

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-84976; File No. SR- NYSEARCA-2018-77)

December 26, 2018

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Rule 7.44-E to Expand and Modify the Exchange's Retail Liquidity Program

I. Introduction

On October 26, 2018, NYSE Arca, Inc. ("NYSE Arca" or the "Exchange") filed with the Securities and Exchange Commission (the "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to amend Rule 7.44-E to expand the Exchange's Retail Liquidity Program ("RLP") to all securities traded on NYSE Arca and make certain other modifications.

The proposed rule change was published for comment in the Federal Register on November 14, 2018.³ On December 10, 2018, the Commission extended to February 12, 2019, the time period in which to approve, disapprove, or institute proceedings to determine whether to approve or disapprove, the proposed rule change.⁴ The Commission received no comments on the proposed rule change. This order institutes proceedings under Section 19(b)(2)(B) of the Act⁵ to determine whether to approve or disapprove the proposed rule change.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 84547 (November 7, 2018), 83 FR 56890 ("Notice").

⁴ See Securities Exchange Act Release No. 84772, 83 FR 64381 (December 14, 2018).

⁵ 15 U.S.C. 78(s)(b)(2)(B).

II. Summary of the Proposed Rule Change

The Exchange proposes to amend Rule 7.44-E, which sets forth the Exchange's Retail Liquidity Program (the "Program"), to: (i) expand the Program's availability to all securities traded on the Exchange; (ii) remove unused functionality by eliminating the Type 2 - Retail Order and no longer permit Retail Price Improvement Orders ("RPI") to be designated as a Mid-Point Liquidity ("MPL") Order;⁶ and (iii) offer additional functionality to RPI Orders by allowing them to include an optional offset.

The Program is intended to attract retail order flow to the Exchange, and allow such order flow to receive potential price improvement.⁷ The Program is currently limited to trades occurring at prices equal to and greater than \$1.00 a share. The program currently operates on a pilot basis and was set to expire on December 31, 2018, but was recently extended to expire on June 30, 2019.⁸

Under Exchange Rule 7.44-E, a class of market participant called Retail Liquidity Providers ("RLPs")⁹ and non-RLP member organizations are able to provide potential price improvement to retail investor orders in the form of a non-displayed order that is priced better than the best protected bid or offer ("PBBO"), called an RPI. When there is an RPI in a particular security priced at least \$0.001 better than the PBB or PBO, the Exchange disseminates an indicator, known as the Retail Liquidity Identifier ("RLI"), that such interest exists. Retail

⁶ Rule 7.31-E(d)(3).

⁷ See Securities Exchange Act Release No. 71176 (December 23, 2013), 78 FR 79524 (December 30, 2013) (SR-NYSEArca-2013-107) ("RLP Approval Order").

⁸ See Securities Exchange Act Release No. 84773 (December 10, 2018), 83 FR 64419 (December 14, 2018).

⁹ The Program also allows for RLPs to register with the Exchange. However, any firm can enter RPI orders into the system.

Member Organizations (“RMOs”) can submit a Retail Order to the Exchange, which interacts, to the extent possible, with available contra-side RPIs and orders with a working price between the PBBO. The segmentation in the Program allows retail order flow to receive potential price improvement as a result of their order flow being deemed more desirable by liquidity providers.¹⁰

Expansion of Program’s Scope

The Exchange proposes to expand the Program’s availability to all securities traded on the Exchange. As more fully set forth in the Notice, the Exchange proposed that in addition to NYSE Arca-listed securities and UTP Securities, the Program would cover securities listed on the New York Stock Exchange LLC (“NYSE”), which are currently excluded from the Program would be covered by the Program. The Exchange states that this expansion would make the Program more similar to the retail price improvement program offered by Cboe BYX Exchange, Inc. (“BYX”), that is available to all securities trading on BYX.¹¹

Elimination of Type 2 - Retail Orders

Also as more fully set forth in the Notice, the Exchange proposes to amend Rule 7.44-E(k) to remove unused functionality by eliminating the Type 2 - Retail Order.¹² As a result, the Exchange would offer a single category of Retail Orders. The Exchange states that it has not received a Retail Order designated as Type 2 and, therefore, proposes to no longer support this functionality.¹³

¹⁰ RLP Approval Order, 77 FR at 79528.

