2014–41, and should be submitted on or before October 28, 2014.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[20]

Kevin M. O'Neill,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–73282; File No. SR–NYSEArca–2014–04]

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Amend NYSE Arca, Inc.'s Rules by Revising the Order of Priority of Bids and Offers When Executing Orders in Open Outcry

October 1, 2014.

I. Introduction

On January 15, 2014, NYSE Arca, Inc. (''Exchange'' or ''NYSE Arca'') filed with the Securities and Exchange Commission (''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 revise the order of priority of bids and offers when executing orders in open outcry. The proposed rule change was published for comment in the **Federal Register** on February 3, 2014.[3] On March 18, 2014, the Commission extended the time period for Commission action on the proposal to May 2, 2014.[4] The Commission received ten comment letters from seven commenters regarding the proposal,[5] as well as a response to the comment letters from NYSE Arca.[6] On April 29, 2014, the Exchange filed Amendment No. 1 to the proposed rule change.[7] On May 2, 2014, the Commission instituted proceedings pursuant to Section 19(b)(2)(B) of the Act[8] to determine whether to approve or disapprove the proposed rule change.[9] The Order Instituting Proceedings was published for comment in the **Federal Register** on May 8, 2014.[10] The Commission received an additional response letter and data submission from NYSE Arca.[11] This order approves the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal

NYSE Arca proposed to amend its rules governing the priority of bids and offers on its Consolidated Book by revising the order of priority in open outcry to afford priority to bids and offers represented by Market Makers[12] and Floor Brokers[13] (collectively, ''Crowd Participants'')[14] over certain equal-priced bids and offers of non–Customers[15] on the Consolidated Book[16] during the execution of an order in open outcry on the Floor[17] of the Exchange.[18]

Current Rule 6.75(a) provides that any bids displayed on the Consolidated Book have priority over same-priced bids represented in open outcry. Such priority also is described in current Rule 6.47, which governs crossing orders in open outcry. Floor Broker crossing transactions, as described in Rule 6.47(a)(3), may not trade ahead of bids or offers on the Consolidated Book that are priced equal to or better than the proposed crossing price. The Exchange stated that, because of this priority afforded to the Consolidated Book, Crowd Participants who have negotiated a large transaction ultimately might not be able to participate in its execution.[19]

The Exchange proposed to restructure its priority rules so that bids and offers of Crowd Participants would have priority over equal-priced bids and offers of non-Customers on the Consolidated Book that are ranked in time priority behind any equal-priced Customer bids and offers on the Consolidated Book. Equal-priced Customer[20] interest would continue to be afforded priority over Crowd Participants in the execution of an open outcry transaction. In addition, consistent with the existing price/time priority presently applicable to bids and offers on the Consolidated Book, equal-priced non-Customer bids and offers ranked in time priority ahead of Customer interest also would be

[20] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Securities Exchange Act Release No. 71425 (January 28, 2014), 79 FR 6258 (''Notice'').

[4] *See* Securities Exchange Act Release No. 71733 (March 18, 2014), 79 FR 16072 (March 24, 2014).

[5] *See* Letter from Darren Story, dated January 29, 2014 (''Story Letter I''); Letter from Abraham Kohen, AK FE Consultants LLC, dated January 31, 2014 (''Kohen Letter I''); Letter from David Spack, Chief Compliance Officer, Casey Securities, LLC, dated February 3, 2014 (''Casey Letter''); Letter from Abraham Kohen, AK FE Consultants LLC, dated February 4, 2014 (''Kohen Letter II''); Letter from Angel Alvira, dated February 12, 2014 (''Alvira Letter''); Letter from Donald Hart, dated February 12, 2014 (''Hart Letter I''); Letter from Doug Patterson, Chief Compliance Officer, Cutler Group, LP, dated February 13, 2014 (''Cutler Letter''); Letter from Donald Hart, dated February 18, 2014 (''Hart Letter II''); Letter from Gerald D. O'Connell, Chief Regulatory Officer, Susquehanna International Group, LLP (''SIG''), dated March 14, 2014 (''SIG Letter''); and Letter from Darren Story, dated March 21, 2014 (''Story Letter II'').

[6] *See* Letter from Martha Redding, Chief Counsel, NYSE Euronext, dated April 4, 2014 (''NYSE Arca Response I'').

[7] In Amendment No. 1, the Exchange revised the rule text for proposed Rule 6.47: (1) To clarify that Floor Brokers, when crossing two orders in open outcry, may not trade through any non-Customer bids or offers on the Consolidated Book that are priced better than the proposed execution price; and (2) to conform the term ''bids and offers'' to ''bids or offers'' in paragraphs (a) and (c) thereunder. Amendment No. 1 has been placed in the public comment file for SR–NYSEArca–2014–04 at *http://www.sec.gov/comments/sr-nysearca-2014-04/nysearca201404.shtml* (*see* letter from Martha Redding, Chief Counsel, NYSE Euronext, to Kevin M. O'Neill, Deputy Secretary, Commission, dated April 30, 2014) and also is available on the Exchange's Web site at *http://www.nyse.com/nysenotices/nysearca/rule-filings/pdf.action;jsessionid=FACF4F6772B1316D973F5D4E2D258ACE?file_no=SR-NYSEArca-2014-04&seqnum=2*.

