

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-85637; File No. SR-NYSE-2018-34)

April 12, 2019

Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1, to Amend NYSE Rule 104

I. Introduction

On July 31, 2018, New York Stock Exchange LLC (“NYSE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend NYSE Rule 104 governing transactions by Designated Market Makers (“DMMs”). The proposed rule change was published for comment in the Federal Register on August 16, 2018.³

On September 24, 2018, pursuant to Section 19(b)(2) of the Act,⁴ the Commission extended to November 14, 2018, the time period in which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove, the proposed rule change.⁵ On November 1, 2018, the Commission issued an order instituting proceedings, pursuant to Section 19(b)(2)(B) of the Act,⁶ to determine whether to approve or disapprove the proposed rule

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 83821 (Aug. 10, 2018), 83 FR 40808 (Aug. 16, 2018) (“Notice”).

⁴ 15 U.S.C. 78s(b)(2).

⁵ See Securities Exchange Act Release No. 84276 (Sep. 24, 2018), 83 FR 49143 (Sep. 28, 2018).

⁶ 15 U.S.C. 78s(b)(2)(B).

change.⁷ On February 11, 2019, the Commission extended to April 13, 2019, the period for Commission action on proceedings to determine whether to approve or disapprove the proposed rule change.⁸ The Commission has received one comment letter on the proposal.⁹

On April 9, 2019, the Exchange filed Amendment No. 1 to the proposal, which supersedes the original filing in its entirety. The Commission is publishing this notice to solicit comments on Amendment No. 1 from interested persons, and is approving the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

II. Self-Regulatory Organization's Description of the Proposal, as Modified by Amendment No. 1

In its filing with the Commission, the Exchange 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 V 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 consolidate and restructure subsections (g), (h) and (i) of Rule 104 governing DMM transactions and make a related change to Rule 98(c)(5) (Operation of a DMM Unit). This Amendment No. 1 supersedes the original filing its entirety.¹⁰

⁷ See Securities Exchange Act Release No. 84515 (Nov. 1, 2018), 83 FR 55763 (Nov. 7, 2018) (“Order Instituting Proceedings”).

⁸ See Securities Exchange Act Release No. 85096 (Feb. 11, 2019), 84 FR 4553 (Feb. 15, 2019).

⁹ See Letter from Stephen John Berger, Managing Director, Government and Regulatory Policy, Citadel Securities, to Assistant Secretary, Commission (Nov. 28, 2018) (“Citadel Letter”).

Background

Rule 104 sets forth the obligations of Exchange DMMs. Under Rule 104(a), DMMs registered in one or more securities traded on the Exchange are required to engage in a course of dealings for their own account to assist in the maintenance of a fair and orderly market insofar as reasonably practicable. Rule 104(a) also enumerates the specific responsibilities and duties of a DMM, including: (1) maintenance of a continuous two-sided quote, which mandates that each DMM maintain a bid or an offer at the National Best Bid (“NBB”) and National Best Offer (“NBO,” together the “NBBO”) for a certain percentage of the trading day,¹¹ and (2) the facilitation of, among other things, openings, re-openings, and the close of trading for the DMM’s assigned securities, all of which may include supplying liquidity as needed.¹² Rule 104(f) imposes an affirmative obligation on DMMs to maintain, insofar as reasonably practicable, a fair and orderly market on the Exchange in assigned securities, including maintaining price continuity with reasonable depth and trading for the DMM’s own account

¹⁰ In this Amendment No. 1, the Exchange proposes to amend the original filing by modifying proposed Rule 104(g)(1)(B) relating to Aggressing Transactions prior to the close. In the original filing, the Exchange proposed that Aggressing Transactions in the last ten seconds of trading would be prohibited if they would result in a new consolidated high or low price of the day unless such transaction would bring the price of that security into parity with an underlying or related security or asset. As amended, the Exchange proposes that Aggressing Transactions in the last ten minutes of trading would be prohibited if they would result in a new Exchange high or low price of the day, with three exceptions for matching another market’s better bid or offer, bringing the price of that security into parity with an underlying or related security or asset, or liquidating or decreasing the DMM unit’s position. This Amendment No. 1 also proposes to amend Rule 98(c)(5).

¹¹ See Rule 104(a)(1).

¹² See Rule 104(a)(2)-(3). Rule 104(e) further provides that DMM units must provide contra-side liquidity as needed for the execution of odd-lot quantities eligible to be executed as part of the opening, reopening, and closing transactions but that remain unpaired after the DMM has paired all other eligible round lot sized interest.

when lack of price continuity, lack of depth, or disparity between supply and demand exists or is reasonably to be anticipated.

Rule 104(g) provides that transactions on the Exchange by a DMM for the DMM's account must be effected in a reasonable and orderly manner in relation to the condition of the general market and the market in the particular stock. More particularly, Rule 104(g) describes certain transactions that are permitted to render the DMM's position adequate to the market's needs, including Neutral and Non-Conditional Transactions, and certain DMM transactions that are prohibited.