¹¹ See Notice at supra note 3 at 56891.

¹² See Id.

¹³ See Id.

RPI Orders

In addition, as more fully set forth in the Notice, the Exchange proposes to remove unused functionality by no longer permitting RPI Orders to be designated as MPL Orders, and also proposes to offer additional functionality to RPI Orders by allowing them to include an optional offset.¹⁴

RPIs are non-displayed and only execute against Retail Orders. RPIs are generally entered at a single limit price, rather than being pegged to the PBBO. One exception is that a RPI Order could also be designated as an MPL Order, in which case the order would be pegged to the midpoint of the PBBO and re-priced as the PBBO changes.

Designation as MPL Orders. The Exchange proposes to remove unused functionality that permits RPI Orders to be designated as MPL Orders. Rule 7.44-E(a)(4)(D) currently states that “[a]n RPI must be designated as either a Limit Non-Displayed Order or MPL Order, and an order so designated will interact with incoming Retail Orders only and will not interact with either a Type 2- Retail Order Day or Type 2- Retail Order Market that is resting on the NYSE Arca Book.” The Exchange notes that to date all RPI Orders have been designated as Non-Displayed Limit Orders, not MPL Orders.

As proposed, RPI Orders could no longer be designated as MPL Orders. To effect this change, the Exchange proposes to revise the above-referenced sentence from Rule 7.44-E(a)(4)(D) to provide instead that “[a]n RPI . . . will interact with incoming Retail Orders only.” The remaining text of the current rule is no longer necessary because the reference to Non-Displayed Limit Orders is superfluous as RPI Orders by definition are non-displayed and must

¹⁴ See id. at 56892.

include a limit price.¹⁵ Further, references to Type 2-Retail Orders are unnecessary because they would no longer be offered by the Exchange, as proposed above.

Optional Offset Functionality. The Exchange proposes to allow RPIs to include an optional offset. Rule 7.44-E(a)(4) would be amended to include new paragraph (a)(4)(C)¹⁶ that would provide that an RPI may include an optional offset, which may be specified up to three decimals. The working price of an RPI to buy (sell) with an offset would be the lower (higher) of the PBB (PBO) plus (minus) the offset or the limit price of the RPI. An RPI with an offset would not be eligible to trade if the working price is below \$1.00. If an RPI to buy (sell) with an offset would have a working price that is more than three decimals, the working price would be truncated to three decimals.

RPIs that include an offset would interact with Retail Orders as follows. Assume an RLP enters RPI sell interest with an offset of \$0.001 and a limit price of \$10.10 while the PBO is \$10.11. The RPI could interact with an incoming buy Retail Order at \$10.109. If the PBO changes to \$10.12, the RPI could interact with an incoming buy Retail Order at \$10.119. If, however, the PBO changes again to \$10.10, the RPI could not interact with the Retail Order because the price required to deliver the minimum \$0.001 price improvement (\$10.099) would violate the RLP's limit price of \$10.10.

If an RLP otherwise enters an offset greater than the minimum required price improvement and the offset would produce a price that would violate the RLP's limit price, the offset would be applied only to the extent that it respects the RLP's limit price. By way of illustration, assume RPI buy interest is entered with an offset of \$0.005 and a limit price of

¹⁵ Under Rule 7.44-E(a).

¹⁶ The Exchange proposes to renumber the remaining paragraphs under Rule 7.44-E(a)(4) accordingly.

\$10.112 while the PBB is at \$10.11. The RPI could interact with an incoming sell Retail Order at \$10.112, because it would produce the required price improvement without violating the RLP's limit price, but it could not interact above the \$10.112 limit price.

The Exchange proposes to make a related change to Rule 7.16-E(f)(5)(C) to specify that, like Pegged Orders and MPL Orders, RPIs with an offset would use the National Best Bid ("NBB") instead of the PBB as the reference price when a Short Sale Price Test is triggered pursuant to Rule 201 of Regulation SHO.¹⁷

III. Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act¹⁸ to determine whether the proposal should be approved or disapproved. Institution of proceedings is appropriate at this time in view of the legal and policy issues raised by the proposal. Institution of disapproval proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described in greater detail below, the Commission seeks and encourages interested persons to provide additional comment on the proposal.