[8] 15 U.S.C. 78s(b)(2)(B).

[9] *See* Securities Exchange Act Release No. 72081 (May 2, 2014), 79 FR 26474 (''Order Instituting Proceedings'').

[10] *See* Order Instituting Proceedings at 79 FR 26474. The comment period closed on May 29, 2014, and the rebuttal period closed on June 12, 2014. On July 29, 2014, the Commission extended the time period for the proceedings for the Commission to determine whether to approve or disapprove the proposed rule change to October 1, 2014. *See* Securities Exchange Act Release No. 72703 (July 29, 2014), 79 FR 45535 (August 5, 2014).

[11] *See* Letter from Martha Redding, Chief Counsel, New York Stock Exchange, dated September 11, 2014 (''NYSE Arca Response II''). The response letter included summary data concerning participation and competition in non-Customer-to-Customer open outcry crossing transactions on NYSE Arca and NYSE Amex Options and is available at *http://www.sec.gov/comments/sr-nysearca-2014-04/nysearca201404.shtml*.

[12] *See* Rule 6.32 (Market Maker Defined).

[13] *See* Rule 6.43 (Options Floor Broker Defined).

[14] The term ''Crowd Participants'' means the Market Makers appointed to an option issue under Rule 6.35, and any Floor Brokers actively representing orders at the best bid or offer on the Exchange for a particular option series. *See* Rule 6.1(b)(38).

[15] A non-Customer is a market participant who does not meet the definition of Customer as defined in paragraph (c)(6) of Rule 15c3–1 under the Securities Exchange Act of 1934, 17 CFR 240.15c3–1. *See* Rule 6.1(b)(29).

[16] The term ''Consolidated Book'' means the Exchange's electronic book of limit orders for the accounts of Public Customers and broker-dealers, and Quotes with Size. *See* Rule 6.1(b)(37).

[17] *See* Rule 1.1(i).

[18] The Exchange also proposed to make non-substantive changes to existing rule text contained in Rules 6.47 and 6.75. *See* Notice, 79 FR at 6260 for a description of these non-substantive changes.

[19] *See* Notice, 79 FR at 6258. The Exchange stated that Crowd Participants could negotiate a transaction with an understanding of the make-up of bids and offers on the Consolidated Book at the beginning of open outcry. However, as the trade is executed, the Consolidated Book could update with newly-arriving electronically-entered bids and offers that have priority under current Rule 6.75(a). The Exchange noted that, given the speed at which quotes can flicker in the Consolidated Book, Crowd Participants who have agreed to a transaction in open outcry do not know if they will actually participate on the trade until after execution. *Id.* at 6258–59.

[20] *See supra* note 15.

afforded priority over Crowd Participants in the execution of an open outcry transaction. In the Exchange's view, the proposed rule change strikes the appropriate balance between encouraging larger negotiated transactions in open outcry, while at the same time protecting Customer interest on the Consolidated Book, and any interest that has time priority over such protected Customer interest.[21]

To effect this change to its floor priority rules, the proposal would amend the Exchange's rules as follows. As noted above, Rule 6.75(a) presently states that the highest bid shall have priority but where two or more bids for the same option contract represent the highest price and one such bid is displayed on the Consolidated Book, such bid shall have priority over any bid at the post (*i.e.,* the Trading Crowd[22]). The Exchange proposed to amend Rule 6.75(a)[23] by limiting the priority of bids in the Consolidated Book over bids in the Trading Crowd solely to those bids for Customers along with non-Customers that are ranked in time priority ahead of such Customers.[24]

Rule 6.76 presently governs order ranking, display and allocation of orders on the NYSE Arca Options platform (''OX system''). The Exchange proposed new paragraph (d) to Rule 6.76 that would set forth the priority of bids and offers on the Consolidated Book against orders executed through open outcry in the Trading Crowd. The proposed text provides a step-by step-description of the order of priority to be afforded bids and offers of both Customers and non-Customers on the Consolidated Book. The Exchange noted that the priority scheme described in proposed Rule 6.76(d) is consistent with the proposed changes to Rule 6.75.[25]

The Exchange also proposed to include language in Rule 6.76(d)(4) that sets forth certain OTP Holder[26] obligations under Section 11(a) of the Act.[27] The proposed rule text states that, notwithstanding the priority scheme set forth in proposed Rule 6.76(d)(2), an OTP Holder effecting a transaction on the Floor for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion pursuant to the ''G Rule'' must still yield priority to any equal-priced non-OTP Holder bids or offers on the Consolidated Book.[28]

