



November 3, 2015

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

**RE: Investors' Exchange, LLC ("IEX"); Notice of Filing of Application, as Amended, for Registration as a National Securities Exchange under Section 6 of the Securities Exchange Act of 1934; Release No. 34-75925; File No. 10-222.**

Dear Mr. Fields:

BATS Global Markets, Inc. ("BATS") appreciates the opportunity to comment on the above-referenced Form 1 application for registration as a national securities exchange filed by IEX. At the outset, BATS applauds IEX for agreeing to the higher standards and burdens of being a registered exchange as compared to an alternative trading system ("ATS"). BATS supports IEX's application and believes the Commission should act promptly to approve it. IEX follows the well-trodden path of other "upstarts" before it, including BATS and Direct Edge, both of whom launched as ATSS and subsequently transitioned to the higher standards of national securities exchanges after their innovative platforms and pricing gained critical support of customers and investors. BATS welcomes the additional competition in the exchange market, and IEX should be allowed to compete with full exchange status and the obligations that accompany that status.

As discussed in greater detail below, while BATS supports IEX's Form 1 application, BATS believes it is incumbent on the Commission to articulate in its approval order the permissible standards for intentional delays by a registered exchange in accessing a quotation that would still qualify such quotation as automated under Regulation NMS. BATS further believes that IEX's Form 1 application should be amended to remove an unfair and unreasonably discriminatory advantage the IEX exchange system currently plans to provide to its limited purpose, exchange-affiliated broker-dealer; namely, private, instantaneous access to execution information from IEX while other market participants are denied such access. While such discriminatory advantages are acceptable as an ATS, they do not meet the enhanced obligations of a registered exchange.

### **Automated Quotations under Regulation NMS**

As has been widely reported, the IEX platform includes a 350 microsecond delay in the processing of inbound orders and outbound market data, which is made possible by the spooling of cable into what is commonly referred to as the "magic shoebox". As an ATS dark pool, this 350 microsecond delay provides IEX the ability to update the prices of resting orders that are

pegged to the national best bid or offer (“NBBO”), the midpoint of the NBBO, or some offset from the NBBO, before market participants with faster access to market data can access those now stale prices on IEX.

This advantage is much less clear as a registered national exchange with publicly disseminated quotes that will contribute to the NBBO. In fact, BATS believes the inclusion of the IEX quote in the NBBO will negate the current protections the 350 microsecond delay affords its customers. Consider the following example:

Assume the NBBO is \$10.00 x \$10.01 and there are bids on multiple exchanges, including IEX, at \$10.00. Also assume there are midpoint pegged orders on IEX to buy at \$10.005. Also assume market conditions change and bids on all exchanges as reflected in the direct market data feeds are reduced to \$9.99. As an ATS dark pool without a protected quotation, the 350 microsecond delay afforded IEX time to update the prices of their resting midpoint pegged orders before they could be adversely executed at the midpoint of the stale market data.

As a registered exchange with protected quotes, IEX can no longer adjust pegged orders in response to orders executing against the NBBO on other exchanges if an IEX member has an order at that NBBO on IEX. Instead, using the example above, if an IEX member has displayed an order on IEX at the soon to be stale national best bid of \$10.00, IEX is dependent on that member to adjust its bid before IEX can adjust its own view of the NBBO and the ranked prices of their resting midpoint pegged orders. Any market participants with access to faster market data than the member who placed the soon to be stale \$10.00 national best bid on IEX can enter orders into IEX and can trade against the resting midpoint pegged orders at the stale price of \$10.005 or the stale displayed bid at \$10.00.

In effect, the 350 microsecond delay affords no benefits to the member who placed the displayed bid at \$10.00 on IEX and any benefits to hidden orders that previously existed when IEX was an ATS dark pool are eliminated whenever IEX has protected quotations at the NBBO. In fact, the more successful IEX is in attracting displayed liquidity to its exchange – a core function of the price discovery process provided by registered exchanges – the less effective IEX’s intentional delay is in protecting its customers’ orders.

This, of course, is not necessarily a reason to disapprove this aspect of the IEX Form 1 application; however, it does raise questions that are deserving of an answer from the Commission regarding the extent to which the magic shoebox furthers the protection of investors as required of registered exchanges under Section 6 of the Exchange Act. BATS further believes IEX should be required to amend its Form 1 to include a description of the magic shoebox in its rules describing its operation in detail and including a discussion of the statutory basis in support of this feature.

