

FINANCIAL INFORMATION FORUM

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Via Electronic Delivery

December 22, 2014

Mr. Brent J. Fields
Secretary
U. S. Securities and Exchange Commission
100 F Street, NE,
Washington, DC 20549-1090

Re: Release No. 73511; File No. 4-657 - Joint Industry Plan; BATS Exchange, Inc., BATS Y-Exchange, Inc., Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, The Nasdaq Stock Market LLC, New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc.; Notice of Filing of Proposed National Market System Plan to Implement a Tick Size Pilot Program On a One-Year Pilot Basis

Dear Mr. Fields,

The Financial Information Forum (FIF)¹ would like to take this opportunity to comment on the joint industry plan to establish an NMS plan to implement a tick size pilot on a one-year pilot basis (“Tick Size Pilot”). The FIF Tick Size Pilot Working Group (“FIF”) has reviewed the Tick Size Pilot from an implementation perspective and believes that while there are opportunities to simplify the Pilot, it will be imperative to allow for sufficient implementation time in order for firms to undertake the analysis, development and testing that will be required. It is important to recognize that the limited duration of the Pilot does not reduce the implementation effort required to make the necessary system modifications. The remainder of this document outlines FIF comments on each of the major functional areas of the Tick Size Pilot including FIF recommendations and considerations with respect to the implementation effort associated with implementing the pilot as a whole.

Identification of Pilot Securities/Selection for Pilot Groups

FIF believes the identification of Pilot securities should be published at least thirty days prior to the initiation of the data collection effort which includes the collection of data six months prior to the inception of the Pilot. To this end, the Measurement Period should be redefined to conclude seven months before the effective date of the Pilot. Alternately, the Pilot could begin with the initiation of the data collection period.

¹ FIF (www.fif.com) was formed in 1996 to provide a centralized source of information on the implementation issues that impact the securities industry across the order lifecycle. 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 and productive solutions to technology developments, regulatory initiatives, and other industry changes.

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In order to reduce operational complexity, changes to the list should be limited to corporate actions. FIF would expect access to Pilot Securities in the format described in Appendix A via a downloadable file from each primary exchange website. Email updates via existing alert mechanisms should be used to alert firms to changes to the list due to corporate actions.

Test Group One – Quoting in Nickels

In order to meet the quoting requirements of the rule that are applicable to all three pilot groups, FIF anticipates changes to order entry, order management and order routing systems. Based on our understanding of the Tick Size Pilot, orders and quotes received by market centers in non-nickel increments will be rejected. Changes would be required to identify pilot securities and prevent order submission at prices which are not integer multiples of nickels. In addition to business analysis, development and testing activities, internal and external training will be required to explain these changes to staff and customers.

At this point it is unclear if SRO members will be required to reject customer orders or if broker dealers can rely on market centers to perform this function. As a practical matter, we believe many broker dealers will choose to modify their order entry systems to prevent the submission of orders outside of nickel increments in order to avoid investor confusion. We request clarification as to whether the Tick Size Pilot will be similar to Rule 612(a) which states: “No national securities exchange, national securities association, alternative trading system, vendor, or broker or dealer shall display, rank, or accept from any person a bid or offer, an order, or an indication of interest in any NMS stock priced in an increment smaller than \$0.01 if that bid or offer, order, or indication of interest is priced equal to or greater than \$1.00 per share.”

Test Group Two – Quoting/Trading in Nickels

In addition to the effort involved in implementing Test Group One, Test Group Two introduces additional implementation questions associated with restrictions on trading in nickels. Specifically, Test Group Two includes an exemption for retail investor orders with \$.005 price improvement. While the term Retail investor order is defined in the Tick Size Pilot, FINRA OATS already defines the term individual customer account type as “an account that does not meet the definition of [FINRA Rule 4512\(c\)](#) and is also not a proprietary account.”² FIF recommends incorporating the FINRA definition of individual as part of the definition of retail investor order. Clarification of this definition is important especially since it is possible for retail order flow originating from natural persons to subsequently be routed to a marketplace via an algorithm.

Currently, the Tick Size Pilot is silent with respect to the applicability of Test Group Two exemptions to opening/closing prints. FIF believes that nickel increments would apply to opening/closing prints. FIF respectfully requests that opening/closing prints be specifically addressed in the final Tick Size Pilot Plan.

Additionally, FIF recommends an additional exemption to Test Group Two to allow the offsetting "riskless" leg of a riskless principal transaction to print outside of nickel increments when it is associated with multiple first legs. This would be necessary to allow a riskless trade that is executed at the weighted average of two or more street-side trades each street-side trade executed at prices permissible under the Pilot.

² See [OATS Technical Specification](#), p. 202

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Test Group Three – Quoting/Trading in Nickels Plus Trade-At

Please note that concerns identified with Test Group One and Test Group Two above apply to Test Group Three as well. The following concerns are focused specifically on the inclusion of the trade-at requirements unique to Test Group Three.