Rule 6.47 outlines the procedures used when a Floor Broker attempts to cross two orders in open outcry. Currently, Floor Brokers must trade against all equal-priced Customer and non-Customer bids and offers in the Consolidated Book before effecting a cross transaction in the Trading Crowd. The Exchange proposed to revise Rule 6.47 to conform the priority rules applicable to open outcry cross transactions to the proposed changes described above. Accordingly, the Exchange proposed to amend the procedures for the crossing scenarios described in Rule 6.47[29] by stating that Floor Brokers, when crossing two orders in open outcry, must yield priority to: (1) Any Customer bids or offers on the Consolidated Book that are priced equal to or better than the proposed execution price and to any non-Customer bids or offers on the Consolidated Book that are ranked ahead of such equal or better-priced Customer bids or offers; and (2) to any non-Customer bids or offers on the Consolidated Book that are priced better than the proposed execution price.[30] The Exchange noted that Floor Brokers would be required to trade against equal and better-priced Customer bids or offers on the Consolidated Book, any better-priced bids or offers of non-Customers on the Consolidated Book and any non-Customer bids or offers that are ranked ahead of equal-priced Customer bids or offers, before attempting a cross transaction.[31] Consistent with proposed Rule 6.75(a), Floor Brokers would not be required to trade against equal-priced non-Customer bids and offers that are ranked behind such Customer and non-Customer bids and offers.[32]

The Exchange stated that it would announce the implementation date of the proposed rule change by Trader Update to be published no later than 90 days following approval[33] and the implementation date would be no later than 90 days following the issuance of the Trader Update.

III. Comment Letters and NYSE Arca's Responses

The Commission received ten comment letters from seven commenters.[34] NYSE Arca submitted a response to the comment letters and an additional letter and data submission in response to the Order Instituting Proceedings.[35]

Five of the commenters, four of whom identified themselves as Crowd Participants on NYSE Arca,[36] generally were supportive of the proposal to revise the order of priority of bids and offers when executing orders in open outcry.[37] Four of these commenters stated a view that the proposal would

[21] *See* Notice, 79 FR at 6259.

[22] The term ''Trading Crowd'' means all Market Makers who hold an appointment in the option classes at the trading post where such trading crowd is located and all Market Makers who regularly effect transactions in person for their Market Maker accounts at that trading post, but generally will consist of the individuals present at the trading post. *See* Rule 6.1(b)(30).

[23] The Exchange noted that the changes made to Rule 6.75(a) dealing with the priority of ''bids'' also would effect a corresponding change to the meaning of Rule 6.75(b) dealing with ''offers,'' although there would be no change to the rule text in Rule 6.75(b). *See* Notice, 79 FR at 6259.

[24] *See* Notice, 79 FR at 6259–60 for examples illustrating how the Exchange's priority and allocation rules would be applied under the proposed rule change.

[25] *See* Notice, 79 FR at 6259. According to the Exchange, the inclusion of a description of open outcry priority procedures in Rule 6.76 would serve as a useful cross reference to Rule 6.75. The Exchange stated that including such a cross reference is consistent with similar rule structures by the Chicago Board Options Exchange, Inc. (''CBOE'') and NYSE MKT LLC (''NYSE MKT''). *See id.* (citing CBOE Rule 6.45A(b) and NYSE MKT Rule 964NY(e)).

[26] *See* Rule 1.1(q).

[27] Specifically, pursuant to Section 11(a)(1)(G) of the Exchange Act and Rule 11a1–1(T) thereunder (the ''G Rule''), an OTP Holder may effect transactions on the Floor for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion, provided that such transaction yields priority in execution to orders for the account of persons who are not OTP Holders or associated with OTP Holders. *See* 15 U.S.C. 78k(a)(1)(G) and 17 CFR 11a1–1(T). The Exchange stated that the proposed rule text is based on the rules of the CBOE and NYSE MKT on behalf of NYSE Amex Options. *See* Notice, 79 FR at 6259 (citing CBOE Rule 6.45A(b)(i)(D) and NYSE MKT Rule 910NY).

[28] According to the Exchange, at this time, no OTP Holder that currently operates on the Exchange's Floor as a Floor Broker enters orders for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion. The Exchange stated, however, that the Financial Industry Regulatory Authority, Inc. on behalf of NYSE Regulation, Inc., monitors whether Floor Brokers comply with Section 11(a) of the Act. *See id.*

[29] The crossing scenarios described in Rule 6.47 are: (a) Non-Facilitation (Regular Way) Crosses; (b) Facilitation Procedures; (c) Crossing Solicited Orders; (d) Mid-Point Cross; and (e) Customer-to-Customer Cross. The Exchange did not propose any change to Rule 6.47(d) relating to Mid-Point Cross, and thus Mid-Point Cross transactions would not be affected by the proposed rule change. Telephone conversation between Glenn Gsell, Managing Director, NYSE Arca and Commission staff, dated April 23, 2014.

[30] *See* Notice, 79 FR at 6259–60 for examples illustrating the proposed priority changes as applicable for Non-Facilitation and Facilitation Crosses. *See also* Amendment No. 1, *supra* note 7.

[31] *See* Notice, 79 FR at 6259.

[32] The Exchange stated its belief that affording priority to Crowd Participants ahead of such non-Customer interest on the Consolidated Book would create an increased incentive for block-sized transactions on the Floor. *See* Notice, 79 FR at 6259.

[33] *See* Notice, 79 FR at 6260.

[34] *See supra* note 5.

[35] *See supra* notes 6 and 11.

