Bats
a CBOE company

August 2, 2017

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F. Street N.E.
Washington, D.C. 20549-1090

RE: Securities Exchange Act Release No. 80683 (May 16, 2017), 82 FR 23320 (May 22, 2017) (SR-BatsBZX-2017-34)

Dear Mr. Fields:

Bats BZX Exchange, Inc. ("Bats" or the "Exchange") appreciates the opportunity to respond to comments submitted on the above-referenced proposed rule change in which the Exchange proposes to adopt Bats Market Close, a closing match process for non-BZX Listed Securities[1] under new Exchange Rule 11.28 (the "Proposal"). As described more fully in the Proposal, all buy and sell Market-On-Close ("MOC") orders[2] designated for participation in Bats Market Close would be matched at the official closing price for such security published by the primary listing market. A number of comment letters both in support of and against the Proposal have been submitted to the Securities and Exchange Commission (the "SEC" or "Commission") on the Proposal.[3] The Exchange submits this letter in response to those comments.

As an initial matter, the Exchange represents that Bats Market Close is consistent with Section 6(b) of the Securities Exchange Act of 1934 (the "Act"),[4] in general, and furthers the objectives of Section 6(b)(5) of the Act,[5] in particular, because it would execute MOC orders at the official closing price without disrupting the price discovery process of the primary listing

[1] A BZX Listed Security is a security listed on the Exchange pursuant to Chapter 14 of the Exchange's Rules and includes both corporate listed securities and Exchange Traded Products ("ETPs").

[2] The term "Market-On-Close" or "MOC" means a BZX market order that is designated for execution only in the Closing Auction. *See* Exchange Rule 11.23(a)(15).

[3] *See e.g.*, letters to Mr. Brent J. Fields, Secretary, Commission from John Ramsey, Chief Market Policy Officer, IEX Group, Inc., dated June 23, 2017 ("IEX Letter"); Theodore R. Lazo, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association ("SIFMA"), dated June 13, 2017 ("SIFMA Letter"); Venu Palaparthi, SVP, Compliance, Regulatory and Government Affairs, Virtu Financial, dated June 12, 2017 ("Virtu Letter"); Ray Ross, Chief Technology Officer, Clearpool Group, dated June 12, 2017 ("Clearpool Letter"); Donald K Ross, Jr., Executive Chairman, PDQ Enterprises, LLC, dated June 6, 2017 ("PDQ Letter"); James J. Angel, Ph.D., CFA, Associate Professor of Finance, Georgetown University, dated July 30, 2017 ("Angel Letter"); Alexander J. Matturri, Jr., Chief Executive Officer, S&P Dow Jones Indices, dated July 18, 2017 ("S&P Letter"); Elizabeth K. King, General Counsel and Corporate Secretary, New York Stock Exchange, Inc., dated June 13, 2017 ("NYSE Letter"); and Edward S. Knight, Executive Vice President and General Counsel, Nasdaq, Inc., dated June 12, 2017 ("Nasdaq Letter").

[4] 15 U.S.C. 78f.

[5] 15 U.S.C. 78f(b)(5).

markets' respective closing processes. Therefore, it promotes just and equitable principles of trade and competition among national securities exchanges. Bats Market Close will also remove impediments to and perfect the mechanism of a free and open market and a national market system by providing a mechanism for market participants to execute their orders at the official closing price should a system disruption occur on the primary listing market that prevents them from entering orders. The Proposal is also designed to enhance order execution opportunities at the close by providing market participants with an alternative pool of liquidity within which they may receive an execution at the official closing price. Certain commenters seek to distract from the above standard set forth in the Act by raising issues that are not germane to the Proposal. The Exchange submits this letter in response to the issues raised in both the NYSE Letter and Nasdaq Letter as well as similar issues raised by other commenters and to reassert its strong belief that Bats Market Close is consistent with the Act and will serve to benefit all market participants.

The Exchange proposed Bats Market Close as a competitive response to requests from market participants, including agency broker-dealers, bulge-bracket, buy-side, and retail firms, for an alternative to the primary listing markets' closing auction that also provides an execution at the security's official closing price. The Proposal is designed to introduce a meaningful alternative to a single area of the market – the closing auction. It is not designed to adversely impact the trading environment for issuers and their securities. In fact, the Exchange specifically designed the Proposal so that it does not impact the very important price discovery function performed by the primary listing markets' closing auction.

Comment letters, including the NYSE Letter and Nasdaq Letter generally attack the Proposal on four points by arguing it would: (i) impair the price discovery process performed by the NYSE and Nasdaq closing auction processes; (ii) fragment the market at the close; (iii) place an inappropriate burden on competition; and (iv) increase operational and regulatory risk. For the reasons discussed below, the Exchange disagrees with these issues raised by the NYSE Letter and Nasdaq Letter. Bats' response to commenters can be summarized by the following points:

1. The Proposal was carefully designed to avoid disrupting the price discovery process;

2. Despite Nasdaq's inaccurate statement, the SEC and other international regulators have granted prior approval for competing market closing mechanisms to the American Stock Exchange, the NYSE's affiliate, NYSE Arca, Nasdaq, Nasdaq's affiliate Chi-X Canada, Chi-X Australia, and Bats Europe;

3. The Proposal will not introduce market fragmentation at the close as such fragmentation exists today;

4. The Proposal will enhance and not burden competition; and

5. The Proposal will not increase operational and regulatory risk, nor would it present new opportunities to manipulate the closing price. The NYSE's argument that the Proposal creates risk of closing price manipulation is disingenuous given the regular price disruption caused by the NYSE's d-Quote which creates final seconds "imbalance flipping".