Rule 104(g)(i)(A)(I) defines Neutral Transactions as a purchase or sale by which a DMM liquidates or decreases a position. Neutral Transactions may be made without restriction as to price. However, the DMM's obligation to maintain a fair and orderly market may require re-entry on the opposite side of the market trend after effecting one or more Neutral Transactions. Such re-entry transactions should be in accordance with the immediate and anticipated needs of the market.

Rule 104(g)(i)(A)(II) defines Non-Conditional Transactions as a DMM's bid or purchase and offer or sale that establishes or increases a position, other than a transaction that reaches across the market to trade with the Exchange BBO. Non-Conditional Transactions may be made without restriction as to price in order to (i) match another market's better bid or offer price; (ii) bring the price of a security into parity with an underlying or related security or asset; (iii) add size to an independently established bid or offer on the Exchange; (iv) purchase at the published bid price on the Exchange; (v) sell at the published offer price on the Exchange; (vi) purchase or sell at a price between the Exchange BBO; and (vii) purchase below the published bid or sell above the published offer on the Exchange. As with Neutral Transactions, the DMM's obligation

to maintain a fair and orderly market may also require re-entry on the opposite side of the market trend after effecting one or more Non-Conditional Transactions. Such re-entry transactions should be commensurate with the size of the Non-Conditional Transactions and the immediate and anticipated needs of the market.

Rule 104(g)(i)(A)(III) provides that, except as otherwise permitted by Rule 104, during the last ten minutes prior to the close of trading, a DMM with a long or short position in a security is prohibited from making a purchase or sale in such security that results in a new high or low price, respectively, on the Exchange for the day at the time of the DMM's transaction ("Prohibited Transactions").¹³

Finally, Rule 104(h) addresses DMM transactions in securities that establish or increase the DMM's position. Rule 104(h)(i) defines a Conditional Transaction as a DMM transaction in a security that establishes or increases a position and reaches across the market to trade as the contra-side to the Exchange published bid or offer.¹⁴

Rule 104(h)(ii) permits "Conditional Transactions" without restriction as to price if they are followed by appropriate re-entry on the opposite side of the market commensurate with the size of the DMM's transaction. Thus, if a DMM establishes or increases a long position by buying from the Exchange best offer, or establishes or increases a short position by selling to the Exchange best bid, such transaction would be followed by the DMM quoting on the opposite side of the last transaction in order to dampen the impact of that transaction on the market.

¹³ Rule 104(g)(i)(A)(III) contains two exceptions to Prohibited Transactions: (1) matching another market's better bid or offer price, and (2) bringing the price of a security into parity with an underlying or related security or asset.

¹⁴ A DMM reaches across the market when the DMM buys from the NYSE offer or sells to the NYSE bid.

The re-entry obligations for Conditional Transactions are set forth in Rule 104(h)(iii). Under Rule 104(h)(iii)(A), DMMs must re-enter within certain Exchange issued guidelines, called price participation points (“PPP”), that identify the price at or before which a DMM is expected to re-enter the market after effecting a Conditional Transaction. PPPs are only minimum guidelines and compliance with them does not guarantee that a DMM is meeting its obligations.

Notwithstanding that a security may not have reached the PPP, the DMM may be required to re-enter the market immediately after a Conditional Transaction based on the price and/or volume of the DMM's trading in reference to the market in the security at the time of such trading. In such situations DMMs may or may not rely on the fact and circumstance that there may have been one or more independent trades following the DMM's trading to justify a failure to re-enter the market. As set forth in Rule 104(h)(iii)(C)(I) and (II), immediate re-entry is required after the following Conditional Transactions:

- a purchase that (1) reaches across the market to trade with an Exchange published offer that is above the last differently priced trade on the Exchange and above the last differently priced published offer on the Exchange, (2) is 10,000 shares or more or has a market value of \$200,000 or more, and (3) exceeds 50% of the published offer size; and
- a sale that (1) reaches across the market to trade with an Exchange published bid that is below the last differently priced trade on the Exchange and below the last differently priced published bid on the Exchange, (2) is 10,000 shares or more or

has a market value of \$200,000 or more, and (3) exceeds 50% of the published bid size.¹⁵

Rule 104(h)(iv) permits certain other Conditional Transactions without restriction as to price. Specifically, under subsection (h)(iv)(A), a DMM's purchase from the Exchange published offer that is priced above the last differently-priced trade on the Exchange or above the last differently-priced published offer on the Exchange. Similarly, under subsection (h)(iv)(B), a DMM's sale to the Exchange published bid that is priced below the last differently-priced trade on the Exchange or below the last differently-priced published bid on the Exchange.

Rule 104(i) provides that re-entry obligations following such Conditional Transactions would be the same as the re-entry obligations for Non-Conditional Transactions pursuant to Rule 104(g).

Finally, paragraph (c)(5) of Rule 98 provides that the member organization operating a DMM unit must provide the Exchange with real-time net position information in DMM securities by the DMM unit and any independent trading unit of which it is part at such times and in the manner prescribed by the Exchange.

