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January 17, 2017

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Re: SEC Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Adopt the CHX Liquidity Taking Access Delay
Release No. 34-79608; File No. SR-CHX-2016-16

Dear Mr. Fields:

The FIA Principal Traders Group (“FIA PTG”)¹ appreciates the opportunity to further comment on the proposal by the Chicago Stock Exchange, Inc. (“CHX” or “the Exchange”) to introduce the Liquidity Taking Access Delay (“LTAD”). Herein we specifically respond to the two questions posed in the SEC Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Adopt the CHX LTAD (“the Order”).

Further to our previous comment letter,² FIA PTG believes the CHX proposal should not be approved because it is not consistent with the Securities Exchange Act of 1934 (the “Exchange Act”) and Regulation NMS (“Reg NMS”). In our view, among other things,

¹ FIA PTG is an association of more than 20 firms that trade their own capital on exchanges in futures, options and equities markets worldwide. FIA PTG members engage in manual, automated and hybrid methods of trading, and they are active in a wide variety of asset classes, including equities, fixed income, foreign exchange and commodities. FIA PTG member firms serve as a critical source of liquidity, allowing those who use the markets, including individual investors, to manage their risks and invest effectively. The presence of competitive professional traders contributing to price discovery and the provision of liquidity is a hallmark of well-functioning markets. FIA PTG advocates for open access to markets, transparency and data-driven policy and has previously made recommendations about a variety of equity market structure issues, including Regulation NMS (See <https://ptg.fia.org/keywords/equity-market-structure>).

² <https://www.sec.gov/comments/sr-chx-2016-16/chx201616-5.pdf>

the proposal would permit unfair discrimination and would impose unnecessary, inappropriate burdens on competition.

In response to the Order, we reiterate and expand on our discrimination and burdens on competition concerns below.

Asymmetric Advantage

As noted in our first comment letter, the LTAD is a one-way speed bump that would apply only to marketable orders, and not to resting orders or cancellations of resting orders. This provides an asymmetric advantage to a specific class of traders. It has the effect of giving automated traders who post quotes extra time to move their quotes out of the way when the market appears to be moving against them. We agree with the interpretation of Automated Quotations Under Reg NMS in which the Commission raised concerns about potential “access delays that were imposed only on certain market participants”.³

Unfair Discrimination

The result of this asymmetric speed bump is unfair discrimination among market participants. Allowing some market participants to have a structural latency advantage over others frustrates the purposes of Rule 611 by impairing fair and efficient access to an exchange’s quotations. CHX has commented that the LTAD would not favor certain market participants “other than minimizing the possibility of stale quotes being executed by latency arbitrageurs.” There are a number of flaws with this argument, however.

First, there are tangible benefits to quoters overlooked by CHX. Specifically, when a liquidity provider submits a displayed order on a Reg NMS venue, that order is given order protection against being traded through. The advantage of order protection cannot be overlooked, and that is why under Reg NMS, quotes receiving these benefits are required to be immediately accessible. Rather than “leveling” the playing field, by eliminating a primary requirement of Reg NMS, the CHX proposal would tilt the field significantly and unfairly towards certain automated market makers.

Second, the CHX application of the definition of “latency arbitrage” is flawed. CHX uses this term whenever a liquidity provider on its venues is unable to cancel an order before it is executed (e.g. the liquidity provider receives a “Too Late To Cancel” (TLTC) message from CHX). CHX asserts that this only occurs when the price taker is engaged in taking resting liquidity at stale prices. This simplistic view of market structure fails to account for the handling of orders by market intermediaries for their clients. Since the implementation of Reg NMS, brokers have invested in smart order routing technology to provide the highest and best quality executions for their clients. To assume that nearly every liquidity taking order that results in a TLTC message to a liquidity provider is the result of latency arbitrage grossly mischaracterizes the nature of today’s marketplace.

³ Securities Exchange Act Release No. 78102 (June 17, 2016) (the “Commission Interpretation”) at 27, note 75 (Citations Omitted).

Third, it is too simplistic to say that the only impact of LTAD will be to protect against latency arbitrageurs executing against “stale quotes.” Our markets are complex and dynamic, and many different constituencies are represented in both liquidity taking and liquidity provision. Among other impacts, the LTAD would frustrate strategies that involve taking prices across multiple venues (or across both futures and equity markets), because it would give extra time to automated market participants quoting on CHX to pull their quotes in the middle of a multi-venue order. Additionally, there will be complex trickle-down impacts on the NBBO including CHX quotes that may not really be accessible.

