under which a Limit Order would be rejected, to specify that Limit Order Price Protection for both buy and sell orders that are not in the MPV for the security, as defined in Rule 7.6, would be rounded down to the nearest price at the applicable MPV. The Exchange further proposes to amend Rule 7.35P regarding Indicative Match Price. Under Rule 7.35P(a)(8), Indicative Match Price means the best price at which the maximum volume of shares, including non-displayed quantity of Reserve Orders, is tradable in the applicable auction, subject to the Auction Collars. The Exchange proposes to specify, as proposed in Rule 7.35P(a)(8)(F), that unless the Indicative Match Price is based on the midpoint of an Auction NBBO, if the Indicative Match Price is not in the MPV for the security, it would be rounded to the nearest price at the applicable MPV. In both such rounding scenarios, for Tick Pilot Securities, pursuant to proposed Rule 7.46(f)(2)(A), references to MPV in these rules would instead mean the quoting MPV specified in Rules 7.46(c), (d), and (e).

#### Proposed Non-Substantive Amendments to Rule 7.46

Finally, the Exchange proposes to make non-substantive, technical amendments to Rule 7.46. First, the Exchange proposes to amend Rule 7.46(a)(1)(D)(ii) to add the word “displayed” between the words “full” and “size” so that the full clause would provide “are routed to execute against the full displayed size of any protected bid.” This proposed amendment makes the rule text parallel with the existing rule text that provides “or the full displayed size of any protected offer.” Second, the Exchange proposes to amend Rule 7.46(e)(4)(C)(xv) to correct a

typographical error and change the word “bond” to “bona” when using the phrase “bona fide error.”

### Implementation Date

If the Commission approves the proposed rule changes, the proposed rule changes will be effective upon Commission approval and shall become operative upon the commencement of the Pilot Period.

### 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>30</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>31</sup> in particular, in that it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in 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. The Plan requires the Exchange to establish, maintain, and enforce written policies and procedures that are reasonably designed to comply with applicable quoting and trading requirements specified in the Plan. The proposed rule change is designed to comply with the Plan, reduce complexity and enhance system resiliency while not adversely affecting the data collected under the Plan. Therefore, the Exchange believes that the proposed rule changes are reasonably designed to comply with applicable quoting and trading requirements specified in the Plan and, as discussed further below, other applicable regulations.

The Exchange believes that the proposed changes to order behavior for Pilot Securities in Test Group Three would remove impediments to and perfect the mechanism of a free and open

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<sup>30</sup> 15 U.S.C. 78f(b).

<sup>31</sup> 15 U.S.C. 78f(b)(5).

market and a national market system because they are designed, and necessary, to modify order behavior to comply with the Trade-at Prohibition by eliminating the ability for orders with a non-displayed working price to price match protected quotations. As the Commission noted in the Tick Plan Approval Order, the Plan is reasonably designed to provide measurable data that should facilitate the ability of the Commission, the public, and market participants to review and analyze the effect of tick size on the trading, liquidity, and market quality of securities of smaller capitalization companies.<sup>32</sup> The Plan thus provides for a mechanism to provide a data-driven approach to evaluate whether certain changes to market structure for Pilot Securities would be consistent with the Commission’s mission to protect investors, maintain fair and orderly and efficient markets, and facilitate capital formation.<sup>33</sup> By having three test groups, the data that will be collected will demonstrate how behavior will change based on the differing requirements of the test groups. Because there are different requirements for the three Test Groups, a logical consequence is that order behavior will change depending on the requirements of each Test Group, which is the purpose of having a pilot with three test groups.

With respect to Pilot Securities in Test Group Three, the Commission recognized the particular complexity of implementing and complying with the Trade-at Prohibition, including that trading centers would need to “monitor protected quotations on other trading centers and prevent an execution that would match the price of any such quotation unless the trading center itself was displaying a protected quotation” and that “compliance with the Trade-at Prohibition would require systems changes by trading centers.”<sup>34</sup> Trading centers that are not registered exchanges will be able to implement compliance with the Trade-at Prohibition by modifying the

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<sup>32</sup> See Tick Plan Approval Order, supra note 6, at 27529.

<sup>33</sup> Id.

<sup>34</sup> Id. at 27530.

behavior of order types that currently price match protected quotations and without public notice and without filing any rule changes with the Commission. Such modified behavior would be applicable, and indeed required, only for Pilot Securities in Test Group Three. Applying the modified order behavior for compliance with the Trade-at Prohibition to Pilot Securities in other Test Groups would moot the differences between the Test Groups, which would thwart the ability to assess any meaningful differences in order behavior for the three Test Groups.

As a trading center, the Exchange must also modify behavior of order types to comply with the Trade-at Prohibition. However, as a registered exchange, the Exchange has rules that are filed with the Commission that describe in detail order behavior, including current order behavior that is designed in compliance with Rules 610(d) and 611 of Regulation NMS. These existing rules provide for non-displayed order types to price match protected quotations even if not displaying a quote at that price. Unlike a trading center that is not a registered exchange, the Exchange is required to file a proposed rule change to describe how it would modify order behavior in compliance with the Plan.<sup>35</sup> For the Exchange to implement compliance with the Plan, and specifically the requirements of the Trade-at Prohibition, the Exchange assessed its order type behavior and identified those changes that would be necessary to prevent an execution on a non-displayed order that would match the price of protected quotation unless that Away Market is displaying a protected quotation.

