



November 30, 2015

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

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

Dear Mr. Fields:

Citadel LLC ("Citadel")¹ appreciates the opportunity to submit a second comment letter on the Investors' Exchange, LLC ("IEX" or the "Exchange") application for registration as a national securities exchange (the "Application").² We are writing to address three issues that continue to present concern and create confusion for the marketplace, and for retail investors in particular: (1) the need for transparency regarding the operation of the IEX market, (2) the need for the Commission to directly and thoroughly address the irreconcilable conflict between protected quotation status for IEX quotations and Regulation NMS, and (3) the insurmountable advantages that IEX proposes to give its affiliated router.

Citadel Securities is one of the largest market makers in the world, executing approximately one third of all U.S. retail listed stock orders. We care deeply about issues that affect the markets and retail investors in particular. We applaud innovation and market structure improvements, and have been one of the most outspoken advocates for best execution and market safeguards. As a major market participant, we trade on a number of venues, including IEX. We are consistently one of the most active participants on IEX, and on some days the most active participant. Despite this fact, and perhaps because we know the IEX model so well, we feel strongly that the model as proposed does not serve the best interests of investors, is not appropriate for a public exchange, and would create fundamental issues that could ultimately threaten the quality of our equity markets.

¹ Established in 1990, Citadel is a leading global alternative asset manager and market maker. With over 1,500 employees, Citadel serves a diversified client base through its offices in the world's major financial centers, including Chicago, New York, London, Hong Kong, San Francisco, Dallas and Boston. On an average day, Citadel accounts for over 14 percent of U.S. listed equity volume, over 20 percent of U.S. listed equity option volume, and comparable market share in many of the world's leading financial markets.

² Available at <https://www.sec.gov/rules/other/2015/investors-exchange-form-1.htm>.

I. IEX Market Design Should Be Clear and Transparent in the IEX Rulebook

It is critically important that the Commission and the public be fully informed about how IEX will operate, especially given that IEX wants to take the unprecedented step of giving its affiliated routing broker-dealer (the “IEX router”) significant speed advantages over the members that IEX will regulate. For example, the design of the planned IEX access delays, router, and methods of dissemination of market data are not adequately described in the IEX Application. While IEX has stated that it will amend its Application to describe its access delay and router in more detail,³ it is unclear whether IEX plans to amend its Application to fully answer a number of fundamental questions surrounding those items and others about how IEX will operate. Instead, IEX seems content to rest on its assertion that some of these questions are “fully addressed” by the IEX November 13 Letter.⁴ It is further unclear whether any new information that IEX does add to its Application will be incorporated into its rulebook versus some other exhibit in the Application.

Members of the public should not have to hunt for answers to fundamental questions in a comment letter. Nor should they have to try to piece together remote exhibits in an exchange application to understand how IEX operates. They should instead be able to go directly to the current version of the Exchange rulebook.

Although IEX asserts that its structure is far less complicated than that of other exchanges,⁵ most of the new products or services offered by existing exchanges were adopted pursuant to a proposed rule change that included an accompanying explanation of the product or service and a justification for why it is consistent with the Exchange Act. The explanation and justification under the Exchange Act of IEX’s unique features such as its intentional access delay, dissemination of data, and advantages for its router exist only in IEX’s comment letters.⁶ In this way, IEX’s structure is relatively less transparent than other exchanges as the public must guess how IEX will work and assume these unique features are consistent with the Exchange Act without any formal explanation from IEX as to why this may be true.

³ Letter to Brent J. Fields, Secretary, Commission, Sophia Lee, General Counsel, IEX Group, Inc. (November 13, 2015) (the “IEX November 13 Letter”) at 13, 16.

⁴ See IEX November 13 Letter at 18. See also Letter to Brent J. Fields, Secretary, Commission, from Sophia Lee, General Counsel, IEX Group, Inc. (November 23, 2015) (the “IEX November 23 Letter”) at 4.

⁵ IEX November 23 Letter at 8-9.