Proposed Rule Change

The Exchange proposes to consolidate and restructure current Rules 104(g), (h) and (i), which would be deleted and incorporated as modified into a new subsection (g) titled "Transactions by DMMs."

As discussed below, proposed Rule 104(g) would revise the requirements for DMM transactions based on the type of trading by the DMM, rather than by reference to the DMM's

¹⁵ For purposes of subsections (h)(iii)(C)(I) and (h)(iii)(C)(II), a Sweep is viewed as a transaction with the published bid or offer.

position. Rule 98(c)(5) would be amended to require DMMs to provide net position information to the Exchange daily. The Exchange also proposes certain technical and conforming changes.¹⁶

As restructured, proposed Rule 104 would replace the four current types of DMM transactions based on the DMM's position (Neutral, Non-conditional, Conditional and Prohibited) with a single, enhanced DMM transaction called an "Aggressing Transaction" that would retain existing re-entry requirements. During the ten minutes before the scheduled close of trading, Aggressing Transactions that would result in a new high (low) price for a security on the Exchange for the day at the time of the DMM's transaction would be prohibited with three exceptions discussed below.

Proposed Rule 104(g)(1)

Proposed Rule 104(g)(1) would be based on current Rule 104(g)(i). Like current Rule 104(g)(i), proposed Rule 104(g)(1) would specify that transactions on the Exchange by a DMM unit for the DMM unit's account are to be effected in a reasonable and orderly manner in relation to the condition of the general market and the market in the particular stock. Proposed Rule 104(g)(1) would eliminate the definitions of Neutral and Non-Conditional Transactions¹⁷ and retain Conditional Transactions, which would be enhanced and renamed "Aggressing Transactions."

¹⁶ The Exchange proposes the following technical and conforming changes: (1) romanettes (i) through (vi) in Rule 104(b) and (i) through (iv) in Rule 104(f) would be replaced with numbers 1 through 6 and 1 through 4, respectively; (2) current subsection (j) would become new subsection (h); and (3) current subsection (k) would become new subsection (i).

¹⁷ As discussed below, the re-entry obligations for Neutral and Non-Conditional Transactions would be retained and incorporated into proposed subsection (g)(2).

Aggressing Transactions

In proposed Rule 104(g)(1)(A), the Exchange would define an Aggressing Transaction as a DMM unit transaction that:

- (i) is a purchase (sale) that reaches across the market to trade as the contra-side to the Exchange published offer (bid); and
- (ii) is priced above (below) the last differently-priced trade on the Exchange and above (below) the last differently-priced published offer (bid) on the Exchange.

The proposed definition of Aggressing Transaction would be the same as the current definition of Conditional Transaction in Rule 104(h)(i) and (ii), except that Aggressing Transaction would not be defined by reference to whether the transaction increases or decreases the DMM's position. Accordingly, a DMM unit Aggressing Transaction would be any trade where the DMM both reaches across the market and aggressively moves the price of the security.

Prohibited Transactions

The Exchange proposes to retain certain of the existing prohibitions on specified DMM transactions during the final ten minutes of the trading day and the current exceptions to Prohibited Transactions, which are described in current Rule 104(g)(i)(A)(III). With this proposed rule change, the Exchange proposes a substantive difference for determining whether a DMM transaction should be prohibited in the last ten minutes of trading. Rather than the current rule, which looks at the DMM's position (long or short) and then determines whether the trade should be prohibited based on whether it results in a new Exchange high or low, as proposed, a DMM transaction in the last ten minutes of trading would be prohibited if it is an Aggressing Transaction, i.e., reaches across the market, and, as a result, creates a new Exchange high or low.

The Exchange also proposes exceptions to this prohibition, which are based on exceptions to prohibited transactions in the current rule.

To effect this change, proposed Rule 104(g)(1)(B) would define “Prohibited Transactions” as Aggressing Transactions during the last ten minutes prior to the scheduled close of trading that would result in a new high (low) price for a security on the Exchange for the day at the time of the DMM’s transaction. The proposed three exceptions to this prohibition would be if the trade:

- matches another market’s better bid or offer price;
- brings the price of that security into parity with an underlying or related security or asset; or
- liquidates or decreases the position of the DMM unit.

The first two exceptions are in current Rule 104(g)(i)(A)(III) and the Exchange proposes to retain these exceptions in the proposed rule.¹⁸ The third exception is based in part on the position-based review of whether a transaction would be prohibited under current rules. Current Rule 104(g)(i)(A)(III)(1) prohibits a DMM with a long position in a security from making a purchase in that security during the last ten minutes that results in a new high price; the rule does not prohibit a DMM with a long position from selling or decreasing their position in the security. Likewise, current Rule 104(g)(i)(A)(III)(2) prohibits a DMM with a short position in a security from making a sale in that security during the last ten minutes prior to the close of trading that results in a new low price, but the rule does not prohibit a DMM with a short position from purchasing or liquidating their position in that security. Because looking at the DMM’s position

¹⁸ See Rule 104(g)(i)(A)(III) (referencing Rules 104(g)(i)(A)(II)(2)(i) through (g)(i)(A)(II)(2)(ii)).

would be an exception rather than the basis for the prohibition, the Exchange proposes to restate the rule as an exception that permits a DMM to liquidate or decrease a position of the DMM unit, rather than focus on what is prohibited when the DMM is long or short. This proposed rule text is also based on Rule 104(g)(i)(A)(I), which has no restrictions as to price for “Neutral Transactions,” i.e., transactions when the DMM liquidates or decreases a position.