The Proposal Will Not Impact the Price Discovery Process

Several commenters raised concerns about whether the Proposal will adversely impact the price discovery process performed by the primary listing markets. The Proposal would not impede the ability of other national securities exchanges to discover their own price for a security. By matching only MOC orders, and not Limit-On-Close ("LOC") orders, and executing those matched MOC orders that naturally pair off with each other and effectively cancel each other out, the Exchange believes the Proposal would avoid any impact on price discovery. In addition, the Bats Market Close mechanism would occur well in advance of primary market cutoff times so any orders not matched on Bats will have plenty of time to reach the primary listing markets. Several commenters who support the Proposal also agreed with Bats that Bats Market Close would not harm price discovery.[6]

The NYSE and Nasdaq, in particular, argue that the Proposal would harm price discovery by potentially pulling market orders from their closing auctions. The Exchange questions the validity of the NYSE's and Nasdaq's concern since both Nasdaq and NYSE Arca, an affiliate of the NYSE, currently conduct closing auctions in securities listed elsewhere on a daily basis. The NYSE and Nasdaq would currently argue that these auctions act as a back-up to primary listing markets and must run every day to ensure that they work properly. This is a newly developed argument, and is akin to turning every light on in your house when you get home each night to ensure the electricity is working. Performing a back-up auction is not what Nasdaq's intent was when it proposed expanding its closing auction process to NYSE listed securities in 2007.[7] Nor did the NYSE express concern at the time that the Nasdaq's proposal would impact the price discovery process performed by their closing auction.

NYSE and Nasdaq now raise the fear of Bats Market Close harming price discovery with no evidence to support that notion. Both NYSE and ARCA operate competing, price-forming auctions, positioned to siphon order flow, including price-setting limit orders. In addition to fragmenting the market, these non-primary listing market auctions can produce bad auction prices on the non-primary market itself. Our research found that competing NYSE Arca and

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6 *See* Angel Letter, IEX Letter, SIFMA Letter, Virtu Letter, and Clearpool Letter. Virtu is a registered Designated Market Maker on the NYSE.

7 *See* Securities Exchange Act Release No. 55721 (May 7, 2007), 72 FR 27344 (May 15, 2007) (SR-Nasdaq-2007-047) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Establish an Opening and Closing Cross for Securities Listed on the NYSE, Amex, and Regional Exchanges).

Nasdaq closing auctions usually print a different closing price than that of the primary listing market.[8] 86% of the competing closing auctions conducted by Nasdaq for NYSE-listed securities in June 2017 resulted in closing prices different from the official closing price published by the NYSE. Similarly, 84% of competing closing auctions conducted by NYSE Arca for Nasdaq-listed securities in the same month resulted in closing prices different from the official closing price published by Nasdaq. Both Nasdaq and NYSE seem to be comfortable with creating dueling closing auctions themselves but they are unwilling to allow for a non-disruptive closing process when it creates competitive pressures on their revenues.

NYSE and its Designated Market Makers ("DMMs") have encouraged several corporate issuers to write form comment letters expressing concern about market fragmentation, seemingly unaware of the divergent closing prices calculated by the competing closing auctions of NYSE Arca and Nasdaq that are conducted under the auspices of resiliency. In contrast, the Bats Proposal does not seek to fundamentally alter the primary listing markets' closing auction functionality or impact their calculation of the official closing price.

Matched MOC orders are recipients of price formation, but do not contribute to the price formation process. While the Proposal may reduce the number of market orders pooled together at the primary listing market, the Exchange removes any perceived adverse impact on the primary listing markets' close by publishing the number of matched market order shares by security in advance of the primary market's cutoff time. There is no logic to support the notion that all MOC orders must be matched in a single place. Matched MOC orders simply have no impact on price discovery. The Proposal and its order entry cutoff time would leave plenty of time for any imbalance of MOC orders not matched via Bats Market Close to reach the primary market to be included in their closing auction process. Further, the complaint that market participants would need to look to another pool of liquidity to understand total matched order size is not valid. The Exchange will disseminate the matched MOC order volume not only via its own Bats Auction Feed, but would also disseminate this information via the applicable securities information processor, if permissible. Modern software can easily and simply add these two sums together. Further, the Exchange recognizes the value of aggregated limit orders to price formation, reflected by its offering of functionality that routes limit orders to the primary listing market[9] to participate in their opening, reopening, or closing auctions.

The NYSE and Nasdaq also argue that the Proposal may pull all MOC orders away from the primary listing market closing auction, altering the calculation of the official closing price. First, both Nasdaq and NYSE permit their members to collect and retain MOC orders and match them internally. In fact, some members actively market these MOC order matching solutions and neither NYSE nor Nasdaq prohibit their members from withholding MOC orders from their

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8 *See* Table 2 in Appendix A attached hereto. Both NYSE Arca and Nasdaq's competing closing auctions are price forming. Table 2 in Appendix A shows that the closing prices that these competing auctions effect are usually different from the official closing price determined by the primary listing markets' closing auction.