More specifically, the Exchange believes that the proposed changes regarding ISOs, MPL Orders, Market Pegged Orders, Tracking Orders, RPI Orders, priority of resting orders, Reserve Orders, Limit Non-Displayed Orders and Orders with instructions not to route are consistent with

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<sup>35</sup> Section 19(b)(1) of the Act requires that each self-regulatory organization shall file with the Commission, in accordance with Rule 19b-4 thereunder, copies of any proposed rule or any proposed change in, addition to, or deletion from the rules of such self-regulatory organization. 15 U.S.C. 78s(b)(1).



the Act because they are intended to modify the Exchange's system to comply with the provisions of the Plan and the different requirements for the three Test Groups and are designed to assist the Exchange in meeting its regulatory obligations pursuant to the Plan. For Pilot Securities in Test Group Three, the Exchange believes that the proposed modifications to order behavior are designed to prevent executions of orders with a non-displayed working price from price matching a protected quotation. These are precisely the type of order behavior changes contemplated by the Plan; complying with the Trade-at Prohibition by definition requires differing order behavior as compared to the other Test Groups or the control group. For example, both Tracking Orders and Market Pegged Orders are designed in compliance with Rule 611, which permits non-displayed orders to price match a protected quotation. If such orders cannot trade at the price of the PBBO, such order types are moot; there is no alternate behavior for such orders. As such, the Exchange proposes to reject those order types in Pilot Securities in Test Group Three. Similarly, the Exchange proposes that order types with a non-displayed working price that is equal to the PBBO would be re-priced to assure that such orders would not price match a protected quotation in violation of the Trade-at Prohibition. The Exchange would not apply these order behavior changes to Pilot Securities in Test Groups One and Two because to do so would subvert the quality of data collected; Test Groups One and Two do not have the Trade-at Prohibition and therefore non-displayed orders in those Test Groups may price match a protected quotation, provided such executions are in the applicable MPV for the security. Because these proposed rule changes are intended to comply with the Plan, the Exchange believes that these proposals are in furtherance of the objectives of the Plan, as identified by the Commission, and are therefore consistent with the Act.

The Exchange further believes that the proposed amendments to Rules 7.11P, 7.31P(a) and 7.35P would remove impediments to and perfect the mechanism of a free and open market and a national market system as they provide transparency regarding (1) how the Exchange would calculate and round Price Bands under the LULD Plan after the Exchange opens or reopens an Exchange-listed security but before receiving Price Bands from the SIP, (2) that Limit Order Price Protection for both buy and sell orders that are not in the MPV for the security will be rounded down to the nearest price at the applicable MPV, and (3) when the Exchange would round down the Indicative Match Price if it is not in the MPV for an applicable security. The Exchange proposes to implement these changes for all securities, not only Pilot Securities under the Plan. As provided for in proposed Rule 7.46(f)(2)(A), any references to MPV in these rules would instead mean the quoting MPV specified in Rule 7.46(c), (d), and (e).

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

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is intended to assist the Exchange in meeting its regulatory obligations pursuant to the Plan, reduce system complexity and enhance resiliency. The Plan requires all trading centers, including over-the-counter markets, to implement changes to comply with the requirements of the Plan and specifically the Trade-at Prohibition. The Exchange fully expects that, in order to comply with the Trade-at Prohibition, trading centers other than registered exchanges will modify the behavior of orders for Pilot Securities in Test Group Three that will not be applied to Pilot Securities in Test Groups One and Two. Unlike such trading centers, as a self-regulatory organization, under Section 19(b)(1) of the Act,<sup>36</sup> the Exchange is required to file

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<sup>36</sup> 15 U.S.C. 78s(b)(1).

proposed rule changes for any modifications to order behavior that it proposes for the Plan. The absence of Commission approval of these proposed rule changes would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act because trading centers that are not registered exchanges would be able to implement changes to comply with the Plan, but the Exchange would not. The Exchange believes that a disapproval of the Exchange's proposed rules would therefore put the Exchange at a competitive disadvantage vis-à-vis the over-the-counter markets because such trading centers would be able to modify the behavior of non-displayed orders in Test Group Three without restriction. The Exchange further notes that the proposed rule change will apply equally to all ETP Holders that trade Pilot Securities.

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

The Exchange respectfully requests accelerated effectiveness of this proposed rule change pursuant to Section 19(b)(2) of the Act.<sup>37</sup> The Exchange believes that there is good cause for the Commission to accelerate effectiveness because the proposed rule changes are designed to specify procedures for the handling, executing, re-pricing and displaying of certain order types and order type instructions applicable to Pilot Securities in Test Groups One, Two, and Three. In determining the scope of these proposed changes to implement the Plan, the Exchange reviewed its order types and identified which orders and instructions would be inconsistent with the Plan and propose to modify the operation of such order types so they will comply with the Plan, or, to the extent inconsistent with the Plan, eliminate them. These

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<sup>37</sup> 15 U.S.C. 78s(b)(2).

proposed changes are consistent with the protection of investors and the public interest because they are designed to comply with the Plan and to allow the Exchange to meet its regulatory obligations under the Plan. Because the Plan will be implemented beginning on October 3, 2016, the Exchange believes there is good cause to accelerate effectiveness so that the Exchange may implement the proposed changes concurrent with the implementation date of the Plan.

Within 45 days of the date of publication of this notice in the Federal Register or 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](mailto:rule-comments@sec.gov). Please include File Number SR-NYSEARCA-2016-123 on the subject line.

##### Paper Comments:

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

All submissions should refer to File Number SR-NYSEARCA-2016-123. 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-NYSEARCA-2016-123, and should be submitted on or before [insert date 14 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>38</sup>

Brent J. Fields  
Secretary

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<sup>38</sup> 17 CFR 200.30-3(a)(12).