In addition, BATS believes that when approving the IEX Form 1 application, it is incumbent on the Commission to specifically articulate the extent of permissible delays that

would be considered consistent with the Exchange Act, including Regulation NMS thereunder, for registered exchanges. In particular, to the extent the Commission grants IEX protected quotation status under Regulation NMS, it is incumbent on the Commission to articulate the standards it applies to determine that status. For example, Rule 600(b)(57) of Regulation NMS defines a protected bid or offer in part as a quotation that “[i]s displayed by an automated trading center.” Rule 600(b)(4) of Regulation NMS in turn defines an automated trading center in part as a trading center that is “capable of displaying quotations that meet the requirements for an automated quotation.” And, Rule 600(b)(3) defines an automated quotation as a quotation displayed by a trading center that “(ii) [i]mmediately and automatically executes an order marked as an immediate-or-cancel order against the displayed quotation up to its full size;” (iii) [i]mmediately and automatically cancels any unexecuted portion of an order marked as immediate-or-cancel without routing the order elsewhere; (iv) [i]mmediately and automatically transmits a response to the sender of an order marked as immediate-or-cancel indicating the action taken with respect to such order; and (v) [i]mmediately and automatically displays information that updates the quotation to reflect any change to its material terms.”

In the Regulation NMS Approval Order, the Commission further articulated the limitations on the concepts of “immediately and automatically.” The Commission wrote, “[t]he term ‘immediate’ precludes any coding of automated systems or other type of *intentional device* that would delay the action taken with respect to a quotation.”<sup>1</sup> BATS believes IEX’s magic shoebox qualifies as an intentional device that delays action with respect to a quotation and, hence, precludes such quotation from being considered an automated quotation under Regulation NMS. However, BATS recognizes that this standard, set 10 years ago, was applied to a market that was not operating in sub-millisecond time frames. As such, BATS supports reconsideration of what it means to be an automated quotation for registered exchanges under Regulation NMS; however, BATS firmly believes it is incumbent on the Commission, in the context of approving IEX’s Form 1 application, to articulate clear standards regarding the precise amount of time an intentional device can delay access to the quotation of a registered exchange and still be considered an automated quotation.

This is a critically important issue because any intentional delay in the access to a protected quotation negatively effects the accuracy of the NBBO and the price discovery process for all market participants, not just the market participant with the delay. Consider the following example:

Assume a single Market Maker has bids for 100 shares at \$10.00 on Exchange A, Exchange B, and Exchange C (300 shares total across 3 exchanges), and the NBBO is \$10.00 (300) x \$10.01 (100). Assume Exchange C has deployed an intentional device to delay access to its quotations and publication of market data by 500 microseconds. Also, assume market conditions change and the Market Maker attempts to adjust his bids on all three exchanges to \$9.99. Exchange A and Exchange B receive the order update request and change the Market Maker’s

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<sup>1</sup> Regulation NMS Approval Order at p. 145; Exchange Act Release No. 51808 (June 9, 2005) (emphasis added).

Bid to \$9.99, and update their market data feeds immediately to reflect the new information. However, the order update sent to Exchange C must go through a 500 microsecond delay before reaching the Exchange C matching engine, and then an additional 500 microsecond delay before the new \$9.99 quote is disseminated to market participants. The 1000 microsecond intentional delay is additive to any normal, non-intentional, system latency.

As a result of the above scenario, the protected NBBO is stale and remains at \$10.00 x \$10.01 instead of \$9.99 x \$10.01, for 1000 microseconds longer than necessary. The impact to market participants of this stale quote are several:

- Participants on other exchanges will not be able to update their contra side offer quote to \$10.00 until the exchanges receive the Exchange C quote update.
- Order routers will be routing sell orders to the Exchange C \$10.00 protected bid for 1000 microseconds with no chance of being executed.
- Midpoint Peg orders will be executed at \$10.005 for 1000 microseconds instead of the true price of \$10.00.
- Other pegged order types will be mispriced and unnecessarily exposed to bad executions for 1000 microseconds.