[36] *See* Casey Letter (Floor Broker); Alvira Letter (Market Maker); Hart Letters I and II (Market Maker); Cutler Letter (Crowd Participant), *supra* note 5.

[37] *See* Story Letters I and II; Casey Letter; Alvira Letter; Hart Letter I and II; and Cutler Letter.

allow NYSE Arca to compete with other exchanges that currently have similar priority rules.[38] Three of these commenters stated that the proposal would allow Crowd Participants to compete with bids and offers of non-Customers on the Consolidated Book,[39] and two of them stated that Crowd Participants were the market participants most likely to provide services during times of market duress.[40] Two commenters also noted that the rule change would maintain priority for Customer orders resting on the Consolidated Book.[41]

Two commenters stated their belief that the proposal would increase competition on the floor for orders,[42] and one of these commenters noted that this competition would benefit the investing public.[43] Similarly, two commenters stated their view that the proposal would improve investor executions on the floor.[44] One commenter noted that the proposal would create an advantage for price improving customers.[45]

Two commenters expressed concerns about the proposal.[46] One commenter stated its view that the proposal would disenfranchise and disadvantage certain market participants, and suggested instead that the Exchange give size preference for equal bid prices.[47] The commenter believed that such preference would be a more fair way of revising the priority of bids and offers.[48] This commenter further noted that, under the Exchange's proposal, even small bids from Crowd Participants would take priority over electronic non-Customer bids.[49] The same commenter also noted its belief that best execution is not enhanced by allowing more exchanges to disadvantage other traders.[50] The commenter suggested that, regardless of the merits of high frequency trading, there was no reason to disadvantage all non-Customers by giving priority to one class of traders that would allow them to jump ahead of the queue.[51] One commenter who supported the proposal took issue with views expressed by this commenter and noted that current NYSE Arca rules are structured so as to disadvantage on-floor market makers.[52]

Another commenter also raised concerns with the proposal.[53] The commenter acknowledged that the proposal would reduce the number of instances where high-frequency, non-Customer orders arriving on to the book could cause Crowd Participants to be ''scaled-back'' from agreed-upon negotiated amounts. The commenter acknowledged that this ''scaling back'' currently presented certain operational and hedging challenges to Crowd Participants.[54] The commenter remarked, however, that the proposal apparently was focused on attracting block cross volume to the Exchange.[55]

The commenter noted that when NYSE Arca uses the term ''Crowd Participants,'' it appears to refer to off-floor trading houses that attempt to internalize, in large part, block orders from institutional customers (*i.e.,* clean cross orders). The commenter acknowledged that this term also includes option market makers on the NYSE Arca Floor, but stated its view that the market maker participation in such orders is often minimal as a percentage of the total order size.[56] The commenter stated that the majority of available market maker liquidity at the Exchange is represented by a group of off-floor market maker firms that are collectively responsible for over 90% of displayed liquidity in multiply traded options, rather than on-floor market makers.[57]

The commenter further stated its view that the proposal would attract more clean-cross type orders that it believes would further insulate customer interest from competition by parties other than crowd participants.[58] In its view, because such negotiations usually occur outside the view of off-floor market makers, the crosses often occur at prices that have not been sufficiently vetted by those most likely to offer price improvement.[59] Given its concerns, the commenter believed that the proposal would be detrimental to investors, as the opportunity for price improvement would be significantly diminished.[60]

The commenter stated that the proposal did not provide an explanation regarding how more crowd participation in larger-sized block floor crosses would benefit customers or the market in general.[61] The commenter acknowledged that, as other floor exchanges have rules that place booked

[38] *See* Casey Letter (''The Proposal would still leave Arca Crowd Participants at a slight disadvantage to crowd participants on CBOE and Amex, but would go a long way towards leveling the playing field''); Alvira Letter (''I would like to see us in a competitive balance with the AMEX who have already implemented the change''); Cutler Letter (''AMEX and CBOE currently have similar rules in place''); and Hart Letter II (''This would enable the PCX to level the rules with other exchanges''). *See also* SIG Letter (''the proposal at least relates in part to a legitimate competitive concern'').

[39] *See* Casey Letter (''The current market structure leaves NYSE Arca Crowd Participants and their customers at a distinct disadvantage . . . to non-customer professional traders, including High Frequency Traders''); Hart Letter I (''This rule disadvantages floor based market makers, which are the only ones providing liquidity when the markets are under duress''); and Cutler Letter (''This Proposed Rule change will level the competitive balance between floor market makers and electronic non-customer professional traders'').

[40] *See* Hart Letter I (''market makers . . . are the only ones providing liquidity when the markets are under duress'') and Story Letter II (''Perhaps one of the most compelling arguments for floor based market-makers is that they are required to stand in and make two-sided markets in volatile environments. They cannot just turn off the machines and walk away'').

[41] *See* Story Letter I (''It will allow for price discovery and improvement, but at the same time maintaining protection for customer orders resting on the order book'') and Casey Letter (''As Crowd Participants will still be required to interact with any Customer orders in the Consolidated Book, public Customers will not be adversely affected'').

[42] *See* Casey Letter (''The Proposal, by creating more uniform open outcry priority rules across floors, will increase competition for execution of these negotiated transactions'') and Story Letter II (''This filing will create an advantage for price improving CUSTOMER orders'') (emphasis in original).