9 *See* Exchange Rule 11.13(b)(3)(m) and (n).

closing auctions. Bats is simply proposing to provide an identical facility to match MOC orders under a similar process that Nasdaq and NYSE members currently are permitted to operate. Secondly, Nasdaq's and NYSE's concern regarding the complete loss of MOC orders is overblown. They should have this concern today because they (i) conduct competing closing auctions that pull both MOC and LOC orders from the primary market's closing auction; and (ii) permit their members to do exactly what we are asking. It is possible that all MOC orders in NYSE and Nasdaq listed securities could be sent to NYSE Arca's competing closing auction. For example, symbol FINQ, a Nasdaq-listed security, had no volume in Nasdaq's own closing auction for the entire month of June 2017, while orders were entered and executed in NYSE Arca's competing closing auction in 14 of June 2017's 22 trading days.[10] NYSE's and Nasdaq's SEC approved competing auctions already create this risk of MOC orders leaving the primary market's closing auction. We find their sincerity about this concern quite lacking given they run this risk every day.

Even in the rare event that all MOCs did reside on Bats, the respective primary market can simply read the total matched shares disseminated by the Exchange at 3:35 p.m. Eastern Time via the Bats Auction Feed, which is provided free of charge. This information could be incorporated in the primary market's closing process.

The NYSE and Nasdaq accuse Bats of simply using its calculation of the official closing price to execute orders without contributing to the price discovery process ("free riding"). Bats believes that on balance the Proposal provides materially better value to the marketplace without disrupting the price-formation auctions in two ways:

1. It does not siphon price-forming limit orders from the primary listing market or further fragment the market; and

2. It provides users with the official closing price, since any other price is undesirable to the user and at the same time potentially harmful to the primary market's price formation process.

As also stated in the Proposal, it is a well-established practice for an exchange to price buy and sell orders based upon reference data, even where the price is based on quote or trade data not originating on that exchange.[11] Both the NYSE and Nasdaq have the ability to use reference

[10] *See* Table 5 in Appendix A attached hereto for an illustration of this real-life edge case.

[11] *See* Exchange Rule 11.9(c)(9) (Mid-Point Peg Order); *see also* Nasdaq Rule 4702(b)(5)(A) (Midpoint Peg Post-Only order); NYSE Arca Equities Rule 7.31(h)(3) (Mid-Point Passive Liquidity Orders); Bats EDGX Exchange, Inc. ("EDGX") Rule 11.8(d) (MidPoint Peg Orders). What these order types have in common is that their execution prices are derived from the top of book prices of all "Protected Quotations", as such term is defined in Rule 600(b)(58) of Regulation NMS under the Exchange Act. In addition, several pegged order types on various exchanges, including EDGX, NYSE Arca, and Nasdaq, are set in some relationship to the NBBO, regardless of which exchange established or currently has liquidity at the NBB or NBO. *See* Exchange Rule 11.9(c)(8); EDGX

prices today to establish their official closing price.[12] Importantly, there is precedent for an exchange to execute orders solely at reference prices while not also displaying priced orders for that security. For example, the NYSE offers an afterhours crossing session which permits the entry and execution after regular trading hours of orders at the NYSE's official closing price.[13] In addition, the ISE Stock Exchange initially executed orders only at the midpoint of the NBBO, and did not display any orders, therefore never contributing to the determination of the NBBO.[14] Therefore, the Exchange continues to believe executing trades at the official closing price disseminated by the primary listing market is consistent with existing behavior and does not present any novel issues not already considered by the Commission when those orders types and practices were established.

<u>The SEC and Other Regulators Have Granted Prior Approval of Competing Closing Auctions</u>

Nasdaq's claim that it "is aware of no regulator in any jurisdiction in the world that has sanctioned the diversion of orders from the primary market close such as Bats proposes here" suggests that Nasdaq may want to do further legal research. First, the SEC has in fact granted approvals to Nasdaq itself, NYSE Arca and the American Stock Exchange to operate competing closing auctions. While Nasdaq may have forgotten receiving their own SEC approval to operate a competing closing cross mechanism, we are sure they must remember when the American Stock Exchange not only received approval from the SEC to launch a competing closing process but Standard and Poor's announced its decision to use the American Stock

Rule 11.6(j) (Pegged instruction); Bats EDGA Exchange, Inc. ("EDGA") Rule 11.6(j) (Pegged instruction); Nasdaq Rule 4703(d) (Pegging); *and* NYSE Arca Rule 7.31(h)(1) and (2) (Primary Pegged Orders and Market Pegged Orders).

12 The Exchange also notes that in the event a primary listing market cannot perform a closing auction due to a systems issue, in some circumstances it may determine their official closing price pursuant to contingency procedures that do not utilize a closing auction process. In such case, the official closing price may be either the: (i) volume-weighted average price ("VWAP") of the consolidated last-sale-eligible prices of the last five minutes of trading during regular trading hours as calculated by the applicable securities information processor; or (ii) the last consolidated last-sale-eligible trade for the security during regular trading hours on that trading day. *See* Exchange Rule 11.23(i); *see also* Securities Exchange Act Release No. 78015 (June 8, 2016), 81 FR 38747 (June 14, 2016) (SR-NYSE-2016-18) and (SR-NYSEMKT-2016-31) ("OCP Approval Order"). *See also* Nasdaq Rule 4754(b)(8); *and* NYSE Arca Rule 1.1(ggP).