The above-described problem is really one of degree in the sense that BATS recognizes that some existing exchange systems have natural, or non-intentional, system latencies in excess of IEX's 350 microsecond (700 microseconds round trip) intentional delay. Nonetheless, there is a fundamentally sound market structure principle around the Commission's prior pronouncement that access to automated quotations not be subject to intentional delays – it removes unnatural friction from the marketplace and enables investors and intermediaries to transact at the most accurate prices possible. To the extent the Commission believes there should be some tolerance in the Exchange Act for de minimus intentional delays, BATS respectfully requests that the Commission articulate with specificity the full scope of that tolerance.

### **Unfair and Unreasonably Discriminatory Advantage to the IEX Broker-Dealer**

There is one issue associated with IEX's magic shoebox in the context of the IEX exchange-affiliated routing broker-dealer that BATS objects to. While not referenced in IEX's Form 1 application or rulebook, BATS understands that IEX provides its routing broker-dealer with real-time market data in the form of an execution report from the IEX's private market data feed enabling that broker-dealer to instantaneously update its view of the NBBO and take action on this updated view of the NBBO, while the rest of the IEX members wait 350 additional microseconds to receive that information. This provides a distinct and unfair advantage to IEX's broker-dealer that no other routing broker-dealer has. Consider the following example:

Assume the NBBO in stock XYZ is \$24.10 x \$24.11, with 9,000 shares offered in away markets at \$24.11, and 2,000 shares offered on IEX at \$24.11. If IEX then receives a routable buy order for 8,000 shares, it executes 2,000 shares against its

quote and then updates its offer to \$24.12. IEX instantly reports the 2,000 share execution against its quote through its private market data feed to its affiliated routing broker-dealer, which then updates its view of the NBBO by removing IEX's 2,000 shares from its calculation and instantaneously routes the remainder of the order to the other displayed prices in the market at \$24.11. Meanwhile, other market participants must wait 350 microseconds to discover that IEX executed and exhausted its \$24.11 offer.

Because of the disparate manner in which IEX is disseminating its market data, it is providing a distinct unfair and unreasonably discriminatory advantage to its exchange-affiliated broker-dealer that cannot be replicated by any other broker-dealer, including the future member broker-dealers of the IEX registered exchange. As a result of this IEX-only private data feed, (i) other broker-dealers will be routing to IEX's now stale quote; and (ii) the IEX broker-dealer will have an exclusive routing speed advantage over all other broker-dealer members of the IEX exchange.

BATS believes this feature of the IEX's system, unless provided to all broker-dealers, provides an unfair and unreasonably discriminatory advantage to its affiliated broker-dealer that cannot be considered consistent with the Exchange Act. While discriminating among broker-dealers and others with respect to access to information may be acceptable when engaged in by an ATS dark pool, it fails to adhere to the higher standards registered exchanges are held to under Section 6 of the Exchange Act, including requirements to "promote just and equitable principles of trade", "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 "permit unfair discrimination between customers, issuers, brokers, or dealers," as well as distribute market data on terms that are not unreasonably discriminatory in compliance with Rule 603 under Regulation NMS. BATS respectfully requests that the Commission require IEX to amend its Form 1 application to remove this unfair and unreasonably discriminatory advantage.

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BATS appreciates the opportunity to comment on IEX's Form 1 application. As discussed above, BATS applauds IEX for agreeing to adhere to the higher standards applied to registered exchanges than those applied to ATSS, and BATS believes IEX should be granted registration as a national securities exchange. BATS believes that in doing so, it is incumbent on the Commission to articulate clear standards regarding the amount of intentional delay a registered exchange can implement to accessing its quotation that would allow such quotation to be consider automated under Regulation NMS. BATS further believes that as currently configured, IEX is providing an unfair and unreasonably discriminatory advantage to its affiliated broker-dealer in the form of real-time transaction reports from its private market data feed that is delayed to the rest of the industry, and that while that may be acceptable while IEX is an ATS, that feature of the IEX system must be remediated as a condition to granting IEX's Form 1 application for registration as a national securities exchange. Please feel free to contact me at (913) 815-7000 if you have any questions related to this matter.

Sincerely,



Eric Swanson  
EVP and General Counsel

Cc: Mary Jo White, Chair  
Luis Aguilar, Commissioner  
Michael Piwowar, Commissioner  
Kara Stein, Commissioner  
Stephen Luparello, Director, Division of Trading & Markets  
Gray Goldsholle, Deputy Director, Division of Trading & Markets  
David Shillman, Associate Director, Division of Trading & Markets  
Dan Gray, Senior Special Counsel, Division of Trading & Markets