Test Group Three – Implementation Complexity

FIF believes that implementing the trade-at requirements of Test Group Three are significantly more complex than the implementation of the other groups due to its impact on smart order routing technology (SORT), matching engine logic and surveillance systems. The benefits of including Test Group Three should be evaluated against the cost, complexity and additional implementation time that will be required to implement trade-at. Additionally, FIF requests clarification on quotes that would be subject to trade-at protection. It is our understanding that the Commission Order focused on the NBBO whereas the Tick Size Pilot Plan focuses on all protected quotes. In either case, it is our understanding that the trade-at provision will not include depth of book protection.

Test Group Three Exemptions

FIF agrees with the intent of the Plan to mirror Regulation NMS (“Reg NMS”) exemptions. To that end, FIF recommends the inclusion of exemptions to mirror the Reg NMS Error Correction and Print Protection exemptions. Consistent with the Regulation NMS FAQs, it should also be made clear that the second leg of a riskless principal trade will not be considered for trade-at purposes.

Additionally, we request clarification of the block exemption to confirm our understanding that the block exemption would apply if a block order is crossed against an aggregation of non-block size orders.

While we believe it is implicit that mid-point executions are exempt from trade-at provisions, FIF requests that an exemption for midpoint executions be explicitly included as one of the trade-at exemptions.

Test Group Three – Impact on Market Infrastructure

One consequence of the trade-at provisions of Test Group Three may be an increased number of participants reporting to the ADF in order to benefit from being a protected venue. The impact of additional quote traffic and the need to establish connectivity to new ADF participants should be considered in the costs associated with implementation.

Data Collection – Appendix B: Data Collected by Participants and Trading Centers

FIF suggests that the Commission consider the following in determining the data collection requirements associated with the Tick Size Pilot:

- Minimize the implementation costs to reporters of data under the data collection provisions by limiting data collection effort to only those required data elements needed to determine if the Tick Size Pilot increases liquidity in Pilot securities.
- Focus data collection on those data elements only available to data reporters as opposed to data available from the SIP, proprietary data feeds or existing Rule 605 reports. This allows for centralization of data analysis related to comparisons with market data. Rather than each data reporter comparing their executions to a market data source, the SEC can analyze both quote and trade data from the SIP or from MIDAS.

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- Focus analysis on “child” rather than “parent” orders. Child orders are defined as orders that are routed to another market center or that are placed on a market center’s order book. Using child orders reduces ambiguity in terms of determining if an order is marketable or non-marketable. Additionally, the focus on child orders without respect to Rule 605 exemptions would provide the entirety of the executed order flow of market centers.
- Avoid information leakage by maintaining the confidentiality of data reported. The purpose of the Pilot is to determine if further Commission action with respect to the market structure of small cap securities is required; as such, only the Commission should need access to this data. FIF does not believe it will be possible to anonymize the data in such a way as to make it impossible to reverse engineer. Both FINRA ATS transparency data and Rule 605 data could be used to reverse engineer Tick Size Pilot data and compromise data reporter confidentiality.

Appendix B I – Market Quality Statistics

Based on the principles above, FIF recommends focusing data requirements associated with Appendix B I as follows:

Daily statistics categorized by security, order type, and order size including the following columns of information:

- a. For regular hours orders which are market orders (10), marketable limit orders (11), inside-the-quote resting limit orders (12), at-the-quote resting limit orders (13), near-the-quote resting limit orders (within .10 from the NBBO) (14) executed on the trading center:
 - (1) Exchange code or trading center identifier;
 - (2) Ticker Symbol;
 - (3) Order Type, as defined in the Plan or in I.a of the Appendix;
 - (4) Order size with the following modified categories from Rule 605 reports:
 - a. Less than 100 shares;
 - b. 100 to 499 shares;
 - c. 500 to 1999 shares;
 - d. 2000 to 4999 shares;
 - e. 5000 to 9999 shares; and
 - f. 10000 or more shares;
 - (5) The cumulative number of orders;
 - (6) The cumulative number of shares of orders;
 - (7) The cumulative number of shares of orders canceled;
 - (8) The cumulative number of shares of orders executed on the receiving trading center;
 - (9) The cumulative number of shares of orders executed at any other trading center;
 - (10) The share weighted average time to execution for shares executed at the receiving market center;
 - (11) The share weighted average time to execution for shares executed at any other trading center;
 - (12) The share weighted average time to cancellation for shares canceled;
 - (13) Percentage Hidden – the received share-weighted average percentage of shares not displayable as of order receipt;
 - (14) Percentage ISO – the received share-weighted average percentage of shares labelled as ISO as of order receipt;
 - (15) Percentage Retail Liquidity Providing Orders – the received share-weighted average percentage of shares labelled as Retail Liquidity Providing Orders as of order receipt;