13 *See* NYSE Rule 902. One could argue that by permitting the entry of orders after the closing auction has occurred while guaranteeing the official closing price, the NYSE crossing session could possibly siphon orders from the closing auction.

14 *See* Securities Exchange Act Release No. 54399 (September 1, 2006), 71 FR 53728 (September 12, 2006) (SR-ISE-2006-45). *See also* ISE Announces MidPoint Match Launch On September 8, *available at* https://www.globalcustodian.com/Market-Infrastructure/ISE-Announces-MidPoint-Match-Launch-On-September-8/.

Exchange's closing prices for Nasdaq listed stocks in the calculation of its index.[15] Additionally, in 2009 the UK Financial Conduct Authority granted Bats Europe approval to operate a competing closing auction.[16] In 2015, the Ontario Securities Commission ("OSC') approved a proposal by Chi-X Canada ATS (currently owned by Nasdaq) to adopt MOC orders that it would match at the closing price published by the Toronto Stock Exchange ("TSX").[17] Commenters were supportive of the Chi-X Canada proposal and included letters from National Bank Financial, ITG Canada Corp., TD Securities Inc., BMO Capital Markets, RBC Capital Markets and the Canadian Securities Traders Association. In its approval order, the OSC stated that Chi-X Canada's proposal would not "threaten the integrity of the price formation process" and would put pressure on the TSX to competitively price executions during their closing auction process. In addition, the Australian Securities and Investments Commission has permitted Chi-X Australia to adopt a process for matching MOC orders at the closing price published by the Australian Stock Exchange.[18] These are all clear and direct precedents of a regulator approving a proposal that seeks to match MOC orders at the primary market's closing price. Chi-X Canada obviously believes in competition in the closing auction north of the border and now their parent company, Nasdaq, ironically argues against instilling that same competition within its home market in the U.S.

<u>The Proposal Will Not Introduce Market Fragmentation at the Close as Such Fragmentation Exists Today</u>

Commenters, including the NYSE and Nasdaq, expressed concern that the Proposal would fragment trading at the close of regular trading hours. The Proposal would not introduce new fragmentation at the close. The NYSE and Nasdaq ignore the fact that fragmentation at the close exists today through their own competing closing auctions conducted daily on a broad base

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15 *See also* S&P Letter against the Proposal. We find it curious that S&P failed to remember their own support for the American Stock Exchange's competing closing cross mechanism that materially disrupted closing price formation. The Commission approved a proposal by the American Stock Exchange to operate a competing closing method for Nasdaq stocks following Nasdaq's failure to close its market on the Russel Rebalance day in 2002. *See* Securities Exchange Act Release No. 47658 (April 10, 2003), 68 FR 19041 (April 17, 2003) (SR-Amex-2003-18).

16 *See* http://www.bats.com/europe/equities/notices/2647/release_notes/.

17 *See* OSC's Notice of Commission approval of Proposed Changes, dated April 21, 2015, *available at* http://www.osc.gov.on.ca/en/Marketplaces_ats_20150430_nca-pro-changes.htm. *See also* OCS's Notice of Proposed Rule Change and Request for Comment *available at* http://www.osc.gov.on.ca/en/Marketplaces_ats_20150219_rfc-pro-changes.htm.

18 *See* Chi-X Australia process for matching MOC orders at the closing price published by the Australian Stock Exchange, *available at* https://cmsau.chi-x.com/Portals/15/CXA_MOC_2015_brochure_v1web.pdf and Australian Securities and Investments Commission ASIC Market Integrity Rules (Competition in Exchange Markets) 2011 – Rule 1.2.1(1) –Class Rule Waiver *available at* https://www.legislation.gov.au/Details/F2013L02062.

of non-primary listings.[19] In addition, off-exchange venues siphon order flow at the close from the primary listing markets by offering executions at the official closing price.[20] For example, on June 20, 2017, 430,000 shares of FedEx were matched at the official closing price by off-exchange venues, compared to 380,000 shares that were matched at NYSE, FedEx's listing market.[21] Arguing that the Proposal would introduce new market fragmentation is not correct. If, on the other hand, NYSE's and Nasdaq's argument evolves to claim that today's competition is de minimus and does not impact price discovery or fragment the market, then we question why the introduction of Bats Market Close to the market should be any different and thus not allowed. The Commission's approval of a new product must not hinge upon speculation of whether the product would be successful and that such predicted success or failure would negatively impact the market. That was not the standard when Nasdaq's and NYSE Arca's competing auctions were approved by the Commission and it should not be the standard here.[22] The Proposal must simply be consistent with the Act, as this one clearly is. More importantly, the SEC's prior precedent in this area further supports that the Proposal is consistent with the Act.

As mentioned previously, the NYSE's argument that NYSE Arca must run their competing auction on a daily basis to ensure it operates properly in the case of a market impairment is not a rational basis to do so. Use of the market impairment process is rare to non-existent, whereas the auctions are an every-day event. The NYSE should address its concern about market fragmentation by only conducting the NYSE Arca competing auction in the event of an impairment, and cease doing so on a daily basis. The potential for a market impairment event neither justifies nor necessitates their daily operation. Nasdaq and NYSE Arca's daily competing auctions already fragment the market at the close. Those arguing that fragmentation would now only result if the Proposal is approved are making a poor attempt to fend off a much needed price competitive alternative to their current auction processes. In addition, this existing fragmentation could increase today should NYSE Arca's or Nasdaq's competing auctions see an increase in order flow.

