

# FINANCIAL INFORMATION FORUM

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## **Via Electronic Delivery**

Mr. Robert W. Errett  
Deputy Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-1090

December 22, 2015

Re: SR-BATS-2015-108; Release No. 34-76552; Notice of Filing of a Proposed Rule Change to Adopt Rule 11.27 Regarding the Quoting and Trading Requirements of the Tick Size Pilot Program

Dear Mr. Errett,

On behalf of Financial Information Forum (“FIF”)<sup>1</sup> members that do not represent an exchange, I am writing to provide comment on the BATS Exchange, Inc. (the “Exchange” or “BATS”) proposed rule filing SR-BATS-2015-108 (“BATS’ filing”), related to the Quoting and Trading requirements of the Tick Size Pilot.<sup>2</sup>

It was our understanding that NYSE’s filing of SR-NYSE-2015-46 on October 22, 2015 (NYSE’s filing”) was meant to provide a template for other Plan Participants to publish rules instituting policies and procedures for quoting and trading; as well as rules requiring their member organizations to establish policies and procedures in compliance with the quoting and trading provisions of the Tick Size Pilot Plan. FIF non-exchange members submitted a comment letter on November 5, 2015, in response to NYSE’s filing.<sup>3</sup>

BATS’ proposed Rule 11.27(a) differs from NYSE’s filing on two important issues highlighted in FIF’s NYSE comment letter. Financial Industry Regulatory Authority, Inc. (“FINRA”) also proposed a rule filing, SR-FINRA-2015-047 (“FINRA’s filing”), which addressed those same issues. While details in BATS’ filing appear to be in alignment with FINRA’s filing, several key concerns for FIF members remain in both filings. They have been discussed in FIF’s response to FINRA’s filing, and several will be reiterated here.<sup>4</sup>

For organizations that are members of both FINRA and BATS (as well as other exchanges), particularly those member firms for whom FINRA is their DEA, it is imperative that Plan Participants’ rule filings related to quoting and trading are completely harmonized under the Regulation NMS Tick Size Pilot Plan.

### *Differences in BATS’ filing and NYSE’s filing*

In proposing Rule 11.27(a), BATS has alleviated two issues that FIF members had with NYSE’s filing; specifically:

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<sup>1</sup> FIF ([www.fif.com](http://www.fif.com)) was formed in 1996 to provide a centralized source of information on the implementation issues that impact financial services and technology firms. Our participants include trading and back office service bureaus, broker-dealers, market data vendors and exchanges. Through topic-oriented working groups, FIF participants focus on critical issues to arrive at productive solutions to meet the requirements of new regulations, technology developments, and other industry changes.

<sup>2</sup> <http://www.sec.gov/rules/sro/nms/2015/34-74892-exa.pdf>

<sup>3</sup> [SR-NYSE-2015-46. FIF Comment Letter regarding SR-NYSE-2015-46.](#)

<sup>4</sup> [SR-FINRA-2015-047. FIF Comment Letter regarding SR-FINRA-2015-048.](#)

1. NYSE stipulated in proposed Rule 67(a)(1) that a retail exemption to the quoting and trading restrictions could only be relied upon when the order is submitted to the *Exchange* under an *exchange program* [emphasis added].

Both BATS and FINRA have removed that limitation, allowing Retail Investor Orders to be exempt from the trading provisions when executed internally by a Trading Center.

2. NYSE's filing states: "Proposed Rule 67(e)(4)(C) would allow member organizations to execute a sell order for a Pilot Security in Test Group Three at the price of a Protected Bid or execute a buy order for a Pilot Security in Test Group Three at the price of a Protected Offer if any of the following circumstances exist: (A) The order is executed by a Trading Center within a member organization that has a displayed quotation for the account of that Trading Center *on a principal basis*, [emphasis added] via either a processor or an SRO Quotation Feed, at a price equal to the traded-at Protected Quotation, that was displayed before the order was received, but only up to the full displayed size of the Trading Center's previously displayed quote."<sup>5</sup>