[43] *See* Casey Letter (''Increasing competition in financial markets is nearly always beneficial for investors; the Proposal would increase competition among options floor brokers, and would ultimately benefit the investing public'').

[44] *See* Story Letter I (''This rule change will allow market participants to IMPROVE fills for customers without creating any disadvantage for other market participants'') and Casey Letter (''The execution of sizeable negotiated transactions in listed options is an important service provided to investors almost exclusively by the few remaining options Floor Brokers. The Proposal . . . will provide investors with greater flexibility, greater access to liquidity, and lower execution costs'') (emphasis in original).

[45] *See* Story Letter II.

[46] *See* Kohen Letters I and II; and SIG Letter.

[47] *See* Kohen Letter I.

[48] *See* Kohen Letter I.

[49] *See* Kohen Letter I (''otherwise Crowd Participants' 1 contract or 100 share bid will always take priority'').

[50] *See* Kohen Letter II.

[51] *See* Kohen Letter II.

[52] *See* Story Letter II.

[53] *See* SIG Letter.

[54] *See* SIG Letter at 1.

[55] *See* SIG Letter at 1 (''This focus is made apparent by Arca when it asserts that the new rule . . . will provide greater opportunity for bids and offers of crowd participants to participate in open outcry transaction [sic] and therefore promote larger-sized negotiated transactions'').

[56] *See* SIG Letter at 2.

[57] *See* SIG Letter at 2. The commenter remarked that, due to the off-floor market makers, electronic crossing systems for block sized orders generally have shown to be a better alternative to floor crosses, at least on a transparency and price competition basis. *Id.*

[58] *See* SIG Letter at 2.

[59] *See* SIG Letter at 2. The commenter also noted that it had submitted a Petition for Rulemaking filed with the Commission in April 2013. The commenter represented that, in that petition, several market making firms (including the commenter) asserted their belief that exchanges with trading floors would generate better priced executions for customers if they required crosses to be auctioned through electronic systems that included off-floor registered market makers in the respective option classes. *See* Petition for Rulemaking Regarding Option Floor Crosses, File No. 4–662 (April 22, 2013), available at *http://www.sec.gov/rules/petitions/2013/petn4-662.pdf.*

[60] *See* SIG Letter at 2–3.

[61] *See* SIG Letter at 3.

parity interest behind crowd participants, NYSE Arca's proposal at least relates in part to a legitimate competitive concern for the Exchange.[62] However, the commenter stated that it was important that exchanges give sufficient reason why a proposed rule is not injurious to customers or the market in general, and that the Exchange's proposal fails to give such reasons, perhaps, as the commenter opined, because there were none to give.[63] The commenter requested that the Commission establish the reasoning behind the Exchange's desire to increase block-cross volume and the reasons, if any, for NYSE Arca's belief that more (and cleaner) block floor crosses were good for investors.[64]

One commenter who supported the proposal raised issues with the arguments made by the commenter who expressed several concerns regarding the proposal.[65] The commenter who supported the proposal stated that the other commenter's concerns were misguided and unfounded because the proposal would allow for price improvement on any size order, whether large or not. The commenter who supported the proposal also noted that the proposal would allow large market-making groups like itself to continue to provide inside markets and actually trade at those prices on NYSE Arca.[66] The commenter who supported the proposal disagreed with the suggestion that the proposal was necessarily about attracting clean-crosses outside the view of off-floor market makers, and stated its belief that the rule was designed to provide opportunity to improve markets.[67]

NYSE Arca provided a response letter addressing issues raised by the commenters.[68] NYSE Arca emphasized that the proposal would align the rules of the Exchange with other U.S. options exchange trading floors, but with a unique caveat that any non-Customer electronic interest with time priority over a Customer order in the Book also would maintain priority over floor participants.[69]

In response to one commenter's suggestion that the Exchange adopt a pure size priority model,[70] NYSE Arca stated that a wholesale restructuring of its priority model was beyond the scope of the current proposal.[71] NYSE Arca further noted its view that such a model would unduly disadvantage small size retail customer orders by allowing later-arriving professional participants willing to trade a larger quantity to be accorded priority.[72]

In response to one commenter who expressed several concerns regarding the proposal, NYSE Arca stated that the concerns about the practice of crossing institutional orders without electronic participants providing price improvement was unrelated to the proposal to allocate priority among participants at the same price.[73] NYSE Arca noted that its rules would continue to give priority to participants who display an improved price.[74]

NYSE Arca disagreed with that commenter's suggestion that the proposal would attract more clean-cross type orders, noting that the proposal was intended to promote liquidity and price discovery, and stated that nothing would ''insulate customer interest from competition by parties other than crowd participants.'' [75] NYSE Arca stated that the proposal is intended to promote liquidity and price discovery on the Exchange by adopting a priority structure that would be similar to, but more favorable for electronic non-Customer participants than, the priority structure that exists on other U.S. options trading floors.[76] The Exchange pointed out that the execution price would have to be equal to or better than the NBBO and that Crowd Participants would have to yield to superior electronic bids or offers.[77] NYSE Arca stated further that the proposal would not reduce the ability or incentive for any participant to improve its displayed quote electronically, as the proposal only would impact the allocation of orders among multiple participants at the same price.[78]

