GIBSON DUNN

Gibson, Dunn & Crutcher LLP

1050 Connecticut Avenue, N.W.
Washington, DC 20036-5306
Tel 202.955.8500
www.gibsondunn.com

Amir C. Tayrani
Direct: [redacted]
Fax: +1 [redacted]

May 19, 2016

Brent J. Fields
Secretary
United States Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Notice of Proposed Commission Interpretation Regarding Automated Quotations Under Regulation NMS (File No. S7-03-16); Investors' Exchange LLC—Application for Registration as a National Securities Exchange (File No. 10-222)

Dear Mr. Fields:

Nasdaq, Inc. previously submitted a comment letter expressing support for the Commission's decision to open its proposed Interpretation Regarding Automated Quotations Under Regulation NMS (the "Interpretation") to public comment, but urging the Commission to adopt a different interpretation than the one currently proposed. *See* Comment of Nasdaq, Inc., File No. S7-03-16 (Apr. 14, 2016). Nasdaq has also submitted several comments regarding the application of Investors' Exchange LLC ("IEX") to register as a national securities exchange and has questioned whether IEX's proposed POP/coil—which would impose an intentional delay on quotation response times of 350 microseconds—is consistent with Regulation NMS and the Commission's prior interpretations of that regulation. *See*, *e.g.*, Comment of Nasdaq, Inc., File No. 10-222 (Mar. 16, 2016).

This supplemental letter explains our view that the Commission's proposed Interpretation of the term "immediate[ ]" as permitting an intentional delay of less than one millisecond would conflict with the plain language of Regulation NMS, with the requirements of reasoned decision-making under the Administrative Procedure Act ("APA"), and with the Commission's statutory duty to consider the effect of its actions on efficiency, competition, and capital formation. To avoid these legal pitfalls, the Commission should abandon its proposed Interpretation and reaffirm its existing position that a quotation response is not "immediate[ ]"—and a quotation therefore is not "automated"—if it is subject to any programmed delay. Moreover, in light of Regulation NMS's prohibition on intentional response time delays, the Commission lacks the authority to approve IEX's pending application and to treat IEX's intentionally delayed quotations as protected.

The proposed Interpretation—which would redefine the term "immediate[ ]" in Rule 600(b)(3) for purposes of determining whether a trading center maintains an "automated quotation" subject to order protection—is not a permissible construction of Regulation NMS.[1] The Commission would construe the term "immediate[ ]" "to include response time delays at trading centers that are *de minimis*"—defined as "less than a millisecond"—"whether intentional or not." Securities and Exchange Commission Release No. 34-77407, File No. S7-03-16, Notice of Proposed Commission Interpretation Regarding Automated Quotations Under Regulation NMS, 81 Fed. Reg. 15,660, 15,665 (Mar. 24, 2016) ("Notice of Proposed Interpretation"). The Commission's proposal to sanction *intentional* delays would rewrite Regulation NMS, not interpret it.

"Immediate" is defined as "[o]ccurring without delay" or "instant." *Black's Law Dictionary* 816 (10th ed. 2014); *see also Webster's Third New International Dictionary* 1129 (1976) ("occurring, acting, or accomplishing without loss of time; made or done at once"). Unless a statute or regulation includes "clear modifying language" indicating that the term is to be given a "specialized meaning," this well-settled definition of "immediate" controls. *Consol. Bank, N.A., Hialeah, Fla. v. U.S. Dep't of Treasury*, 118 F.3d 1461, 1464 (11th Cir. 1997). For example, where a federal statute used the term "immediately" without elaboration, an agency regulation that construed the statute as permitting "'deferral' and 'postponement'" was struck down as "inconsistent with congressional language and purpose." *Garcia v. Concannon*, 67 F.3d 256, 259 (9th Cir. 1995). Other courts have likewise concluded that the term "immediate" does not permit delay. *See Greenery Rehab. Grp., Inc. v. Hammon*, 150 F.3d 226, 232 (2d Cir. 1998) (defining "immediate" in a statute as "'occurring . . . without loss of time'") (quoting *Webster's Third New International*

---

[1] Rule 600(b)(3) defines an "automated quotation" as one that:

(i) Permits an incoming order to be marked as immediate-or-cancel;
(ii) Immediately and automatically executes an order marked as immediate-or-cancel against the displayed quotation up to its full size;
(iii) Immediately and automatically cancels any unexecuted portion of an order marked as immediate-or-cancel without routing the order elsewhere;
(iv) Immediately 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) Immediately and automatically displays information that updates the displayed quotation to reflect any change to its material terms.