With this proposed difference for Prohibited Transactions, in the last ten minutes of trading, DMMs would be able to trade at prices lower than the published offer, or higher than the published bid, even if such trade would result in a new Exchange high or low for the day. The Exchange believes that this proposed change would support DMMs in meeting their affirmative obligations while at the same time continuing to prevent DMMs from aggressively taking liquidity and moving prices on the Exchange by trading with the published bid or offer in the final ten minutes before the closing auction¹⁹ For example, if the Exchange best bid and offer were \$10.01 x \$10.05, the DMM has a long position, and the DMM posts a bid at \$10.04 to try and tighten that spread, under the current rules, if that \$10.04 bid were to trade with non-displayed sell liquidity at that price and that trade resulted in a new high price on the Exchange for the day, that trade would be prohibited. Under the proposed change to Prohibited Transactions, this trade would no longer be prohibited because the DMM is not reaching across the market.

¹⁹ See Rule 104(g)(i)(A)(III).

Finally, the Exchange notes that the proposal is consistent with, and in no way diminishes or relieves the DMM of, the other obligations regarding the quality of the markets in securities to which DMMs are assigned under Rule 104.²⁰

Proposed Rule 104(g)(2)

Proposed subsection (g)(2) would set forth the re-entry obligations for DMM transactions, which would be based on the current rule's re-entry obligations. Specifically, proposed Rule 104(g)(2) would provide that a DMM unit's obligation to maintain a fair and orderly market may require re-entry on the opposite side of the market after effecting one or more transactions. The proposed rule would provide that such re-entry should be commensurate with the size of the transaction(s) and the immediate and anticipated needs of the market, which are the same re-entry requirements specified in current Rules 104(g)(i)(A)(I)(3) and 104(g)(i)(A)(II)(3) for Neutral and Non-Conditional Transactions, respectively, as well as the types of Conditional Transactions referenced in current Rules 104(h)(iv) and 104(i).²¹

²⁰ In general, as noted above, transactions on the Exchange by a DMM for the DMM's account must be effected in a reasonable and orderly manner in relation to the condition of the general market and the market in the particular stock, and DMMs must refrain from causing or exacerbating excessive price movements. DMMs have affirmative obligations under Rule 104(a) to engage in a course of dealings for their own account to assist in the maintenance of a fair and orderly market insofar as reasonably practicable. Specifically, Rule 104(f)(ii) sets forth the DMM's obligation to act as reasonably necessary to ensure appropriate depth and maintain reasonable price variations between transactions (also known as price continuity) and prevent unexpected variations in trading. Further, under Rule 123D(a), openings and reopenings must be fair and orderly, reflecting the DMM's professional assessment of market conditions at the time, and appropriate consideration of the balance of supply and demand as reflected by orders represented in the market. The Exchange supplies DMMs with suggested Depth Guidelines for each security in which a DMM is registered, and DMMs are expected to quote and trade with reference to the Depth Guidelines. See Rule 104(f)(iii).

²¹ Current Rule 104(h)(iv) provides that two types of Conditional Transactions may be made without restriction as to price: (1) a DMM's purchase from the Exchange published offer that is priced above the last differently-priced trade on the Exchange or above the

Accordingly, these re-entry obligations would be applicable to DMM transactions other than Aggressing Transactions.

Proposed Rule 104(g)(2)(A) and (B) would specify the re-entry obligations for Aggressing Transactions. Following an Aggressing Transaction, proposed Rule 104(g)(2)(A) would require the DMM unit to re-enter the opposite side of the market at or before the applicable PPP for that security commensurate with the size of the Aggressing Transaction. The re-entry requirement for Aggressing Transactions set forth in proposed Rule 104(g)(2)(A) is based on the current re-entry requirements for certain Conditional Transactions set forth in current Rule 104(h)(iii).