In response to the commenter's request that the Exchange explain why more (and cleaner) block floor crosses are good for investors, the Exchange noted its view that institutional trading desks provide a valuable service by providing liquidity to their customers for block-size orders.[79] The Exchange stated, however, that it did not believe that the total level of larger-size block floor crosses in the industry would increase as a result of its proposal.[80] The Exchange noted that other trading floors currently execute existing institutional block cross volume, and the Exchange's goal was to offer an alternative venue for such executions.[81]

After the Commission issued the Order Instituting Proceedings, NYSE Arca submitted a second comment letter, which concerned participation in open outcry crossing transactions on NYSE Arca.[82] According to the Exchange, it believed that comparing data relating to non-Customer-to-Customer Floor crossing transactions on NYSE Arca with similar data for NYSE Amex Options, the Exchange's affiliated options market that provides priority to Floor participants over non-Customers on its electronic book, would support the argument that the proposed rule change would create a more robust open outcry market and benefit investors who choose to send orders to the Exchange.[83]

IV. Discussion and Commission Findings

After careful review of the proposed rule change as well as the comment letters and the NYSE Arca response letter received on the proposal, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange and, in particular, with Section 6(b) of the Act.[84] In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,[85] which requires, among other things, that the rules of a national securities exchange be designed to

[62] *See* SIG Letter at 3 (''No doubt, Arca relies heavily on open outcry crosses for transaction volume. And, no doubt, the more often that high-frequency professional booked orders break-up 'matched' floor crosses, the more likely it becomes that off-floor facilitating firms will send their orders to other exchanges to be crossed'').

[63] *See* SIG Letter at 3.

[64] *See* SIG Letter at 3.

[65] *See* Story Letter II.

[66] *See* Story Letter II.

[67] *See* Story Letter II.

[68] *See* NYSE Arca Response Letter I.

[69] *See* NYSE Arca Response Letter I at 1–4.

[70] *See* Kohen Letters I and II.

[71] *See* NYSE Arca Response Letter I at 2.

[72] *See* NYSE Arca Response Letter I at 2.

[73] *See* NYSE Arca Response Letter I at 2.

[74] *See* NYSE Arca Response Letter I at 2.

[75] *See* NYSE Arca Response Letter I at 2–3.

[76] *See* NYSE Arca Response Letter I at 3.

[77] *See* NYSE Arca Response Letter I at 3.

[78] *See* NYSE Arca Response Letter I at 3.

[79] *See* NYSE Arca Response Letter I at 3.

[80] *See* NYSE Arca Response Letter I at 3.

[81] *See* NYSE Arca Response Letter I at 3. The Exchange also provided examples where a firm looking to facilitate its customer order might choose to send the order to an exchange other than NYSE Arca under the Exchange's current priority rules. *Id.*

[82] *See* NYSE Arca Response Letter II.

[83] *See* NYSE Arca Response Letter II at 1–2. The data provided by the Exchange showed that floor market makers and/or book participants participated in only 34.5% of the total crossing contracts executed on the NYSE Arca Floor, whereas on NYSE Amex Options, such participants participated in 53.4% of the total crossing contracts executed. *See id.* at 2. Although the data did not describe the actual contract execution participation percentages for either floor market makers or book participants, the Exchange believed that the data showed that, if it had rules similar to other options exchange trading floors, the Exchange would see an increase in Floor market maker participation in Floor crossing transactions. *See id.*

[84] 15 U.S.C. 78f(b). In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[85] 15 U.S.C. 78f(b)(5).

prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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 not be designed to permit unfair discrimination between customers, issuers, brokers or dealers.[86]

As noted above, the Commission received ten comment letters from seven commenters in response to the proposed rule change.[87] Five of the commenters supported the proposed rule change,[88] while two other commenters raised concerns about whether the Exchange's proposed revisions to its rules governing priority during open outcry were appropriate, as more fully described above.[89] In its review of the proposal, the Commission has carefully considered all of the comments received. The Commission acknowledges the concerns raised by one commenter, as detailed above,[90] about the potential impact on competition resulting from the proposed change in the Exchange's rules governing priority and order allocation for open outcry transactions. At the same time, the Commission also acknowledges the Exchange's belief that this proposal will lead to greater competition for orders and will create a more robust open outcry market and its belief that, without the proposal, the Exchange would be at a competitive disadvantage compared to other exchanges that operate trading floors.[91]