17 C.F.R. § 242.600(b)(3).

*Dictionary* 1129); *Consol. Bank, N.A.*, 118 F.3d at 1464 (looking to the dictionary definition of "immediately"—"'[w]ithout intermediary; directly' or '[w]ithout delay'"—to determine the term's plain meaning) (quoting *American Heritage Dictionary* 472 (2d college ed. 1982)).

The Commission's proposed Interpretation of "immediate[ ]" in Rule 600(b)(3) would depart from the unambiguous meaning of that term by condoning *intentional* response time delays of up to one millisecond in duration. Indeed, the Commission itself recognized when it first adopted Regulation NMS that the requirement of "immedia[cy]" imposed by Rule 600(b)(3) is incompatible with intentional delays in response time. In promulgating Regulation NMS, the Commission rejected commenters' requests to "specify[ ] a specific time standard" for "immedia[cy]" "that may become obsolete as systems improve over time." Securities and Exchange Commission Release No. 34-51808, File No. S7-10-04, Regulation NMS, 70 Fed. Reg. 37,496, 37,519 (June 29, 2005) ("Regulation NMS Adopting Release"). Instead, the Commission confirmed that the definition of "automated quotation" in Rule 600(b)(3) does "not set forth a specific time standard for responding to an incoming order," and emphasized that "the standard should be 'immediate'—*i.e.*, a trading center's systems should provide the fastest response possible *without any programmed delay*." *Id.* (emphasis added). "The term 'immediate,'" the Commission explained, "precludes any coding of automated systems or other type of intentional device that would delay the action taken with respect to a quotation." *Id.* at 37,534. An intentional response time delay—such as the 350-microsecond delay imposed by the POP/coil that IEX seeks to institute—is flatly inconsistent with the plain meaning of "immediate[ ]" and with the Commission's own understanding that the term requires response times that are as fast as technologically feasible.

To be sure, courts often afford deference to an agency's interpretation of its own regulations, including to reinterpretations of existing provisions. But that deference is hardly boundless and would not shield the proposed Interpretation from judicial scrutiny. Deference to an agency's interpretation of a regulation is not warranted unless "the language of the regulation is ambiguous." *Christensen v. Harris Cty.*, 529 U.S. 576, 588 (2000). This limitation on judicial deference reflects the fact that courts will not defer to an interpretation that is "plainly erroneous or inconsistent with the regulation." *Auer v. Robbins*, 519 U.S. 452, 461 (1997) (internal quotation marks omitted). Where "the text of a regulation is unambiguous, a conflicting agency interpretation . . . will *necessarily* be plainly erroneous or inconsistent with the regulation." *Chase Bank USA, N.A. v. McCoy*, 562 U.S. 195, 211 (2011) (emphasis added; internal quotation marks omitted).

As explained above, the term "immediate[ ]" in Rule 600(b)(3) unambiguously forecloses intentional, planned delay. A court would therefore afford no deference to the

Commission's construction of Rule 600(b)(3) as permitting intentional delays of less than one millisecond. *See Perez v. Mortg. Bankers Ass'n*, 135 S. Ct. 1199, 1208 (2015) (holding that an agency interpretation is "substantively invalid" where it "conflict[s] with the text of the regulation the agency purported to interpret"); *In re Sealed Case*, 237 F.3d 657, 667 (D.C. Cir. 2001) (rejecting agency interpretation where regulation was "unambiguous" because its "plain meaning . . . controls our decision"). In fact, deference to the proposed Interpretation would be particularly inappropriate because it conflicts not only with the unambiguous meaning of "immediate[ ]" but also with the Commission's own prior interpretation of Rule 600(b)(3) issued contemporaneously with Regulation NMS. *See Christopher v. SmithKline Beecham Corp.*, 132 S. Ct. 2156, 2166 (2012) (explaining that deference may be unwarranted where "the agency's interpretation conflicts with [the agency's] prior interpretation").[2]

In addition, the proposed Interpretation would be unlikely to survive judicial scrutiny because this de facto rewriting of Rule 600(b)(3) would impermissibly circumvent the Commission's statutory obligation to consider whether changes to Regulation NMS are justified on the basis of cost-benefit considerations. As the Commission acknowledged when it adopted Regulation NMS, Sections 3(f) and 23(a)(2) of the Exchange Act required it to consider the effects of Regulation NMS on efficiency, competition, and capital formation before promulgating those rules. *See* Regulation NMS Adopting Release, 70 Fed. Reg. at 37,594 (citing 15 U.S.C. §§ 78c(f), 78w(a)(2)). Any amendment of Regulation NMS—including deleting the term "immediate[ ]" in Rule 600(b)(3) or adding an exception for *de minimis* intentional delays—would trigger the Commission's statutory obligation to "assess the economic effects" of a rule. *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir.

