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March 13, 2017

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

Re: Chicago Stock Exchange, Inc.; Notice of Filing of Proposed Rule Change to Adopt the CHX Liquidity Enhancing Access Delay Release No. 34-80041; File No. SR-CHX-2017-04

Dear Mr. Fields:

The FIA Principal Traders Group ("FIA PTG")[1] appreciates the opportunity to comment on the proposal by the Chicago Stock Exchange, Inc. ("CHX" or "the Exchange") to introduce the Liquidity Enhancing Access Delay ("LEAD").

Consistent with our previous two comment letters[2] opposing the proposed CHX Liquidity Taking Access Delay ("LTAD"), FIA PTG believes this new 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"). While we appreciate CHX pulling the LTAD proposal, we are disappointed to see it replaced with a proposal that not only fails to address our major concerns with the LTAD, but also even more unfairly discriminates by providing a speed advantage to a small number of favored market participants.

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[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 and https://www.sec.gov/comments/sr-chx-2016-16/chx201616-1502061-130587.pdf

In addition to our important objections about this proposal, FIA PTG believes more broadly that the Commission should impose a moratorium on new types of artificial delays like this proposal until it is able to complete a comprehensive review of Reg NMS. Layering complexity upon complexity with new exotic delays of different kinds risks making the US equity markets even more difficult to understand and increasingly fragile.

Asymmetric Advantage

The new CHX proposal states, "LEAD is designed to enhance displayed liquidity and price discovery by rectifying a current structural bias against displayed liquidity, without having a materially negative impact on the ability of liquidity takers not engaged in latency arbitrage, such as retail investors, to access displayed liquidity at CHX." In summary it suggests "…correcting asymmetry in the market requires asymmetry in the remedy."

FIA PTG does not agree. First of all, we are unaware of any current structural bias against displayed liquidity. Without the speed-bump, as far as we are aware, it is possible to cancel a resting order just as quickly as it is to send a new marketable order. Without an asymmetrical problem, there is no justification for an asymmetrical remedy, especially one with many negative side effects. Moreover, the LEAD would have the effect of giving **certain** favored traders, extra time to move their quotes out of the way when the market is moving against them. We continue to 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] In fact, as we understand it, the fact that new orders and cancels were treated identically was an important part of the Commission's decision to approve IEX's symmetrical speed-bump.

Unfair Discrimination

We reiterate our previous position that 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. The unfair discrimination in CHX's new LEAD proposal is even more egregious than it was in its previous LTAD proposal. The old proposal, while discriminating against firms with different trading styles and technological capabilities, was at least theoretically open to any market participant willing to use computer algorithms to place and manage resting orders. The new LEAD proposal is explicit in its discrimination. While the proposal provides some objective criteria to be eligible to be a LEAD market maker, meeting those criteria is insufficient. Only firms that meet those criteria, and are selected by CHX are given the speed advantage.

In the proposal, CHX would provide a processing speed advantage to LEAD Market Makers (MMs) which will not be provided to non-LEAD MMs. However, the Exchange

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

submits that the LEAD would not confer any unfair advantage to LEAD MMs or introduce incremental risk of manipulative activity. They contend without convincing evidence that while the LEAD is long enough to neutralize microsecond speed advantages exploited by latency arbitrageurs, it is too short to provide any actionable incremental advantage to LEAD MMs in reacting to information not already in their possession. FIA PTG believes that the advantage that CHX proposes to provide to LEAD market makers is huge and that the Exchange's argument that it is only a small advantage continues to be flawed for the following reasons:

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, this new CHX proposal would continue to attempt to tilt the field significantly and unfairly towards certain favored market makers who would have protected quote status even though their quotes would not be immediately accessible.

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. Many of these order routers use different types of "sweeping" algorithms that take all the quotes at a particular price level. The LEAD proposal would presumably allow LEAD market makers to get out of the way and avoid filling orders such as these. 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.

Third, it is too simplistic to say that the only impact of the LEAD 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 LEAD would frustrate strategies that involve taking prices across multiple venues (or across both futures and equity markets), because it would give extra time to certain favored 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 would not really be accessible.

Proposal Will Reshape Price Discovery Everywhere

FIA PTG is concerned that should the LEAD proposal be approved the impact of this asymmetrical speed bump will not be limited to CHX but will impact price discovery in all

Reg NMS protected markets. We fear the impact would be costly to investors as non-LEAD MMs are forced to widen their bid/ask spreads across the marketplace.

Given the Reg NMS linkages – specifically the order protection rule and the prohibition on locked and crossed markets – the LEAD proposal would have significant negative side effects on liquidity on other markets. While CHX argues that its LEAD proposal would lead to tighter bid-ask spreads and more quoted size on the inside, it is important to realize that there is a big difference between quoted spreads and realizable spreads. Specifically, we expect that with the huge advantage that they would be given, LEAD market makers would, in fact, be able to quote (apparently) tighter spreads and (apparently) larger size then market participants on other market centers, but those prices and sizes would often be inaccessible. In fact, non-LEAD market participants would be required by Reg NMS to honor those "fake" prices when considering trade-throughs and locked-and-crossed markets.

Not De Minimis

Aside from the issues of discrimination under the LEAD, CHX argues that the LEAD 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 continue to 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 myriad 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 LEAD is not a de minimis delay and does discriminate against many market participants, we believe it should be rejected by the Commission. CHX notes that the Commission has previously approved functionality that "permissibly discriminates" among members for the purpose of enhancing displayed liquidity. Again, we disagree and continue to 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). The LEAD, 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. 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 remain unconvinced that the LEAD is not a violation of the Firm Quote Rule under Rule 602 of Reg NMS since it is designed explicitly to allow certain 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, the LEAD provides certain 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 LEAD would enable certain market participants to back away from quotes if the market appears to have moved against them.

While some of our members might be in a position to benefit from the proposal – because of the discrimination inherent in the LEAD, 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, Nasdaq ELO and now CHX LEAD – all four of these iterations highlight the need for a holistic market structure review. Indeed, consider if the time and effort spent developing, evaluating, and responding to these proposals were instead devoted to developing, evaluating, and responding to proposals for comprehensive market structure reform. We might see real progress in addressing the fundamental complexity in market structure. 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

[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

execution requirements will simplify the markets in meaningful ways and provide other important benefits for the investing public.

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

Joanna Mallers
Secretary

cc: Michael S. Piwowar, Acting Chairman
Kara M. Stein, Commissioner