HEALTHY MARKETS
TRANSPARENCY & TRUST

April 1, 2016

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

RE: Release No. 34-77407; File No. S7-03-16

Dear Mr. Fields:

The Healthy Markets Association[1] appreciates the opportunity to comment on the SEC's proposed interpretation of the definition of an automated quotation under Regulation NMS. The SEC has proposed to revise its guidance to redefine "immediate" to explicitly permit "de minimis" delays in "automated quotations" that are under one millisecond.

We are concerned that the SEC's new proposed interpretation would undermine the fairness and efficiency of the markets, introduce significant unnecessary complexities, and create significant risks for investors.

Accordingly, as detailed below, we recommend that the SEC either: (i) decline to revise its interpretation and separately address IEX's application,[2] or, alternatively, (ii) modify its proposed "de minimis" exemption to better reflect its Exchange Act obligations and protect investors.

"De minimis" time delays of less than one millisecond may create risks for markets and investors

We begin our discussion by noting that, when proposing and adopting Reg NMS, the SEC was forced to confront what it meant to be an "automated quotation." At that time, recognizing the evolving nature of the markets, the SEC "specifically sought to avoid 'specifying a specific time

[1]The Healthy Markets Association is an investor-focused non-profit coalition dedicated to educating market participants and the public, and improving the transparency and quality of the US capital markets. Our motto is simple: Informed investors and regulators are essential for healthy capital markets. For more information about Healthy Markets or our work, please see our website at HealthyMarkets.org.

[2] The SEC's existing interpretation of "automated quotation" is not inconsistent with the IEX application, and thus believe no further interpretation is necessary. As Healthy Markets noted in our original comment letter, under the current interpretations, the SEC has permitted geographic distances between current market centers that are either identical to the IEX POP/coil, or orders of magnitude greater. These distances have created delays that are greater than those contemplated by IEX. Nevertheless, the SEC has already accepted that, despite such delays, the quotes are "immediately accessible."

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standard that may become obsolete as systems improve over time'."[3] As a general matter, we agree with that conclusion and approach, and worry that any specified timeframes would likely quickly fall victim to this predictable reality.

As far as process for reviewing time delays, in evaluating an exchange application, the Exchange Act obligates the SEC to affirmatively determine that each element--including a delay--is part of an overall exchange rule set that is "designed 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; and [] not designed to permit unfair discrimination between customers, issuers, brokers, or dealers."[4]

The SEC should determine whether, and under what circumstances, a delay promotes fair and efficient markets, and whether, and under what circumstances, a delay may protect investors. Yet, rather than evaluating the merits of IEX's proposed delay, and its impact on investor protection and the markets, the proposed interpretation would permit all sub-millisecond delays, regardless of how those delays operate, the reasoning and incentives behind the delays, or the impacts on the markets and investors.[5]

An unrestricted, sub-millisecond "de minimis" interpretation would leave the door open for a myriad of time delay and order type combinations,[6] leading to excessive complexity, segmentation, and exchanges selectively advantaging certain groups of clients over others. It would also render the markets more susceptible to manipulation while simultaneously making them more difficult to police.

We have the luxury of observing an example from Canada, which demonstrates that not all speed bumps are the same for investors and markets.[7] In Canada, TMX Alpha created a speed bump

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[3] Proposal, at 9 (quoting Adoption of Regulation NMS, Securities Exchange Act Rel. No. 51808 (June 9, 2005) 70 FR 37496, 37519 (June 29, 2005)). At that time, commenters suggested implementing a definition of one second, while others offered a low as 250 milliseconds. Proposal, at 8.
[4] Securities Exchange Act of 1934, Section 6.
[5] While perhaps not expressly required, we question whether this issue would warrant significant economic analysis. The SEC provides no meaningful analysis of why one-millisecond is an appropriate "de minimis" delay. We see no apparent justification for why one-millisecond is appropriate, while Reg NMS elsewhere uses one second increments, and the threshold is still far-below the threshold for manual intervention. We question whether an interpretation such as the proposed may be consistent with the agency's rulemaking responsibilities, or would be entitled to judicial deference.
[6] See, e.g., Nicole Bullock, *SEC interpretation could lead to IEX copycats*, Financial Times, (Mar. 21, 2016).
[7] While this exact situation may not be permitted under US fair access rules, we believe it is critical for the SEC to make such a determination.