The NYSE and Nasdaq's reference to the Commission's recent approval of Amendment 12 to the Limit-Up Limit-Down Plan is also misplaced. Both argue that the Commission endorsed the consolidation of trading on the primary listing market following a Trading Pause. Through submission of Amendment 12, the Commission and Participants sought to prevent executions from occurring outside of the Price Bands. It did not, by any means, force consolidation of orders at the primary listing market. It did, however, grant the primary listing

19 *See* Table 1 in Appendix A attached hereto. NYSE Arca and Nasdaq currently conduct a significant number of competing closing auctions for non-listed securities on a daily basis. For the first six months in 2017, Nasdaq on average conducted more than 2000 competing auctions monthly for NYSE-listed securities while NYSE Arca, an affiliate of NYSE, conducted over 1000 competing closing auctions for NYSE-listed securities.

20 *See* Table 6 in Appendix A attached hereto. Table 6 illustrates that significant volume in shares of FedEx, Proctor & Gamble, and Cardinal Health is being executed at the official closing price at off exchange venues.

21 *Id*.

22 *See supra* note 15.

market the ability to set the re-opening price, just as the Proposal accords the setting of the closing price to the primary listing market. Amendment 12's other purpose of waiting for the primary market to reopen is to avoid outlier executions, i.e., trades outside of Price Bands established by the reopening of the primary listing market. In a similar vein, the Proposal would ensure that it does not fragment the auction process and produce a bad closing price, or an outlier execution in the way that might happen if Amendment 12 did not predicate re-opening bands on the Reference Price established by the primary listing market. Centralizing auction functions has not been brought into question by the Proposal. The Exchange has simply proposed a mechanism that does not affect the centralization of *price-setting* auction orders.

The NYSE and Nasdaq also introduce the concept of time fragmentation suggesting that the Proposal would fragment the market with respect to the time orders are entered. Time fragmentation with regard to closing auctions exists today. In fact, both NYSE Arca's and Nasdaq's competing auctions each have a different order entry cutoff time and disseminate information with regard to the auction at different time intervals. In addition, the NYSE's closing auction process allows for time fragmentation today by permitting the entry, cancellation and modification of d-Quotes up until 3:59:50 p.m., nearly fifteen minutes later than the 3:45 p.m. cutoff time for LOC and MOC orders. Access to enter d-Quote orders is generally not available to retail investors and mainly provided to professional traders. d-Quote order flow is also hidden from the NYSE's imbalance feed up until 3:55 p.m. d-Quotes have an extra level of opaqueness until near the close, and otherwise create anything but a level playing field. Because of d-Quotes' time fragmentation, to use an NYSE concept, the NYSE closing price formation process can be dramatically impacted through imbalance flipping in the final seconds of their closing auction.[23] In fact, a review of the NYSE's closing process reveals that 27% of d-Quotes that flip the sell or buy imbalance on the NYSE's closing auction are entered after 3:59:00.[24] Imbalance flipping in the final seconds of a market close is shockingly frequent on the NYSE and a direct result of their permitted d-Quote time fragmentation. This suggests that the NYSE's concern about "time fragmentation" should be turned towards their own flawed closing auction process given the price formation disruption caused by their d-Quotes. It should be noted that Nasdaq does not offer such a feature and therefore does not experience "time fragmentation" or imbalance flipping in the final seconds of their closing auction. After further studying the NYSE closing auctions as part of this process, Bats calls on the SEC to review the appropriateness of the NYSE's use of the d-Quote and its potential for price manipulation of the NYSE's closing prices.

[23] *See NYSE Probes Market-Maker, Wall Street Journal* (October 5, 2016) which involves a problematic closing price in Versum Material, Inc. (VSM) that was partially caused by a d-Quote order submitted in the final seconds of the NYSE closing auction.

[24] Bats' research is based on the NYSE imbalance messages published for their listed securities between 15:55 to 16:00 ET for September 2016 through March 2017. Bats tracked the number of times an imbalance for a security flipped side from Buy to Sell or vice versa.

The NYSE also claims that the lack of complete order information could cause their DMMs to choose different closing prices for some securities. They cite a hypothetical example where the DMM's knowledge of a large MOC Buy order at the close might well influence the DMM to select a higher closing price. A DMM's use of this information suggests that the NYSE closing auction is not a true auction and can be an immediate detriment to users sending MOC orders of meaningful size to the NYSE. Bats feels this only highlights an additional benefit to allowing BMC to compete with NYSE's closing auction. This is because the Proposal would provide an alternative pool of liquidity and a mechanism for large order senders to avoid the subjective decision making of the DMMs who are free to make closing price decisions to their profit benefit at the client's expense. This would explain why some DMM firms are so vocally opposed to the Bats Market Close proposal.[25] The NYSE closing auctions are one of the most profitable times of day for the DMM. It is not surprising to hear complaints from a DMM about a proposal that would reduce their informational advantages and profit opportunities.

The Proposal will Enhance and not Burden Competition

The Exchange believes the Proposal would increase competition by offering a price-competitive alternative to the primary listing markets' closing auction process. The proposed rule change will promote competition among national securities exchanges in the execution of MOC orders at the official closing price without disrupting the price discovery process performed by the primary listing markets' closing processes.