Under proposed Rule 104(g)(2)(B), if the Aggressing Transaction (i) is 10,000 shares or more or has a market value of \$200,000 or more, and (ii) exceeds 50% of the published offer (bid) size, immediate re-entry on the opposite side of the market at or before the applicable PPP for the security commensurate with the size of the Aggressing Transaction would be required. The re-entry requirement for block-sized Aggressing Transactions set forth in proposed Rule 104(g)(2)(B) is based the current re-entry requirements for block-sized Conditional Transactions under Rule 104(h)(iii)(C). The Exchange proposes a clarifying amendment in proposed Rule 104(g)(2)(B), as compared to current Rule 104(h)(iii)(C), to provide that such re-entry must be at or before the applicable PPP for that security. The Exchange believes that this proposed change will provide greater detail in the rule regarding the price at which the re-entry would be required.

last differently-priced published offer on the Exchange ((h)(iv)(A)); and (2) a DMM's sale to the Exchange published bid that is priced below the last differently-priced trade on the Exchange or below the last differently-priced published bid on the Exchange ((h)(iv)(B)). Current Rule 104(i) provides that the re-entry obligations following transactions defined in Rule 104(h)(iv)(A) and (h)(iv)(B) are the same as for Non-Conditional Transactions pursuant to Rule 104(g) (i)(A)(3).

Proposed Rule 104(g)(3)

Finally, proposed Rule 104(g)(3)(A) would provide that the Exchange would periodically issue PPP Guidelines that identify the price at or before which a DMM unit is expected to re-enter the market following an Aggressing Transaction. PPPs are only minimum guidelines and compliance with them does not guarantee that a DMM unit is meeting its obligations. This portion of the proposed Rule is based on Rule 104(h)(iii)(A) without any differences.

Proposed Rule 104(g)(3)(B) would provide that, notwithstanding that a security may not have reached the PPP, the DMM unit may be required to re-enter the market immediately after an Aggressing Transaction based on the price and/or volume of the DMM unit's trading in reference to the market in the security at the time of such trading. In such situations, DMM units may or may not rely on the fact and circumstance that there may have been one or more independent trades following the DMM unit's trading to justify a failure to re-enter the market. Subsection (B) of the proposed rule is based on current Rule 104(h)(iii)(B).

Proposed Amendment to Rule 98(c)(5)

As noted above, except for an exception to Prohibited Transactions, the Exchange proposes to eliminate reliance on the DMM's position to determine DMM trading requirements under proposed Rule 104(g). The Exchange proposes a related change to Rule 98(c)(5) to require DMMs to provide the Exchange with net position information daily. The Exchange proposes a further clarifying change to require DMM to provide net position information "for" such time "periods," rather than "at" such times, prescribed by the Exchange. The Exchange does not believe that DMM net position information would need to be provided in real time in order for the Exchange to effectively monitor for compliance with the proposed exception to Rule

104(g)(1)(B).²² Rather, the Exchange believes it would be able to effectively monitor for compliance with the proposed exception utilizing DMM position information provided on a same-day basis for its automated surveillances. The Exchange would publish regulatory guidance setting forth the requirement that DMMs provide net position on a daily basis but in no event later than trading day plus one (T+1). To implement this change, the Exchange proposes to delete the term “real time” in Rule 98(c)(5) and add the word “daily” after “must” and before “provide.” The Exchange would also replace “for” for “at” before “such times,” delete the “s” in times, and add “periods” immediately following in order to clarify that the Exchange may request DMM net position information for specific time periods on a daily basis.

Rule Implementation

Subject to approval of this proposed rule change, the Exchange proposes to implement these changes concurrent with the transition of Exchange-listed securities to the Pillar trading system, which is currently anticipated to begin in the third quarter of 2019.²³

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,²⁴ in general, and furthers the objectives of Section 6(b)(5) of the Act,²⁵ in particular,

²² The Exchange currently provides DMMs with a technology interface that supports the submission of DMM real-time position information. In extremely limited circumstances, the Exchange relies on that position information to assist the DMMs in marking certain manual orders as sell short or sell long. When the Exchange transitions NYSE-listed securities to its Pillar trading system, it will no longer support this technology interface; nor will it be marking orders on behalf of the DMM.

²³ The Exchange has announced that, subject to rule approvals, the Exchange will begin transitioning Exchange-listed securities to Pillar on July 15, 2019, available at https://www.nyse.com/publicdocs/nyse/markets/nyse/Pillar_Update_NYSE_Tape_A_NG_W_February_2019.pdf. The Exchange will publish by separate Trader Update a complete symbol migration schedule.

²⁴ 15 U.S.C. 78f(b).

because it is designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

In particular, the Exchange believes that revising the requirements for DMM transactions based on the type of DMM trading rather than the DMM's position and introducing a new, enhanced DMM transaction called an "Aggressing Transaction" would remove impediments to and perfect the mechanism of a free and open market and a national market system by simplifying and streamlining the requirements for DMM transactions. The proposal would eliminate four separate types of DMM transactions and introduce a simplified framework whereby all DMM transactions would be subject to general re-entry requirements based on the current re-entry obligations for Neutral, Non-Conditional and Conditional transactions, and specific re-entry requirements for Aggressing Transactions, except for Aggressing Transactions during the final ten minutes of trading that result in a new high (low) price for a security on the Exchange for the day at the time of the DMM's transaction, which would continue to be prohibited unless subject to a specified exception.