Both BATS and FINRA indicate that the display exception applies to trades executed by a Trading Center otherwise than on an exchange, where the Trading Center has previously displayed a quotation in either an agency, riskless principal or principal capacity. We now understand that the details of that exception limits a Trading Center displaying a quotation as agent or riskless principal to execute in that capacity, while a Trading Center displaying a quotation as principal may rely on that displayed quotation to execute in any capacity.<sup>6</sup>

## **FIF Members' Concerns**

### *Unanswered Questions*

At this point in time, we are very concerned with the many questions that have not been answered regarding the requirements of the program, and the short timeframe in which the program must be fully implemented. There is a general lack of clarity regarding quoting and trading for a variety of scenarios. Without the specifics of each of the SROs' order handling and execution rules for the Pilot, and without a clear understanding of the functional requirements for each of the Test Groups (particularly the details around the trade-at provisions), it is difficult for non-exchange members to complete their analysis to begin programming.

Systems changes necessary to accommodate the differences in quoting and trading between the Control Group and the three Test Groups are extensive and go to the very core of the rules engines that drive the trading process. Impacts will be significant on all upstream and downstream systems, not the least of which will be changes to end-user (investor) interfaces. Sufficient time for development and rigorous testing is imperative; and, investors will need to be educated. With complete implementation of the Pilot scheduled for October 2016, details of the rules and requirements must be thoroughly understood well in advance to ensure all market participants are adequately prepared for the Pilot.

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<sup>5</sup> Footnote 28 of NYSE's filing explains: "By requiring the displayed quotation to be for the account of "that Trading Center," the Trading Center cannot rely on any quotations it may put up on an agency basis, including a riskless principal basis. A Trading Center that is a broker-dealer also cannot rely on any quotation that is not a displayed quotation for its own account, such as the quotation of another broker-dealer, or customer of such broker-dealer."

<sup>6</sup> Footnote 31 of BATS' filing explains: "The Exchange notes that proposed Rule 11.27(a)(6)(D)(ii) a. is identical to that proposed by FINRA under their proposed Rule 6191(a)(6)(D)(ii) a. See SR-FINRA-2015-047 (filed November 13, 2015). The Exchange also notes that the New York Stock Exchange, Inc. ("NYSE") has recently proposed a rule that states the display exception would only apply to trades done by a Trading Center otherwise than on an exchange where the Trading Center has previously displayed a quotation in a principal capacity only. See Securities Exchange Act Release No. 76229 (October 22, 2015), 80 FR 66065 (October 28, 2015) (SR-NYSE-2015-46) (proposing NYSE Rule 67(e)(4)(C)(i)). The Exchange does not believe proposed NYSE Rule 67(e)(4)(C)(i) is consistent with the SEC's modification of the Trade-At Prohibition to remove the venue limitation."

*We are unaware at this time of the process or forum in which our questions may be answered quickly, in order to expedite development.*

There are many topics that have not been discussed publically by Plan Participants, and have not been answered for the benefit of industry members by the proposed rules or the FAQs published to date.

One simple, but very important example is that we would like the exchanges to come together to agree on how “Good Till Cancel” (“GTC”) orders should be handled at the beginning of the Pilot for Test Group Securities. There will surely be GTC orders that are not priced in five cent increments accepted before the Pilot, that remain open once the Pilot commences. Should the industry assume that all resting orders not priced in five cent increments should be canceled? And, will there be any change in the SRO protocols for adjusting GTC orders for corporate actions, particularly for splits, in light of the new minimum quote variation?

Other questions include:

- 1) May indications of interest priced to execute at the mid-point be entered in increments of less than \$0.05?
- 2) Does BATS plan to create new order types or adjust existing order types to accommodate the Tick Size Pilot? If so, we hope to be notified in sufficient time to make the necessary changes.

Above are just a few examples; however, as the industry begins to program for the quoting and trading rules, many more questions will arise.