Both the NYSE and Nasdaq do not disagree that the Proposal would enhance competition amongst exchanges. Instead they seek to contort the issue of competition by advancing concepts that do not apply here. The NYSE cites the Commission's disapproval of Nasdaq's proposed Benchmark Order for the notion that when an exchange offers a service that would compete with a broker-dealer, the Commission must assess whether the Proposal complies with Section 6(b)(8) of the Exchange Act.[26] This is not a novel concept as exchanges must always include a statement in their proposed rule changes that their proposal does not impose an unnecessary burden on competition in compliance with Section 6(b)(8) of the Exchange Act, not just in the context of broker-dealer competition. In any event, the Exchange is not seeking to compete against broker-dealers who already match MOC orders at the official closing price. The Proposal simply states that broker-dealers currently offer the same service with no impact on price discovery of the primary market's closing auction. As made clear in the Proposal, the Exchange is seeking to compete with the primary listing markets on price. Further, the operation of Bats Market Close would be clearly described in the Exchange's rules and the Exchange would be required to submit a proposed rule change pursuant to Section 19(b) of the Act should

[25] *See* letter to Mr. Brent J. Fields, Secretary, Commission from Ari Rubenstein, CEO of GTS Securities, dated June 22, 2017 ("GTS Letter").

[26] *See* Securities Exchange Act Release No. 68629 (January 11, 2013), 78 FR 3928 (January 17, 2013) (SR-Nasdaq-2012-059).

it seek to make any changes.[27] Further, the Proposal is clearly distinguishable from Nasdaq's proposed Benchmark Order and does not implicate the same issue. In addition, the Exchange understands that the Commission disapproved Nasdaq's proposed Benchmark Order not because it imposed an unnecessary burden on competition, but rather because it primarily raised issues under the Market Access Rule, Rule 15c3-5 under the Exchange Act.[28]

In addition, Nasdaq suggests that the Proposal would undermine competition amongst orders. This concern is misplaced. Orders compete with each other for executions within each individual exchange ecosystem based on the parameters the market participant places on their orders. The Exchange believes that paired MOC orders, which are not price-setting and are the beneficiaries of price discovery, does not impact the order interactions that take place on another exchange.

<u>The Proposal Will Not Increase Operational and Regulatory Risk, Nor Would It Present New Opportunities to Manipulate the Closing Price</u>

The Exchange notes that participation in Bats Market Close is voluntary, and its market participants will view the value of participation to be greater than the risks that the NYSE and Nasdaq perceive the Proposal creates. No rule or regulation would require market participants to send orders to the Bats Market Close. In fact, the Proposal is actually quite simple. It is a straightforward crossing process that matches one order type only, MOC orders, at one time (3:35 p.m.) well in advance of the cutoff times of the primary listing markets. Any information that the primary market or a DMM actually needs will have plenty of time to reach them.

The NYSE and Nasdaq suggest a risk arises from the asymmetry of information disseminated pursuant to the Proposal and what they both disseminate (or fail to disseminate) as part of their closing auction processes. They suggest that the difference in information disseminated via the Proposal and the time at which it is disseminated could lead to potential gaming and opportunities to manipulate the official closing price. The Exchange believes the notion that the Proposal would provide increased chances for manipulation is a scare tactic used by those fearing viable competition to sway regulators into disapproving the Proposal. It ignores the supervisory responsibilities and capabilities of exchanges and the expansive cross market surveillance conducted by FINRA today. Following approval of the Proposal, the Exchange, FINRA and others will continue to surveil for potential manipulative activity and seek to punish those that engage in such behavior.

The Proposal would not introduce any specific or new ways to manipulate the closing price. The very nature of trading creates short term asymmetries of information to those who are parties to a trade. The Proposal and the current primary market's closing auctions are no

27 *See e.g.*, Securities Exchange Act Release No. 78181 (June 28, 2016), 81 FR 43297, at 43300 (July 1, 2016) (SR-NYSEArca-2016-44).

28 17 CFR 240.15c3-5.

different. As mentioned above, d-Quotes may be entered, modified or cancelled on the NYSE up until 3:59:50 p.m., nearly fifteen minutes later than the 3:45 p.m. cutoff time for LOC and MOC orders. During that time, brokers and DMMs on the NYSE have more information than others do. d-Quote order flow is also hidden from the NYSE's imbalance feed up until 3:55 p.m. The potential for manipulation exists here today. Ironically, the NYSE wants their DMM and brokers to have this informational advantage but no one else. For the most part, NYSE orders are locked in at 3:45 p.m., while d-Quote users can continue to add, modify, and cancel their orders up to the last minute of regular trading hours.

Concerns were also raised about information leakage where the Exchange proposes to disseminate its total matched volume at 3:35 p.m. The concern is that market participants may decipher the side on which the imbalance exists by seeing what portion of their order has not been matched. This is also fearmongering by the NYSE and Nasdaq. Both the NYSE and Nasdaq disseminate imbalance information leading up to their auctions. The NYSE also provides d-Quotes, which present their own information advantages discussed above. The Exchange believes that the information disseminated via the Proposal would not provide market participants any indication if the return of a particular side of an order is meaningful or just happenstance.