The Exchange believes that the proposal would not be inconsistent with the public interest and the protection of investors. As noted, the proposed rule would carry over the requirement that all DMM transactions be effected in a reasonable and orderly manner in relation to the condition of the general market and the market in the particular stock. Further, DMM Aggressing Transactions would continue to require re-entry on the opposite side of the market at or before the applicable PPP for the security as warranted. Aggressing Transactions in the final ten minutes of trading that result in a new high (low) price for a security on the Exchange for the

²⁵ 15 U.S.C. 78f(b)(5).

day at the time of the DMM's transaction would continue to be prohibited. These safeguards would reasonably ensure that DMM transactions continue to bear a reasonable relationship to overall market conditions and that DMMs cannot destabilize, inappropriately influence or manipulate a security going into the close. In addition, the prohibition on Aggressing Transactions that would create a new high or low price on the Exchange would maintain the current bright-line rule that prohibits DMM transactions that aggressively take liquidity during the final ten minutes prior to the close.

The Exchange believes that the proposed substantive difference to Prohibited Transactions in the last ten minutes of trading to permit DMM trades between the Exchange BBO, even if such trades resulted in a new Exchange high or low and regardless of the DMM's position at the time, would promote fair and orderly markets and not be inconsistent with the public interest and the protection of investors because this proposed change would promote the display of liquidity by enabling DMMs to post bids and offers that would tighten the Exchange published bid and offer. The Exchange further believes that retaining the current exceptions for Prohibited Transactions, and permitting Aggressing Transactions that would liquidate or decrease the DMM unit's position during the ten minutes prior to the scheduled close of trading even if they would result in a new Exchange high or low price, would remove impediments to and perfect the mechanism of a free and open market and a national market system because DMMs would be able to quote appropriately in their assigned securities during the period of the prohibition. The Exchange further believes that not restricting Aggressing Transactions in the last ten minutes of trading that result in a new Exchange high or low price for the day if such trade is the result of the DMM liquidating or decreasing a position would remove impediments to and perfect the mechanisms of a free and open market and a national market system because this

exception is based on the current position-based review of whether a transaction would be prohibited, which does not prohibit such transactions, as well the current definition of “Neutral Transactions” which have no restrictions as to price. Further, the Exchange believes that the proposed exception would remove impediments to and perfect the mechanisms of a free and open market and a national market system because a DMM that reaches across the market when liquidating or decreasing a position is generally not doing so to favor a position leading into the close.

Moreover, the numerous obligations currently imposed by Rule 104 would in no way be altered or diminished by the proposal. The Exchange does not believe that the balance of benefits and obligations under Rule 104 would be impacted by this proposed rule change. DMMs would continue to be prohibited from engaging in specified transactions in the final ten minutes prior to the close. Moreover, the proposed rule would carry over the requirement that all DMM transactions be effected in a reasonable and orderly manner in relation to the condition of the general market and the market in the particular stock. These safeguards would reasonably ensure that DMM transactions bear a reasonable relationship to overall market conditions and that DMMs cannot destabilize, inappropriately influence or manipulate a security going into the close. For the same reasons, the proposed prohibition would not alter or disrupt the balance between DMM benefits and obligations of being an Exchange DMM.

Finally, revising the requirements for DMM transactions based on the type of DMM trading rather than the DMM’s position, and amending Rule 98 to require that DMM units provide net position information to the Exchange on a daily basis and for such time periods as prescribed by the Exchange, would remove impediments to and perfect the mechanism of a free and open market and a national market system by simplifying and streamlining the requirements

for DMM transactions. The Exchange further believes that the proposed rule change would promote just and equitable principles of trade and is designed to prevent fraudulent and manipulative acts and practices because DMMs would be required to provide net position information daily to the Exchange and the Exchange would be able to conduct automated surveillances monitoring for compliance with the amended rule for this exception.

For the foregoing reasons, the Exchange believes that the proposal is consistent with the Act.

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 Exchange proposes amendments to the rule governing DMM obligations to simplify and streamline the requirements for DMM transactions. The Exchange believes that the proposal would promote competition by allowing DMMs to quote more aggressively in the final minutes of trading, thereby permitting DMMs to remain competitive with other traders both on the Exchange and on other trading venues, thereby enhancing the ability of DMMs to meet their affirmative obligation under Rule 104. The Exchange further believes that its proposed rules governing DMMs would not impose any burden on competition that is not necessary or appropriate because the proposed rules are designed to foster a fair and orderly marketplace without diminishing the balance of benefits and obligations under Rule 104 or altering or diminishing the numerous obligations currently imposed by Rule 104 on DMMs.

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. Summary of Comments Received

The Commission received one comment letter in support of the proposal as initially filed by the Exchange. The commenter asserts that the proposal materially increases the obligations of DMMs because the proposal would impose re-entry obligations on DMMs throughout the trading day, including following transactions that reduce or liquidate the DMM's position.²⁶ The commenter asserts that the proposed prohibition prior to the close of trading is also strengthened because it would eliminate reference to the DMM's position.²⁷ The commenter also states that it supports the proposed changes to the NYSE rule regarding prohibited transactions because it would modernize the rule to reflect market structure changes, retain a bright line rule negative obligation, and maintain an appropriate balance of benefits and obligations for DMMs.²⁸

IV. Discussion and Commission Findings

After careful review of the proposal, as modified by Amendment No. 1, and the comments received, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.²⁹ In particular, the Commission finds that

²⁶ See Citadel Letter, *supra* note 9, at 1.