Not De Minimis

Aside from the issues of discrimination under LTAD, CHX also argues that the LTAD is “so short as to not frustrate fair and efficient access to the Exchange’s quotations.” CHX claims, “350 microseconds is not long enough to permit a liquidity taker to act upon knowledge not already in its possession.” We disagree. From the perspective of automated market participants, such as many of our members, 350 microseconds is plenty of time for a computer to process, interpret and act upon new information.

The CHX argument again relies on a simplistic view of market structure. It ignores the fact that brokers take into account many factors regarding when to submit orders to achieve best execution for a client’s order. Similarly, liquidity providers consider a myriad of factors when determining prices at which to rest orders. Any increased amount of time given to a market participant to pull a quote will surely disadvantage market participants routing orders to CHX.

Permissible Discrimination Should be Exercised Cautiously

Given that the LTAD is not a de minimis delay and does discriminate against many market participants, we believe it should be rejected by the Commission. CHX has argued that LTAD “permissibly discriminates” between resting and marketable orders. Again, we disagree. The impact of this differentiation between order types would clearly favor one class of market participants over others in a way that will harm overall market efficiency and transparency.

Furthermore, we take issue with the two examples provided by CHX justifying this “permissible” discrimination. In the instance of maker-taker fees, CHX has ignored the fact that maker/taker pricing does not involve the mechanics of trading under Reg NMS (e.g., it does not impact how one trades, just the fees/rebates one may be charged/receive for trading). LTAD, on the other hand, would affect the regulatory mechanics of trading. Under Reg NMS, in some circumstances traders would be required to route to quotes on CHX, only to have those quotes canceled at the last moment due to the latency advantage provided to the quoter by the LTAD. In the instance of bulk-quoting interfaces at Nasdaq and BATS, CHX is comparing apples to oranges. The options market is a far different marketplace from the equity marketplace, and the bulk quoting mechanism is not directly relevant to how the equity market trades.

Violation of Firm Quote Rule

Finally, we are concerned that the LTAD would be a violation of the Firm Quote Rule under Rule 602 of Reg NMS since it is designed explicitly to allow market participants to back away from their quotes. CHX's claim that traders quoting on the CHX are never presented with the order contradicts the reality of the trading process and needs to be reviewed by the SEC. Simply put, LTAD provides quoters with the ability to cancel their quotes just when a new order is about to execute a trade. Even the Commission's approval of the IEX platform did not allow orders to be processed out of sequence. Under CHX's proposal, the LTAD would enable certain market participants to back away from quotes if the market appears to have moved against them.

While many of our members might be in a position to benefit from the proposal – because of the discrimination inherent in the LTAD, as well as the additional unwarranted complexity it would add to equity market structure – we respectfully request that the Commission disapprove the CHX proposal.

Need for Holistic Review

As we have stated in our responses to the various latency-introducing proposals – IEX, CHX LTAD and Nasdaq ELO – all three of these iterations highlight the need for a holistic market structure review. Without regulatory action to comprehensively address the complexity engendered by the current market structure, proposals like these will continue to multiply like a self-perpetuating computer virus, further complicating and distorting market incentives. We strongly support action by the Commission to address the fundamental complexity in market structure instead of taking a piecemeal approach to individual exchange proposals.

In 2015, FIA PTG published a brief set of recommendations for simplifying the US equity market structure.⁴ These recommendations included the elimination of the requirement to avoid displaying locked and crossed markets (Rule 610.d) and the elimination of the order protection rule (Rule 611). Both of these rules were originally put in place, in part, to help assure that brokers were achieving best execution for their clients. Today we believe however that best execution can be addressed much more simply by clarifying and modernizing the best execution requirements that brokers already have, rather than by sustaining this extremely complex backstop managed by the trading venues. We believe the elimination of both Rules 610.d and 611 along with the modernization of the best execution requirements will simplify the markets in meaningful ways and provide other important benefits for the investing public.

⁴ See FIA PTG, *Simplifying U.S. Equity Market Structure* (January 28, 2015), at http://ptg.fia.org/sites/default/files/content_attachments/FIA%20PTG%20Position%20-%20Simplifying%20US%20Equity%20Market%20Structure.pdf

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If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Joanna Mallers (jmallers@fia.org).

Respectfully,

FIA Principal Traders Group

A handwritten signature in blue ink that reads "Joanna Mallers". The signature is written in a cursive style and is set against a light yellow rectangular background.

Joanna Mallers
Secretary

cc: Mary Jo White, Chairwoman
Kara M. Stein, Commissioner
Michael S. Piwowar, Commissioner
Stephen Luparello, Director, Division of Trading & Markets