⁶ IEX has also not made any concerted attempt to comprehensively describe how these features of IEX, and in particular the use of an intentional access delay, will effect the market more broadly in a market structure that requires participants to trade on IEX where it is at the national best bid or offer. Describing these features in the vacuum of IEX’s model ignores the very real problems that arise when an intentional access delay limits a market participant’s ability to seek the liquidity it needs on other markets and appropriately adjust to changes in the marketplace. See *infra* note 11 for further discussion.

Furthermore, as the NYSE Group pointed out in its comment letter, if IEX does not incorporate this important information into the Exchange rulebook, IEX would be able to unilaterally change features of its system without the safeguards of the exchange rule amendment process.⁷ If IEX instead incorporates all of this information into its rulebook, then IEX could not change how it operates without filing a proposed rule change with the Commission so that the Commission can ensure that the proposed change complies with the law, and provide the public with notice and an opportunity to comment. Again, the IEX approach suggests an unwillingness to be transparent and straightforward.

The Commission should not give IEX a blank check to change important features in the darkness of night, and without prior public notice and Commission input. As the IEX November 13 Letter demonstrates, when IEX wants to, it is quite capable of clearly describing how the Exchange will operate. IEX should live up to its marketing claims and be transparent by incorporating all of this information into their rulebook, in plain English.

II. The Commission Should Not Sidestep Important Regulation NMS Issues As IEX Requests

The IEX November 13 Letter urged the Commission to approve the Application without fleshing out any new standards that would determine whether quotations are protected despite use of intentional quotation access delays. As a company that claims to support transparency, IEX should welcome clarity on this fundamental issue. Simply approving the IEX Application and thereby granting IEX protected quotation status despite the undeniably intentional use of a quotation access delay device in contravention of the plain language of Rule 600 and the Regulation NMS Adopting Release⁸ would create substantial regulatory uncertainty and a lack of transparency about one of the cornerstone requirements of Regulation NMS.

For the reasons provided in our prior comment letter, the Commission should not do so.⁹ Such a conclusion simply cannot be reconciled with the language of Regulation NMS requiring that protected quotations be immediately accessible and the Commission's statement that the "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.*"¹⁰

⁷ See Letter to Brent J. Fields, Secretary, Commission, from Elizabeth King, General Counsel & Secretary, NYSE Group, Inc. (November 12, 2015) at 2.

⁸ See 17 CFR 242.600(b)(3) and (57) (defining "automated quotation" and "protected bid or protected offer" respectively); Securities Exchange Act Release No. 51808 (June 9, 2005).

⁹ See Letter to Brent J. Fields, Secretary, Securities and Exchange Commission, from John C. Nagel, Managing Director and Sr. Deputy General Counsel, Citadel LLC (November 6, 2015) at 2-4.

¹⁰ *Id.* (emphasis added). We note that while the IEX November 13 Letter made much of the fact that the device used by IEX to delay access is a physical device, rather than software or some other device, this distinction is irrelevant. An intentional device is an intentional device, regardless of its precise type.

Despite several creative arguments in the IEX November 13 Letter about the spirit of Regulation NMS,¹¹ IEX simply cannot hide from the letter of the law. Determining whether IEX quotations will be protected quotations is straightforward. To make this determination, the Commission only needs to answer three straightforward questions: Is the IEX POP a device, does it delay access to IEX quotations, and does IEX use this device to intentionally delay access to quotations? The answers are clear. The IEX POP is plainly a device that IEX openly admits is designed to intentionally delay access to IEX quotations. IEX quotations are thus not protected quotations as defined in Regulation NMS.

We submit, however, that if the Commission disagrees with our view that giving IEX quotations protected status would harm market quality and is unwarranted, then the appropriate forum for changing the requirements of Regulation NMS is a rulemaking proceeding, not tacit approval of a Form 1 application. Only through a rulemaking proceeding can the Commission thoroughly, adequately, and transparently vet the likely costs and benefits of the intended and many unintended consequences of such an important change to a foundational component of today's equity market structure.