²⁷ See *id.* at 2. This commenter also asserted that the prohibition would be strengthened because the rule would reference the consolidated high or low price of a security, rather than the high or low price on the NYSE, but Amendment No. 1, which was filed after this comment letter was submitted, changed the Exchange's proposal so that it no longer changed the reference price. See *id.*

²⁸ See *id.* The proposed rule change with respect to Prohibited Transactions was substantially altered by Amendment No. 1, which was filed after this comment letter was submitted.

²⁹ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act,³⁰ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The Commission also finds that the proposed rule change, as amended, is consistent with Section 6(b)(8) of the Act, which provides that the rules of a national securities exchange must not “impose any burden on competition not necessary or appropriate in furtherance of the purposes of” the Act.³¹

The Exchange has proposed to substantially modify the provisions of NYSE Rule 104(g) and (h) that govern the obligations of DMMs to re-enter the market after certain transactions in assigned securities and that prohibit certain transactions by DMMs in assigned securities near the end of the trading day.³² Currently, whether a DMM’s re-entry obligation is triggered depends, in the first instance, on whether the DMM’s transaction establishes or increases the DMM’s position or instead liquidates or decreases the DMM’s position, and this distinction is reflected in

³⁰ 15 U.S.C. 78f(b)(5).

³¹ 15 U.S.C. 78(f)(8).

³² The Exchange has also proposed to make non-substantive changes to renumber provisions within NYSE Rule 104 and to relocate existing rule text regarding Price Participation Points.

the existing definitions in NYSE Rule 104(g) and (h) of Neutral Transactions, Non-Conditional Transactions, and Conditional Transactions.³³

NYSE now proposes to eliminate these transaction-type definitions and replace them with a single transaction type called an Aggressing Transaction, which would be a DMM unit purchase (sale) that reaches across the market to trade with the Exchange’s published offer (bid) and is priced above (below) both the last differently priced trade on the Exchange and the last differently priced offer (bid) on the Exchange. An Aggressing Transaction would be similar to a Conditional Transaction, which also involves a DMM reaching across the market, and the same re-entry obligations that apply to Conditional Transactions under current NYSE Rule 104 would apply to Aggressing Transactions under amended NYSE Rule 104. But, while Conditional Transactions by definition establish or increase a DMM position, whether a transaction is an Aggressing Transaction would not depend on the DMM’s position.

The Commission believes that triggering DMM re-entry obligations based solely on whether the DMM is aggressively taking liquidity—rather than also considering a DMM’s position at the time of trading—is consistent with the Act, because those re-entry obligations are based on price movement, rather than on the DMM’s position. The Commission further notes that, while the Exchange proposes to eliminate the definitions of Neutral Transactions and Non-Conditional Transactions, which currently have their own re-entry obligations, those re-entry obligations are not substantially different from the DMMs’ general obligations under NYSE Rule 104(a) to “engage in a course of dealings for their own account to assist in the maintenance of a fair and orderly market” and under NYSE Rule 104(f) to maintain “price continuity with

³³ See Section II.A.1, *supra*. Non-Conditional Transactions are distinguished from Conditional Transactions by whether a DMM has reached across the market to trade as the contra-side to an Exchange bid or offer. See *id.*

reasonable depth.” Thus, the Commission does not believe that the Exchange’s proposal to replace the existing categories of Neutral Transactions, Non-Conditional Transactions, and Conditional Transactions with a newly defined Aggressing Transaction would substantially alter the balance of DMM benefits and obligations previously approved by the Commission.³⁴

The Exchange has also proposed to modify the existing definition of Prohibited Transactions. Under its initial proposal, the Exchange sought to make four substantive changes: (1) to limit the applicability of the prohibition to the last 10 seconds of trading before the close, rather than the last 10 minutes; (2) to change the price test in the rule to the high or low consolidated price for the day, rather than the high or low Exchange price for the day; (3) to remove from the Prohibited Transactions rule the focus on a DMM’s position at the time of the transaction; and (4) to apply the Prohibited Transactions rule only to Aggressing Transactions, rather than including certain liquidity-providing trades.³⁵

In its Order Instituting Proceedings, the Commission asked questions about whether the proposed changes were consistent with the Act.³⁶ The Exchange subsequently amended its proposal significantly with respect to Prohibited Transactions. First, the Exchange proposed to retain the existing 10-minute period for Prohibited Transactions. Second, the Exchange proposed to retain the existing price test for Prohibited Transactions. And third, the Exchange proposed to

³⁴ See Securities Exchange Act Release No. 58845 (Oct. 24, 2008), 73 FR 64379, 64388–89 (Oct. 29, 2008) (SR-NYSE-2008-46) (approving NYSE New Market Model pilot and finding that it reflected “an appropriate balance of DMM obligations against the benefits provided to DMMs”). See also Citadel Letter, supra note 9, at 1 (asserting that the proposal materially increases the obligations on DMMs during the trading day because the proposal would impose obligations following transactions that reduce or liquidate the DMM’s position).