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- (16) Percentage Midpoint Passive Liquidity Orders – the received share-weighted average percentage of shares labelled as Midpoint Passive Liquidity Orders as of order receipt;

Appendix B II – Market and Marketable Limit Order Data

FIF has also reviewed Appendix B II data and believes that the data collection effort associated with non-booked market and marketable limit orders should be as follows:

The following columns of information with respect to Market Orders and non-booked portions of Marketable Limit Orders:

- a. Exchange code or trading center identifier;
- b. Ticker Symbol;
- c. Date;
- d. Time of order receipt;
- e. Order Type;
- f. Order Size in Shares;
- g. Order side – “B”, “S” (including sell short exempt), “SS”;
- h. Order price (if marketable limit);
- i. ISO flag (Y/N);
- j. Retail Investor Order flag (Y/N);
- k. Routable flag (Y/N);
- l. IOC (Y/N);
- m. Average execution price – share-weighted average that includes only executions on the receiving market;
- n. Average execution time – share-weighted average period that includes only executions on the receiving market;
- o. Executed shares – the number of shares in the order that are executed;
- p. Canceled shares – the number of shares in the order that are canceled;
- q. Routed shares – the number of shares in the order that are routed to another exchange or market;
- r. Routed average execution price – share-weighted average that includes only shares routed away from the receiving market;
- s. Average routed execution time – share-weighted average period that includes only executions on the routed markets; and

Data elements eliminated from the proposed Tick Pilot, e.g., NBBO quoted price, NBBO quoted depth, etc. could be sourced directly from SIP data which includes both NBBO price and size information.

Appendix B III and IV – Market Maker Registration and Participation Statistics

Since the data collection associated with Appendix B I and Appendix B II takes a comprehensive order perspective, FIF does not believe the collection of data from a sub-set of market centers that are registered market makers is warranted. FIF recommends eliminating the data collection requirements associated with market maker registration and market maker participation statistics.

Data Collection – Appendix C: Data Collected by Market Makers

FIF recommends the elimination of Appendix C from the Tick Size Pilot. FIF believes that the data collection recommendation outlined above achieves the Commission’s goal of understanding the impact on liquidity associated with the Pilot securities in a more cost effective manner. The implementation

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involved to provide market maker profitability would be significant. Not all market making entities calculate P&L on a LIFO basis. Additionally, the definition of market maker profitability in the Tick Size Pilot includes accounting for access fees and rebates which may not be captured in the same systems. Rebates and fees are predicated on overall volume of trades and orders, and not determined until after month end. The fees and rebates are not provided on a trade by trade basis at time of execution. Thus, firms would be required to dedicate resources and develop systems to recalculate trading P&L for the pilot stocks.

Assessment

FIF is concerned that development undertaken for the Pilot will be throw away work if the Pilot ends before recommendations are made. If the Tick Size Pilot ends and code associated with the pilot is taken out of production, additional implementation effort will be required (especially testing) to re-instate elements of the Pilot. In addition to an assessment six months after the pilot ends, the Commission may want to consider a preliminary assessment before ending the Pilot to determine if continuation of the Pilot is warranted.

Cost/Benefit Analysis

FIF would like to note that the costs associated with implementing the initiative may impact firms' willingness to trade Pilot securities. As part of the implementation analysis associated with the final Tick Size Pilot each firm will have to weigh the implementation costs associated with the pilot against the benefit of trading the Pilot securities outside of the Control Group.

FIF recommends that the SEC perform a cost benefit analysis of the Tick Size Pilot in a manner similar to other market structure changes. As part of the cost benefit associated with the data collection effort, FIF encourages the Commission to also consider the possibility of leveraging OATS data to fulfill the Tick Size Pilot's data collection needs. While we understand that effort would be required to extract and analyze OATS data, it may be less costly to make changes to OATS as opposed to requiring each market center to collect and submit data.

Implementation Timing and Phasing

Similar to the successful industry implementation of Limit Up-Limit Down, FIF recommends a phased approach to implementation that includes test symbols in production as well as the release of a limited number of securities into the Pilot as part of a phased rollout. Without a full understanding of the final requirements it is difficult to provide a recommendation on implementation timing. For comparison purposes, it is worth noting that Phase 1 of the Limit Up-Limit Down Pilot took 10 months from the time of the Plan approval to the initial roll-out of production securities but did not include a data collection requirement for SRO members or an order reject requirement. In light of these differences, FIF recommends a minimum of 12 months for the implementation of the Tick Size Pilot if the data collection provisions of the rule are simplified. If they are not simplified, then FIF recommends a minimum 20 months for implementation with sufficient time to implement data collection mechanisms prior to the start of data submission.

Regards,



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Manisha Kimmel
Managing Director
Financial Information Forum

cc: The Honorable Mary Jo White, Chair
The Honorable Luis A. Aguilar, Commissioner
The Honorable Daniel J. Gallagher, Commissioner
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner

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