whose design was described in its marketing material as intended "to deliver superior execution quality for natural investors and [to] reduce trading costs for retail and institutional dealers."[8]

ITG studied TMX Alpha, and found some disturbing results. Even though Alpha is not a protected venue,[9] ITG found that "[l]arger orders routing to multiple venues are harmed when they include Alpha in their venue selection."[10] ITG also found it difficult to access the purported quotes on Alpha, a phenomenon often referred to as "quote fading.". The quote fading was so significant that they were able to access "just 44% of the visible liquidity on Alpha. More than half of the Alpha liquidity disappears while our order rests in speed bump purgatory. No timing, gimmick or any other device can prevent this fading."[11] ITG found that Alpha had created "a mechanism for predatory HFT players to identify institutional orders, which are likely to grow, and trade against them."[12] ITG concluded that Alpha "represents a risk free ability to spoof the market and profit elsewhere."

These findings follow logically from the structure of the speed bump, and should serve as a warning to the Commission. None of these problems are a function of the length of the speed bump. Rather, it is the bump in combination with other aspects of the venue that raise concerns with its impact on market integrity and investor protection.

Healthy Markets Recommendations

To better protect investors and promote fair and efficient markets, while also fulfilling its obligations under the Exchange Act, the SEC should evaluate each proposed delay, regardless of its duration, and specifically determine that it is designed and applied in a manner that is consistent with the purposes of the Exchange Act.[13] Many potential delays, including those for under one millisecond in duration, will likely not pass this test.

Further, the SEC should expressly condition any "de minimis" delay upon meeting at least the following conditions:

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[8] See, e.g., Press Release, TMX Group announces regulatory approval of TSX Alpha Exchange model, (Apr. 21, 2015), *available at* **http://www.tmx.com/newsroom/press-releases?id=307**.
[9] Doug Clark, ITG, et al., *Alpha Update - Three Days into the Experiment*, at 6 (2015) (exploring the early results of the trading on TMX Alpha). Further, while these results were based on very limited trading, we understand from the author that a similar analysis performed today would likely yield remarkably similar results.
[10] *Id.*, at 3.
[11] *Id.*, at 3.
[12] *Id.*, at 3.
[13] Specifically, it should be "designed 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; and [] not designed to permit unfair discrimination between customers, issuers, brokers, or dealers." See, Securities Exchange Act of 1934, Section 6.

1. Any response time delays, whether intentional or not, are always less than one millisecond.
2. All intentional response time delays must be applied equally to all participants in their use of the market, and across all order types. Response time delays cannot be altered by any means, including fees. This ensures fair access and just and equitable principles of trade. Time delays should not apply to an exchange's ability to price orders on behalf of all participants (i.e. Pegging).
3. There are no intentional delays in sending data to the Securities Information Processor.
4. The purpose of each intentional response time delay is clearly stated, the delay is expressly intended to benefit long-term investors, and the delay is the simplest means of achieving the stated purpose.

In addition, the SEC should consider the likely different impacts of deterministic or randomized delays on market liquidity, quote accessibility and market integrity. Lastly, because of the evolving nature of the markets and technology, any adopted standard should be reviewed as part of an annual retrospective review to ensure the time period remains appropriate.

Conclusion

The SEC's proposed new guidance could have significant negative ramifications on the markets and investors. If the SEC elects to revise its interpretation of an "automated quotation," we urge it to revise the interpretation as recommended above to better promote fair and efficient markets and protects investors.

Respectfully Submitted,

Dave Lauer[14]
Chairman, Healthy Markets Association

[14] Dave Lauer is the Chairman of the Healthy Markets Association. Mr. Lauer was involved in the early designs of IEX, has a small equity position, and is named in an IEX patent. Mr. Lauer also serves as Independent Director of Aequitas, a Canadian Stock Exchange with an intentional processing delay applied to latency-sensitive traders.