At a bare minimum, if the Commission were to decide to give IEX quotations protected status without amending Regulation NMS, the Commission should at least issue an exemptive order explaining why IEX quotations deserve protected status, and the boundaries of this new authority to intentionally delay access to protected quotations. We agree with Chair White when she explained that she is "wary of prescriptive regulation that attempts to identify an optimal trading speed."¹² The Commission should be equally wary, however, of setting an open-ended precedent without fully vetting the consequences. This would be the result if the Commission

¹¹ For example, IEX argues that other exchanges use an intentional access delay by adjusting the length of their coil to ensure that co-locators have equal latency. However, those other exchanges use relatively small adjustments to the length of coil in order to *facilitate* immediate access to the exchanges' systems and equality amongst those seeking immediate access. In contrast, the intent of IEX's access delay is explicitly to *prevent* immediate access to quotations. Moreover, unlike other exchanges that inform their members of executions as quickly as possible, IEX proposes that execution confirmations would be subject to the same access delay (essentially a separate "dissemination delay"), which will effectively prevent market participants from immediately accessing quotations on other markets in response to what occurs on IEX. For instance, assume a market participant really needs to buy a security for which IEX is at the NBO. The market participant sends an order to IEX, and unfortunately, someone else submitted an order ahead of the market participant and took the NBO. The market participant could then attempt to route to another exchange to access the new NBO, but by the time the message arrives from IEX informing the market participant that there was no execution on IEX, the market participant has been effectively been delayed in accessing the NBO quotation on another market. In an interconnected market system with protected quotations, intentional access delays simply cannot work, which is likely why Regulation NMS specifically prohibited them.

¹² See Mary Jo White, Chair, Commission, *Enhancing our Equity Market Structure*, Speech at the Sandler, O'Neill & Partners, L.P. Global Exchange and Brokerage Conference (June 5, 2014) [available at www.sec.gov/News/Speech/Detail/Speech/1370542004312#.U5HI-fmwJiw](http://www.sec.gov/News/Speech/Detail/Speech/1370542004312#.U5HI-fmwJiw).

sets a precedent potentially indicating that any intentional access delay of less than one second is acceptable for protected quotations.

For example, in the same speech, Chair White explained that she would be receptive to the idea of “frequent batch auctions or other mechanisms designed to minimize speed advantages.”¹³ If the Commission sets a precedent by tacitly approving IEX’s intentional delay and providing IEX with protected quotation status, it would raise numerous questions about protected quotations and batch auctions. Should one assume that a frequent batch auction exchange that intentionally delayed the acceptance of new quotations for a period of 500 microseconds to run the batch auctions would also be considered to have protected quotations? What if it were 500 milliseconds? What about one second? Would it make a difference if the delay is caused by software, coiled fiber, or some other device or method? Must the delay apply to all participants including exchange affiliates? Could the exchange charge different fees for delayed access versus non-delayed access?

III. The IEX Router Would Have Insurmountable Advantages Despite IEX Attempts to Bury This Fact

IEX made a conscious decision not to clearly disclose in its Application the advantages IEX would give its affiliated router. It is ironic that IEX, “the first Alternative Trading System (‘ATS’) to publicly publish its Form ATS, demonstrating its commitment to transparency” would fail to clearly disclose this point, among many others.¹⁴

While the IEX Letters provide important additional information about the IEX routing broker, IEX still attempts to minimize these advantages. IEX asserts that its router will “operate in a manner comparable to the routing logic of other national securities exchanges” and points to The NASDAQ Stock Market LLC’s (“Nasdaq”) routing functionality.¹⁵ This argument ignores a fundamental difference between Nasdaq and IEX: The Nasdaq router does not have an exchange imposed and material speed advantage over Nasdaq participants like the IEX router.

IEX has now clearly disclosed that the IEX router will not have to go through the IEX access delay when instructing the IEX system to post a new order representing the unfilled balance of shares after a route.¹⁶ The following example demonstrates the power of this

¹³ *Id.*

¹⁴ See <http://www.iextrading.com/about/>.

¹⁵ IEX November 13 Letter at 15 (citing Securities Exchange Act Release No. 67639 (August 12, 2012)). See also IEX November 23 Letter at 14.