Rule 6.75(a), as proposed to be revised, describes NYSE Arca's priority and order allocation for open outcry transactions, including procedures to be followed when there is interest at the same price in the Consolidated Book as on the Floor. Rule 6.76(d), as proposed to be revised, describes NYSE Arca's order ranking, display and allocation of orders on the OX system, and the priority described in proposed Rule 6.76(d) is consistent with the changes to Rule 6.75(a). The proposed rules governing priority during open outcry transactions on the Exchange's floor are similar to the priority rules at other exchanges with trading floors.[92] Rule 6.47, as proposed to be revised, describes priority and order allocation for crossing orders in open outcry transactions. The proposed rules governing open outcry during crossing transactions on the Exchange floor are similar to the rules governing priority in crossing transactions at other exchanges.[93] Given that other options exchanges currently have rules that provide lower priority to non-priority customer orders on the electronic book during floor transactions on those exchanges, including during crossing transactions, the Exchange's proposed revisions to its priority scheme for floor transactions will allow NYSE Arca to compete with other floor-based exchanges that have substantially similar rules. Accordingly, the Commission believes that it would be appropriate and consistent with the Act to approve the Exchange's proposed rule change.[94]

As noted above, one commenter remarked that it had submitted a Petition for Rulemaking with the Commission that asserts that exchanges with trading floors would generate better priced executions for customers if they required crosses to be auctioned through electronic systems that included off-floor registered market makers in their respective option classes.[95] Although the Petition for Rulemaking raises concerns involving how orders are crossed on options exchange floors, the recommendations in the Petition for Rulemaking[96] are beyond the scope of the Commission's consideration in connection with the instant proposed rule change. However, Commission staff will evaluate the Petition for Rulemaking and how best to address the concerns raised therein.

[86] The Exchange represented that the proposed rule change is consistent with Section 11(a) of the Act and the rules thereunder and would not limit in any way the obligations of OTP Holders to comply with Section 11(a) or the rules thereunder. *See* Notice, 79 FR at 6261. The Exchange also represented that the proposed rule change raises no novel issues under Section 11(a) and the rules thereunder from a compliance, surveillance or enforcement perspective. *See id.* The Commission notes that each member of the Exchange is responsible for ensuring that its conduct is in compliance with the requirements of Section 11(a) of the Act and the rules promulgated thereunder.

[87] *See supra* note 5.

[88] *See* Story Letters I and II; Casey Letter; Alvira Letter; Hart Letters I and II; and Cutler Letter.

[89] *See* Kohen Letters I and II; and SIG Letter. *See also* notes 46–64 and accompanying text describing the issues and concerns raised by these comments.

[90] *See supra* notes 53–64 and accompanying text.

[91] *See* Notice, 79 FR at 6261.

[92] *See, e.g.,* CBOE Rule 6.45A; NYSE MKT Rules 963NY and 964NY. CBOE Rule 6.45A(b)(i) provides that, after public customer orders in the electronic book, in-crowd market participants shall have second priority and broker-dealer orders in the electronic book and electronic quotes of Market-Makers shall have third priority. NYSE MKT Rule 963NY(a)–(b) provides that, after Customer orders displayed on the Consolidated Book, an order in the crowd shall have priority over a non-Customer order displayed in the Consolidated Book. NYSE MKT Rule 964NY(e) further requires that for Floor Brokers manually representing orders in the trading crowd, Customer orders in the Consolidated Book have first priority, ATP Holders of the trading crowd have second priority and broker-dealers, Professional Customers (including Quotes with Size and orders of Market Makers) in the Consolidated Book have third priority.

[93] *See, e.g.,* CBOE Rule 6.74; NYSE MKT Rule 934NY. CBOE Rule 6.74 provides that for purposes of establishing priority at the same price, bids and offers of In Crowd Market Participants have first priority, except with respect to public customer orders resting in the electronic book; and all other bids and offers (including bids and offers of broker-dealer orders in the electronic book and electronic quotes of Market-Makers) have second priority. NYSE MKT Rule 934NY(b)(3) provides that, for a non-facilitation cross, if there are bids or offers in the Consolidated Book better than the proposed execution price or Customer Orders in the Consolidated Book priced at the proposed execution price, the Floor Broker must trade against such bids or offers in the Consolidated Book. Once bids or offers in the Book are satisfied, the Floor Broker may cross the balance of the orders, if any, to be crossed.

[94] As noted above, the Exchange's proposal is intended to bring its floor priority rules for crossing orders in line with the floor priority rules of certain other options exchanges. However, the Commission is aware of the concerns, as expressed by commenters, that the rules of an options trading floor should allow for sufficient competition for orders. This concern is one that the Commission staff intends to continue to evaluate in the context of its ongoing empirical consideration of market structure. For example, there currently is relatively little information available about the extent and nature of floor crossing transactions. The Commission staff, however, expects that an exchange with a trading floor, as part of its regulatory obligations, will monitor the extent to which competition is maintained in floor crossing transactions. One way an exchange could do so would be to assess periodically the level of participation in such crossing transactions by market makers and other market participants, aside from the firm that initiated the cross, and review whether its rules appropriately allow for such competition. In addition, the Commission reminds broker-dealers that the duty of best execution requires them to assess periodically the quality of competing markets to assure that order flow is directed to the markets providing the most beneficial terms for their customer orders. *See, e.g.,* Order Execution Obligations, Securities Exchange Act Release No. 37619A (September 6, 1996), 61 FR 48290 at 48322–33 (September 12, 1996). Broker-dealers must examine their procedures for seeking to obtain best execution in light of market and technology changes and modify those practices if necessary to enable their customers to obtain the best reasonably available prices. *See id.* at 48323. In doing so, broker-dealers must take into account price improvement opportunities, and whether different markets may be more suitable for different types of orders or particular securities. *See id.*

[95] *See supra* note 59 and accompanying text.