---

[2] Furthermore, Rule 600(b)(3) is not amenable to a *de minimis* exception because an agency's "authority to create [*de minimis*] exceptions does not extend to a situation where the regulatory function does provide benefits, in the sense of furthering regulatory objectives"; rather, "situations covered by a *de minimis* exception must be truly *de minimis*" and thus be limited to "situations where the burdens of regulation yield a gain of trivial or no value." *Shays v. FEC*, 414 F.3d 76, 113-14 (D.C. Cir. 2005) (internal quotation marks omitted). Because Rule 600(b)(3)'s prohibition on planned response delays has *significant* benefits for investors, *see*, *e.g.*, Comment of Nasdaq, Inc., SEC File No. 10-222 (Nov. 10, 2015), there is no room for a *de minimis* exception to that rule. *See Am. Fed'n of Gov't Employees v. Fed. Labor Relations Auth.*, 446 F.3d 162, 165 (D.C. Cir. 2006) (holding that an agency's interpretation of a statute to allow a *de minimis* exception was appropriate "not because [regulated parties] ha[d] a 'right' to" one, but because a *de minimis* action had no "appreciable effect" on the conditions the statute regulated).

2011). Accomplishing the same outcome *indirectly* by adopting a purported "interpretation" of Regulation NMS that is in fact a substantive amendment to the regulation would represent an impermissible end-run around these statutory requirements and undermine Congress's effort to ensure that the Commission's regulations advance the public interest and the goals of the Exchange Act. *See Christensen*, 529 U.S. at 588 (holding that deference to an agency's interpretation of its own regulation is unwarranted where "defer[ring] to the agency's position would be to permit the agency, under the guise of interpreting a regulation, to create *de facto* a new regulation").

The Commission's obligation to consider efficiency, competition, and capital formation before authorizing intentional response time delays is underscored by the fact that the Commission has proposed its reinterpretation of Rule 600(b)(3) to further what it believes may be programmatic and policy benefits. According to the proposed Interpretation, permitting these purposeful delays may result in "more flexibility for trading centers . . . to allow them to develop innovative business models," Notice of Proposed Interpretation, 81 Fed. Reg. at 15,661, and "could encourage innovative ways to address market structure issues," *id.* at 15,665. These are precisely the sort of programmatic assessments and objectives that must be evaluated for their effects on efficiency, competition, and capital formation. The Commission may not circumvent that duty by characterizing its de facto amendment of Regulation NMS as a mere interpretive change.[3]

The Commission should therefore abandon the proposed Interpretation and reaffirm that the plain language of Rule 600(b)(3) prohibits intentional response time delays. In addition, the Commission lacks the authority to approve the IEX application and treat its quotations as protected because Regulation NMS and the Commission's existing interpretations of that provision unambiguously foreclose treating intentionally delayed quotations as automated quotations.[4]

---

[3] Such an analysis of effects on efficiency, competition, and capital formation would, of course, be subject to notice and comment. At a minimum, therefore, the Commission could not proceed further without conducting that analysis and making its assessment available for public review and comment. *See Chamber of Commerce v. SEC*, 443 F.3d 890, 894 (D.C. Cir. 2006) (vacating a rule where the Commission "rel[ied] on materials not in the rulemaking record without affording an opportunity for public comment").

[4] Nasdaq would have standing to challenge any Commission decision that adopted the proposed Interpretation or granted IEX's application without amending Regulation NMS itself. Nasdaq would "suffer [an] injury in fact" if the Commission "lift[ed] regulatory restrictions on [its] competitors or otherwise allow[ed] increased competition against"

*(Cont'd on next page)*

Moreover, even if the proposed Interpretation were a reasonable construction of Regulation NMS, the Commission's endorsement of intentional response time delays would still be arbitrary and capricious in violation of the APA. Like other types of agency action, interpretive rules—which include provisions, such as the proposed Interpretation, that "are issued . . . to advise the public of the agency's construction of [its] . . . rules," *Perez*, 135 S. Ct. at 1204—must satisfy the APA's standards for reasoned decision-making. *See*, *e.g.*, *id.* at 1209 ("The APA contains a variety of constraints on agency decisionmaking"—including "an agency's decision to issue an interpretive rule"—with "the arbitrary and capricious standard being among the most notable"). An agency acts arbitrarily and capriciously where it "rel[ies] on factors which Congress has not intended it to consider, entirely fail[s] to consider an important aspect of the problem, [or] offer[s] an explanation for its decision that runs counter to the evidence before the agency." *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). The APA requires an agency to provide an even "more substantial justification" for its action where it changes course from a prior position and "its new policy rests upon factual findings that contradict those which underlay its prior policy." *Perez*, 135 S. Ct. at 1209 (quoting *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009)). Similarly, when an agency's prior policy has engendered "serious reliance interests," "[i]t would be arbitrary and capricious to ignore such matters." *Id.* (quoting *Fox*, 556 U.S. at 515).