¹⁶ IEX claims that the IEX router does not have an unfair speed advantage over other members because the IEX router “does not route to IEX.” IEX November 13 Letter at 16; see also IEX November 23 Letter at 14. This claim is misleading. The IEX router will, in fact, send messages to IEX to post the remaining balance of an unfilled order after completion of a route. For all practical purposes, there is no distinction between routing an order to IEX and sending a message to post shares on IEX.

advantage when a participant uses the IEX router speed advantages to get to away markets more quickly after trading on IEX:

Assume the National Best Offer (“NBO”) in a stock is \$10.00, with 1,000 shares offered on away markets at \$10.00, and 1,000 shares offered on IEX at \$10.00. If IEX then receives a routable order to buy 2,000 shares, IEX would execute 1,000 shares against its quote, use the IEX router to simultaneously route the remainder of the order to the other displayed prices in the market at \$10.00, while delaying reports of the execution to the member that traded and other participants that use the IEX direct feed. In this type of scenario, due to the speed advantages of the IEX router, participants could thus use the IEX router to consistently get orders to the away markets before any market participant learns of the initial trade on IEX.¹⁷

Similarly, the following example demonstrates how participants could use the IEX router speed advantages to post on IEX more quickly after trading on away markets:

Assume the NBO in a stock is \$10.00, with 1,000 shares offered on away markets at \$10.00, and IEX is not at the NBO. If IEX then receives a routable and postable order to buy 2,000 shares, IEX would use the IEX router to route the order to away markets and execute against the 1,000 shares displayed, and then post the remaining 1,000 shares to buy on IEX without any access delay, and thus likely at the front of the queue on IEX. In this type of scenario, participants could use the IEX router to consistently get orders posted on IEX at the new price level before any market participant could learn of the initial trades on away markets.

IEX should not be permitted to give its affiliated routing broker-dealer these substantial access advantages over all other IEX participants. This will heavily incentivize and subsidize the use of IEX’s routing broker-dealer to implement substantive trading strategies, when the purpose of an exchange router has thus far been limited, with good reason, to accessing protected quotations on other markets consistent with Regulation NMS.

* * *

There are subtle but important features of the proposed IEX structure that much of the public has not fully appreciated. This is hardly the public’s fault given that they had only 45 days to comment on IEX’s 653 page Application. But what is most troubling is that so many significant details of IEX’s structure have only come to light after prodding by commenters.

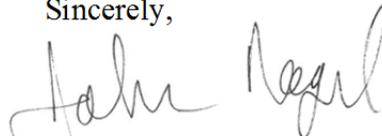
¹⁷ Unlike on Nasdaq where the execution is reported immediately to its direct feed, the SIP, and to the member that submitted the order, IEX will delay the execution report to its direct feed and to the member that traded. Thus, IEX’s access delay would cause an additional delay on top of the natural delay that “any sequential router” would have. IEX November 23 Letter at 16. Contrary to IEX’s assertion, this access delay *would* have a material effect on a sequential router. *Id.*

Regardless of how many times IEX uses the terms “simple” and “transparent” in its marketing, IEX’s proposed structure will harm the “investors” that IEX purports to champion. We urge the Commission to (1) ensure that IEX amends its Application to fully and fairly describe its system and incorporate all material features in its rulebook, and (2) publish the amended Application with a notice and comment period longer than 45 days.

We applaud market innovation that leads to greater efficiency, fairness, liquidity and transparency. We thus support IEX’s conversion from a dark pool to an exchange, but only if it is done in a fair and open manner which supports rather than detracts from the quality of our U.S. equity markets.

Please do not hesitate to contact me with any questions.

Sincerely,



John C. Nagel, Esq.
Managing Director and
Sr. Deputy General Counsel
Citadel LLC

cc: Mary Jo White, Chair
Luis A. Aguilar, Commissioner
Kara M. Stein, Commissioner
Michael S. Piwowar, Commissioner
Stephen Luparello, Director, Division of Trading & Markets