[96] The Petition for Rulemaking requests, among other things, that the Commission require each floor-based U.S. options exchange to provide an electronic-cross auction mechanism for all multiply-listed options traded on its trading floor and ensure that the mechanism is made electronically accessible from on and off the trading floor by qualified members and that all block-sized matched option crosses involving customer orders be auctioned through such mechanism. *See* Petition for Rulemaking regarding Option Floor Crosses, *supra* note 59.

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,[97] that the proposed rule change, as modified by Amendment No. 1, (SR–NYSEArca–2014–04) is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[98]

Kevin M. O'Neill,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–73281; File No. SR–NYSEArca–2014–110]

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Proposed Rule Change Amending Rule 6.2A To Authorize the Exchange To Share Any User-Designated Risk Settings in Exchange Systems With the Clearing Member That Clears Transactions on Behalf of the User

October 1, 2014.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (the ''Act'') [2] and Rule 19b–4 thereunder,[3] notice is hereby given that, on September 19, 2014, NYSE Arca, Inc. (the ''Exchange'' or ''NYSE Arca'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of the Substance of the Proposed Rule Change

The Exchange proposes to amend Rule 6.2A (Access to and Conduct on OX) to authorize the Exchange to share any User-designated risk settings in Exchange systems with the Clearing Member that clears transactions on behalf of the User. The text of the proposed rule change is available on the Exchange's Web site at *www.nyse.com,* at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend Rule 6.2A (Access to and Conduct on OX) to authorize the Exchange to share any User-designated risk settings in Exchange systems with the Clearing Member that clears transactions on behalf of the User.

Rule 6.2A states that ''[u]nless otherwise provided in the Rules, no one but a User shall effect any transaction on OX.'' [4] OX is ''the Exchange's electronic order delivery, execution and reporting system for designated option issues through which orders and quotes of Users are consolidated for execution and/or display.'' [5] The Exchange proposes to amend the current rule by adding the following sentence: ''The Exchange may share any User-designated risk settings in OX with the Clearing Member that clears transactions on behalf of the User.'' [6] A ''User'' is ''any OTP Holder, OTP Firm or Sponsored Participant that is authorized to obtain access to OX pursuant to Rule 6.2A.'' [7]

Each User that transacts through a Clearing Member on the Exchange executes a Clearing Letter of Consent, which ''shall be deemed a letter of guarantee, letter of authorization, or notice of consent pursuant to NYSE Arca Rules and may be relied upon by NYSE Arca, Inc., the [National Securities Clearing Corporation], the [Options Clearing Corporation], and their respective members.'' [8] The Exchange believes that because Clearing Members that execute a Clearing Letter of Consent guarantee all transactions of those Users, and therefore bear the risk associated with those transactions, it is appropriate for Clearing Members to have knowledge of what risk settings a User may utilize within Exchange systems.

At this time, the risk settings covered by this proposal are set forth in Rule 6.40 (Risk Limitation Mechanism).[9] Pursuant to Rule 6.40(b)–(d), Users may set certain risk control thresholds in the Risk Limitation Mechanism, which are designed to mitigate the potential risks of multiple executions against a User's trading interest that, in today's highly automated and electronic trading environment, can occur simultaneously across multiple series and multiple option classes. As proposed, the Exchange may share a User's Risk Limitation Mechanism settings with the Clearing Member that guarantees the User's transactions on the Exchange, and therefore has a financial interest in understanding the risk tolerance of the User.

Because the Clearing Letter of Consent codifies relationships between each User and Clearing Member, the Exchange is on notice of which Clearing Members have relationships with which Users. The proposed rule change would simply provide the Exchange with authority to directly provide Clearing Members with information that may otherwise be available to such Clearing Members by virtue of their relationship with the respective Users.

2. Statutory Basis

The statutory basis for the proposed rule change is Section 6(b)(5) of the Securities Exchange Act of 1934 (the ''Act''), in general, and furthers the objectives of Section 6(b)(5),[10] which requires the rules of an exchange to 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.

The Exchange believes that the proposed rule change removes impediments to and perfects the mechanism of a free and open market by codifying that the Exchange can directly

[97] 15 U.S.C. 78s(b)(2).

[98] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

[4] *See* Rule 6.2A.

[5] *See* Rule 6.1A(13) [sic].

[6] *See* proposed Rule 6.2A.

[7] *See* Rule 6.1A(19) [sic].

[8] *See* NYSE Arca Options OTP Application, Section 8 (Clearing Letter of Consent), available here, *https://www.nyse.com/publicdocs/nyse/markets/arca-options/NYSE_Arca_Options_OTP_Firm_Application.pdf.*

[9] The Exchange may adopt additional rules providing for User-enabled risk settings that would be covered under this proposal. The Exchange will announce via Trader Update any additional risk settings (*i.e.,* other than Rule 6.40(b)–(d)) that are adopted and covered by proposed Rule 6.2A.

[10] 15 U.S.C. 78f(b)(5).