Pursuant to Section 19(b)(2)(B) of the Act,¹⁹ the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of the proposed rule change's consistency with Section 6(b)(5) of the Act,²⁰ which requires that the rules of an exchange be designed, among other things, to

¹⁷ 17 CFR 242.201.

¹⁸ 15 U.S.C. 78s(b)(2)(B).

¹⁹ Id.

²⁰ 15 U.S.C. 78f(b)(5).

prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest, and which prohibits the rules of an exchange from being designed to permit unfair discrimination between customers, issuers, brokers, or dealers, and with Section 6(b)(8) of the Act, which requires that the rules of an exchange not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.²¹

The Exchange notes that the Program was intended to create additional price improvement opportunities for retail investors by segmenting retail order flow on the Exchange.²² When the Commission initially approved the Program on a pilot basis, it explained that it would monitor the Program throughout the pilot period for its potential effects on public price discovery and on the broader market structure.²³ The Exchange seeks to modify and expand the Program as the pilot is approaching expiration, prior to providing an analysis of what it considers to be the economic benefits for retail investors and the marketplace flowing from operation of the Program. Under the Commission's Rules of Practice, the "burden to demonstrate that a proposed rule change is consistent with the [Act] and the rules and regulations issued thereunder . . . is on the [SRO] that proposed the rule change."²⁴ The description of a proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an

²¹ 15 U.S.C. 78f(b)(8).

²² See Notice, supra note 3 at 56891.

²³ See RLP Approval Order, supra note 7.

²⁴ Rule 700(b)(3), Commission Rules of Practice, 17 CFR 201.700(b)(3).

affirmative Commission finding,²⁵ and any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Act and the applicable rules and regulations.²⁶ The Commission questions whether the proposal to expand and modify the Program prior to Commission consideration of whether to approve the Program, as it has been operating, on a permanent basis is consistent with the Act, particularly given that the Commission has questioned whether similar programs have achieved their stated goals.²⁷ The Commission believes it is appropriate to institute proceedings to allow for additional consideration and comment on the issues raised herein, any potential response to comments or supplemental information provided by the Exchange, and any additional independent analysis by the Commission. The Commission believes that these issues raise questions as to whether the Exchange has met its burden to demonstrate that the Program, as proposed to be expanded and amended, is consistent with the Act, and specifically, with its requirements that the Program be designed to perfect the mechanism of a free and open market and the national market system, protect investors and the public interest, and not be unfairly discriminatory; or not impose an unnecessary or inappropriate burden on competition.²⁸

²⁵ See id.

²⁶ See id.

²⁷ See Securities Exchange Act Release Nos. 84600 (November 15, 2018), 83 FR 58802 (November 21, 2018), 84472 (October 23, 2018), 83 FR 54411 (October 29, 2018), and 84183 (September 18, 2018), 83 FR 48350 (September 24, 2018) (orders instituting proceedings to determine whether to approve or disapprove Pilot Retail Price Improvement Programs of CboeBYX, Nasdaq BX, and NYSE, respectively).

²⁸ See 15 U.S.C. 78f(b)(4), (5), and (8).

IV. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposal. In particular, the Commission invites the written views of interested persons concerning whether the proposal is consistent with Sections 6(b)(5) and 6(b)(8), or any other provision of the Exchange Act, or the rules and regulations thereunder. Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.²⁹

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register].

Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NYSE

ARCA-2018-77 on the subject line.

²⁹ Section 19(b)(2) of the Exchange Act, as amended by the Securities Act Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding – either oral or notice and opportunity for written comments – is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSEARCA-2018-77. The file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to

make publicly available. All submissions should refer to File Number SR-NYSEARCA-2018-77 and should be submitted on or before [insert date 21 days from date of publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³⁰

Eduardo A. Aleman
Deputy Secretary

³⁰ 17 CFR 200.30-3(a)(57) and (58).