#### *Block Size Exemptions*

FIF members are disappointed in the qualifiers to the trade-at exemption for block size orders stipulated in BATS', NYSE's and FINRA's proposed rules. These limitations do not exist in either the SEC Order or the approved Plan, which simply defined a “block size order” for purposes of the Tick Size Pilot to be an order “(1) of at least 5,000 shares or (2) with a market value of at least \$100,000”. Similar to NYSE's and FINRA's filings, BATS indicates that to utilize the block-size trade-at exemption, the order may not be: a) an aggregation of non-block orders; b) broken into orders smaller than Block Size prior to submitting the order to a Trading Center for execution; or c) executed on multiple Trading Centers.

We understand this has been added to ensure the purpose of the trade-at prohibition is not undermined; however, we further understand this has been interpreted to mean that trading centers are prevented from facilitating a block cross that in addition to including block size orders, also includes smaller orders. We ask that these filings be amended to permit aggregation of non-block orders, as long as at least one component of the block in itself would constitute a “block size order” as defined in the approved Plan. We also request clarity around the case of executing a block size order and at the same time being obligated to also fill eligible non-block orders at the same price, as is required under our customer order protection obligations (FINRA Rule 5320).

#### *Other Reg NMS Exceptions*

FIF members had understood that the exceptions to the trade-at provision under the Tick Size Pilot were meant to be closely aligned to the exemptions available for Rule 611 (the trade-through rule) of Regulation NMS.<sup>7</sup> In that spirit, there are certain exemptions that we expected to be included in these filings. While not originally in Rule 611, the Commission issued several orders to add Reg NMS trade-through exemptions and provided guidance in the form of FAQs. FIF members believe that the Tick Size Pilot should allow the following exemptions to the Tick Size Pilot trade-at provision and that prior guidance should apply:

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<sup>7</sup> Ibid. pgs. 94, 106. “the Commission expects that market participants would be able to leverage existing Rule 611 systems for implementing and complying with the Tick Size Pilot”

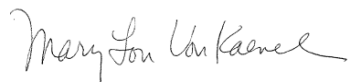
- Order Exempting Certain Error Correction Transactions from Rule 611 of Regulation NMS under the Securities Exchange Act of 1934 <http://www.sec.gov/rules/exorders/2007/34-55884.pdf>
- Order Exempting Certain Print Protection Transactions from Rule 611 <http://www.sec.gov/rules/exorders/2007/34-55883.pdf>
- SEC guidance on Regulation NMS, FAQ 3.04 related to the second leg of a riskless principal transaction (<https://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm>). The open question regarding the trade-at provision in conjunction with this guidance is illustrated in Appendix 1: Scenario 1.
- SEC guidance in connection with Rules 611 and 610 of Regulation NMS, provided in FAQ 7.05, relating Reg SHO and ISOs. <https://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm#sec7>. An open question regarding Reg SHO and the Trade-at requirement is illustrated in Appendix 2: Question 1.

In summary, the quoting and trading models for Tick Size Pilot are complex and will require extensive changes to existing systems. It is important that industry members gain a firm understanding of the policies and procedures that must be followed going forward, so they can begin the analysis and programming necessary to meet required timeframes for implementation.

Complete alignment by Plan Participants, including the Exchanges and the DEAs, is also imperative, as the industry must operate under the same rules in order for firms to navigate the Pilot program while remaining in compliance with existing NMS requirements.

Thank you again for the opportunity to provide comments regarding this important initiative and related rule making. It is important that our questions be addressed in a timely manner for the industry to be ready for the Tick Size Pilot. Please do not hesitate to contact me at (212) 652-4483 to arrange for follow up discussions.

Regards,



Mary Lou Von Kaenel  
 Managing Director  
 Financial Information Forum

cc: The Honorable Mary Jo White, Chair  
 The Honorable Luis A. Aguilar, Commissioner  
 The Honorable Michael S. Piwowar, Commissioner  
 The Honorable Kara M. Stein, Commissioner  
 Stephen Luparello, Director, Division of Trading and Markets  
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