³⁵ See Notice, supra note 3.

³⁶ See Order Instituting Proceedings, supra note 7, 83 FR at 55764–65.

add an exception for transactions that would liquidate or decrease the position of the DMM unit, incorporating as a specific exception to the proposed Prohibited Transactions rule a transaction that is, by definition, not covered by the existing rule.³⁷

The Commission believes that the Exchange's amended proposal with respect to Prohibited Transactions is consistent with the Act. While the language and structure of the Prohibited Transactions rule would be different, the only substantive difference between the Prohibited Transactions rule in Amendment No. 1 and the existing rule would be that DMMs could no longer potentially run afoul of the rule by passively providing liquidity through a quote that narrowed the spread in an assigned security. Consistent with its analysis in disapproving an earlier proposal by the Exchange to eliminate the Prohibited Transactions rule, the Commission does not believe that the provision of liquidity by DMMs under such circumstances risks destabilizing the market.³⁸

Finally, the Exchange proposes to amend the obligation under NYSE Rule 98 of a member organization operating a DMM unit to provide the DMM unit's net position data to the Exchange. As amended, NYSE Rule 98 would require that daily data be provided for specified time periods, rather than requiring real-time data. The Commission notes that the DMM unit net position information to be provided will be relevant under amended NYSE Rule 104 only for the last 10 minutes of trading before the close—when the modified Prohibited Transactions rule

³⁷ Consistent with its initial proposal, the Exchange's amended proposal would also define a Prohibited Transaction as a type of Aggressing Transaction, rather than as a separate type of transaction, and it would retain the existing exceptions to the Prohibited Transactions rule for transactions that would match another market's better bid or offer or that would bring the price of an assigned security into parity with an underlying security or asset. See Proposed NYSE Rule 104(g)(1)(B).

³⁸ See Securities Exchange Act Release No. 81150 (July 1, 2017), 82 FR 33534, 33537 (July 20, 2018) (SR-NYSE-2016-71).

would be in effect—and the Exchange represents that it will be able to effectively monitor for compliance with the proposed exception using information provided as required by amended NYSE Rule 98, rather than in real time, as required by current NYSE Rule 98.³⁹ The Commission therefore believes that this change to NYSE Rule 98 is consistent with the Act.

For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with Sections 6(b)(5) and 6(b)(8) of the Act and the rules and regulations thereunder applicable to a national securities exchange.

V. Solicitation of Comments on Amendment No. 1 to the Proposed Rule Change

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether Amendment No. 1 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-NYSE-2018-34 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-NYSE-2018-34. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

³⁹ Under amended NYSE Rule 98, DMMs would have to provide net position information on a same-day basis, but in no event later than trading day plus one.

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. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSE-2018-34 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

VI. Accelerated Approval of Proposed Rule Change, as Modified By Amendment No. 1

The Commission finds good cause to approve the proposed rule change, as modified by Amendment No. 1, prior to the thirtieth day after the date of publication of notice of the filing of Amendment No. 1 in the Federal Register. As discussed above,⁴⁰ Amendment No. 1 substantially modifies the original proposed rule change with respect to the Prohibited Transactions rule, narrowing the proposed rule change significantly so that the only substantive change to the existing rule governing Prohibited Transactions would be to limit the applicability of the rule to instances in which a DMM was aggressively taking liquidity, rather than including certain

⁴⁰ See supra notes 36–38 and accompanying text.

instances in which a DMM was providing liquidity. As noted above, the Commission does not believe that the provision of liquidity by DMMs under these circumstances risks destabilizing the market.⁴¹ Amendment No. 1 made no other substantive changes to the definition of Aggressing Transaction as published in the original Notice.⁴²

Additionally, in Amendment No. 1, the Exchange proposes to amend Rule 98—which requires that member organizations operating a DMM unit provide the Exchange with real-time net position information for the DMM unit—to require that DMM unit net position information be provided to the Exchange on a daily basis and for such time periods as prescribed by the Exchange. The Commission believes this proposal does not raise regulatory concerns, as the Exchange has represented that it would be able to effectively monitor for compliance with the proposed exception to the Prohibited Transactions rule using information provided under an amended Rule 98, rather than in real time, as required under current Rule 98.⁴³

⁴¹ See supra note 38 and accompanying text.

⁴² See Notice, supra note 3.

⁴³ See supra note 39 and accompanying text.

Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,⁴⁴ to approve the proposed rule change, SR-NYSE-2018-34, as modified by Amendment No. 1, on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁵

Eduardo A. Aleman
Deputy Secretary

⁴⁴ 15 U.S.C. 78s(b)(2).

⁴⁵ 17 CFR 200.30-3(a)(12).