Lastly, Bats Market Close would provide a much needed, seamless, and easy way for the industry to address the single point of failure risk that exists for closing auctions today. While exchanges do have designated backups and redundancy procedures, quite a bit of confusion can arise amongst traders when a market's ability to successfully receive orders and run its closing auction is unclear. When a primary listing market is experiencing systems issues and lacks full operational capability, Bats Market Close can provide an alternative pool of liquidity to which market participants can send MOC orders for execution. For example, the primary listing market may not invoke its back-up procedures where it is experiencing an impairment in a select symbol range, but functioning normally in the remaining symbols. Such a scenario could create uncertainty for market participants on how they are to handle their closing orders for symbols in which the primary listing market is impaired. In such case, market participants may route their MOC orders in the affected symbols to Bats Market Close for execution at the official closing of the primary listing market.[29]

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The Exchange is willing to work with the Commission and others to amend the Proposal to address any remaining concerns. The Exchange is also willing to disseminate more information with regard to Bats Market Close and to include such information not only on its

[29] *See supra* note 12 for a description of how the event a primary listing market may determine its official closing price where it cannot perform a closing auction due to a systems issue. *See also* the proposed operation of Bats Market Close where the primary listing market is impaired *at* Securities Exchange Act Release No. 80683 (May 16, 2017), 82 FR 23320, at 23321, note 17 (May 22, 2017).

Bats Auction Feed (which is provided free of charge), but also disseminate it via the applicable securities information processor, if permissible.

Bats appreciates the opportunity to comment on the above proposed rule change and urges the Commission to approve it in a timely manner. Please feel free to contact Bryan Harkins at [redacted] or me at [redacted] if you have any questions related this matter.

Sincerely,

Joanne Moffic-Silver
Executive Vice President, General
Counsel, and Corporate Secretary

Appendix A

Key Observations:

- Data Source: Bats determined the closing auction volume by date, exchange and symbol by tracking trade messages containing the Sale Condition value of "6" disseminated by the applicable securities information processor.

- NYSE Arca and Nasdaq currently conduct a significant number of competing closing auctions for non-listed securities on a daily basis. For the first six months in 2017, Nasdaq on average conducted more than 2,000 competing auctions monthly for NYSE-listed securities while NYSE Arca, an affiliate of the NYSE, conducted over 1000 competing closing auctions for NYSE-listed securities. Refer to Table 1 below for details.

- Table 2 shows that the closing prices that the NYSE Arca and Nasdaq competing auctions effect usually are different from the official closing prices determined by the primary listing markets' closing auction. In June 2017, 86% of the competing closing auctions conducted by Nasdaq for NYSE-listed securities, and 84% competing auctions conducted by NYSE Arca in Nasdaq-listed securities resulted in closing prices different from the official closing price. A similar observation is true for the competing closing auctions conducted by NYSE Arca in Nasdaq-listed securities.

- Tables 3 and 4 provide symbol specific examples to illustrate the impact when current competing closing auctions result in a closing price different from the official closing price. For example, out of 22 trading days in June 2017, NYSE Arca conducted a competing closing auction for QQQ 16 times. 14 of those 16 auctions resulted in a closing price different from the Nasdaq's official closing price. The average impact per share is $0.03. *See* more examples in Tables 3 and 4.

- Table 5 illustrates where a Nasdaq-listed security, FINQ, had no volume at the primary listing markets' closing auction for the entire month of June 2017, while NYSE Arca's competing closing auction had non-zero volume for 14 of the month's 22 trading days.

- Table 6 provide examples of large off-exchange trades (with size over 10,000 shares) reported to the securities information processors with the same price as the official closing price seconds after the respective listing market reported the official closing prints. In the case of FedEx on July 20, 2017, 430,000 shares are matched off-exchange with the official closing price compared to 380,000 shares matched at NYSE, the listing market.

Table 1: 2017 YTD Competing Closing Auction Statistics

Listing Market	Month	Nasdaq		NYSE		NYSE Arca	
		Closing Volume	# Closing Auctions	Closing Volume	# Closing Auctions	Closing Volume	# Closing Auctions
Nasdaq	Jan-17	1,536,797,357	46,792			1,358,340	486
	Feb-17	1,538,751,096	46,280			1,316,903	404
	Mar-17	2,463,457,093	54,695			1,163,524	1,114
	Apr-17	1,505,753,362	46,258			1,017,001	431
	May-17	1,848,931,047	52,088			1,600,660	437
	Jun-17	3,418,048,329	53,288			1,945,752	528
NYSE	Jan-17	749,953	1,097	4,134,069,602	51,200	1,101,282	943
	Feb-17	328,844	998	3,757,362,563	49,254	878,119	617
	Mar-17	1,275,069	1,729	5,373,649,545	59,278	753,881	2,036
	Apr-17	517,807	4,612	3,782,311,276	49,817	1,523,129	1,126
	May-17	2,192,898	2,784	4,459,192,575	57,707	1,747,845	938
	Jun-17	1,969,366	2,554	6,636,049,969	57,753	262,754	417
NYSE Arca	Jan-17	189,640	134			907,160,515	9,136
	Feb-17	179,508	336			759,518,498	9,280
	Mar-17	361,001	884			1,023,501,189	10,488
	Apr-17	206,998	923			790,005,671	9,152
	May-17	200,741	975			876,243,602	10,925
	Jun-17	341,130	618			911,439,651	11,346

Table 2: June 2017 Competing Closing Auction Statistics – % with Closing Price Different from Official Closing Price

Listing Exchange	Non-Listing Exchange with Competing Closing Auctions	# Competing Closing Auctions Conducted	% Competing Closing Auctions with Closing Price Different from Official Closing Price	# Distinct Symbols with Competing Closing Auctions	Volume from Competing Closing Auction
NYSE	Nasdaq	2554	86%	685	1,969,366
Nasdaq	NYSE ARCA	528	84%	285	1,945,752

Table 3: June 2017 Competing Closing Auction Statistics – Examples of NYSE-Listed Securities

Symbol	Name	Non-Listing Exchange with Competing Closing Auctions	# Competing Closing Auctions Conducted	# Competing Closing Auctions with Closing Price Different from Official Closing Price	Per Share Impact
SWN	Southwestern Energy Company	Nasdaq	6	5	$0.04
BAC	Bank of America Corp	Nasdaq	4	3	$0.05
PANW	Palo Alto Networks Inc.	Nasdaq	3	3	$0.33
BABA	Alibaba Group Holding Ltd	Nasdaq	9	7	$ 0.10
JILL	J. Jill Inc.	Nasdaq	1	1	$0.23
PSTG	Pure Storage Inc.	Nasdaq	1	1	$0.15
GKOS	Glaukos Corp	Nasdaq	2	2	$0.18
F	Ford Motor Company	Nasdaq	2	2	$0.02
EPC	Edgewell Personal Care Co	Nasdaq	1	1	$0.05
CGI	Celadon Group, Inc.	Nasdaq	1	1	$0.10

Table 4: June 2017 Competing Closing Auction Statistics – Examples of Nasdaq-Listed Securities

Symbol	Name	Non-Listing Exchange with Competing Closing Auctions	# Competing Closing Auctions Conducted	# Competing Closing Auctions with Closing Price Different from Official Closing Price	Per Share Impact
TLT	iShares Barclays 20+ Yr Treas.Bond (ETF)	NYSE ARCA	22	16	$0.03
QQQ	PowerShares QQQ Trust, Series 1 (ETF)	NYSE ARCA	16	14	$0.03
AMD	Advanced Micro Devices, Inc.	NYSE ARCA	17	10	$0.01
ACWI	iShares MSCI ACWI Index Fund (ETF)	NYSE ARCA	5	5	$0.03
EA	Electronic Arts Inc.	NYSE ARCA	1	1	$0.05
CSX	CSX Corporation	NYSE ARCA	1	1	$0.04
CA	CA, Inc.	NYSE ARCA	1	1	$0.08
STX	Seagate Technology PLC	NYSE ARCA	1	1	$0.04
HAS	Hasbro, Inc.	NYSE ARCA	2	2	$0.06
AMZN	Amazon.com, Inc.	NYSE ARCA	1	1	$1.99

Table 5: An example of a Nasdaq-listed Security with no primary listing market closing volume but non-zero volume in competing closing auctions.

June 2017 Closing Volume Statistics for FINQ (Purefunds Solactive FinTech ETF), a Nasdaq-Listed Security			
Date	**NYSE Arca Competing Closing Auction Volume**	**NYSE Arca Competing Closing Auction Price**	**Listing Market (Nasdaq) Closing Volume**
6/13/2017	200	$ 27.99	-
6/14/2017	200	$ 28.08	-
6/15/2017	200	$ 28.00	-
6/16/2017	200	$ 28.05	-
6/19/2017	200	$ 28.31	-
6/20/2017	200	$ 28.17	-
6/21/2017	200	$ 28.26	-
6/22/2017	200	$ 28.42	-
6/23/2017	200	$ 28.62	-
6/26/2017	200	$ 28.51	-
6/27/2017	1,800	$ 28.20	-
6/28/2017	200	$ 28.55	-
6/29/2017	200	$ 28.15	-
6/30/2017	200	$ 28.26	-

Table 6: Examples of large off-exchange trades (with size over 10,000 shares) reported to the applicable securities information processor on July 20, 2017 for FDX, PG and CAH following their respective official closing prints.

FedEx					
Date Time	**Participant**	**Symbol**	**Shares**	**Price**	**Vol/Listing Market Close Vol**
07/20/17 16:02:59.339	NYSE	FDX	382,588	211.88	
07/20/17 16:02:59.517	TRF	FDX	215,392	211.88	56%
07/20/17 16:03:01.430	TRF	FDX	70,500	211.88	18%
07/20/17 16:03:01.435	TRF	FDX	145,600	211.88	38%

Procter & Gamble					
Date Time	**Participant**	**Symbol**	**Shares**	**Price**	**Vol/Listing Market Close Vol**
07/20/17 16:00:29.043	NYSE	PG	662,462	88.6	
07/20/17 16:00:29.374	TRF	PG	99,689	88.6	26%

Cardinal Health					
Date Time	**Participant**	**Symbol**	**Shares**	**Price**	**Vol/Listing Market Close Vol**
07/20/17 16:03:37.004	NYSE	CAH	154,053	77.32	
07/20/17 16:03:37.193	TRF	CAH	33,000	77.32	9%
07/20/17 16:03:39.030	TRF	CAH	16,860	77.32	4%