The proposed Interpretation could not satisfy these APA requirements. Allowing an exchange-imposed, intentional response delay for protected quotations would be inconsistent with the policies that animate the Exchange Act and the national market system—including equal treatment for investors and uniform rules providing fair access to the national exchanges—as well as with the Commission's own reasoning when it adopted Regulation NMS. *See* Regulation NMS Adopting Release, 70 Fed. Reg. at 37,497 (Regulation NMS promotes the Exchange Act's objectives of "efficient, competitive, fair, and orderly markets that are in the public interest and protect investors"); *id.* at 37,501 (Commission rules protecting automated quotations "promote[ ] equal regulation and fair competition among markets"); *id.* at 37,518 (justifying automated quotation rules based on the need to avoid "undue delays in the routing of investor orders").

---

*(Cont'd from previous page)*

Nasdaq, *Sherley v. Sebelius*, 610 F.3d 69, 72 (D.C. Cir. 2010) (internal quotation marks omitted), and IEX's proposed "speedbump" would also directly impede the operation of Nasdaq's own exchange by impairing its ability to route to a firm quote and undermining certainty about market data from IEX.

As Nasdaq has already explained at length in its previous comments regarding the proposed Interpretation and IEX's pending registration application, permitting the intentional delay of quotations is impossible to reconcile with these policy goals:

- Where outgoing data are subject to delay, data disseminated may not accurately reflect the state of a quotation, "resulting in confusion regarding the availability of liquidity at the venue," which would likely increase the incidence of "locked and crossed markets." Comment of Nasdaq, Inc., SEC File No. 10-222, at 3 (Nov. 10, 2015); *see also* Comment of Nasdaq, Inc., SEC File No. 10-222, at 3 (Jan. 29, 2016) (same).

- Artificial delays in response times for protected quotations decrease the "informational value of transaction reports"—one of the "main component[s] of market data" on which investors rely—and thereby "contradict and undermine" the purpose and value of "protecting" a quotation in the first place. Comment of Nasdaq, Inc., File No. 27-03-16, at 2 (Apr. 14, 2016).

- Permitting artificial delays would "dramatically elevat[e] the complexity of an already complicated ecosystem," creating a market with up to 1000 permitted variations in delays and available order types. *Id.* at 4.

- There is no evidence of a need for a *de minimis* exception or that planned delays will benefit investors in any meaningful way. *Id.* at 5.

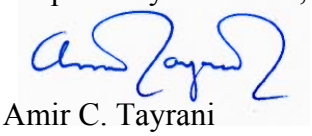
As these and other considerations discussed in Nasdaq's previous comments illustrate, the factual underpinnings of the Commission's original interpretation of Rule 600(b)(3) have not changed, and the industry and investors have developed substantial reliance interests on that interpretation since Regulation NMS went into effect.

Nasdaq is far from alone in expressing these concerns about the proposed Interpretation. Nasdaq's comments are consistent with an overwhelming number of the comments submitted regarding the proposed Interpretation and the IEX application, which provide substantial evidence that the Commission's proposal to allow intentional response delays would undermine the objectives of the national market system. *See*, *e.g.*, Comment of NYSE Group, SEC Release Nos. 34-77406, 77407, at 2, 9 (Apr. 18, 2016) (urging the Commission not to adopt the proposed Interpretation because it would "be a deliberate step towards even more market-wide complexity and fragmentation," which "does not promote investor confidence," and because "market quality will suffer from the introduction of a delay"). Abandoning the Commission's interpretation of Rule 600(b)(3) in the face of these

considerations would be arbitrary and capricious, *see Perez*, 135 S. Ct. at 1209, and "run[ ] counter to the evidence before the agency," *State Farm*, 463 U.S. at 43.[5]

For all of these reasons, Nasdaq urges the Commission not to depart from its existing interpretation of Regulation NMS by authorizing artificially delayed response times for protected quotations, and further submits that the Commission lacks the authority to approve IEX's application and to treat its intentionally delayed quotations as protected.

Respectfully submitted,



Amir C. Tayrani

cc: The Honorable Mary Jo White, Chair
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner
Stephen Luparello, Director, Division of Trading & Markets
Anne K. Small, General Counsel, Office of the General Counsel
Eugene Scalia, Gibson, Dunn & Crutcher LLP

[5] It would be especially problematic if the Commission approved IEX's proposed POP/coil but did not permit Nasdaq and other exchanges to implement similar measures. IEX has no right to preferential treatment by the Commission. *See*, *e.g.*, *Cty. of Los Angeles v. Shalala*, 192 F.3d 1005, 1022 (D.C. Cir. 1999) ("A long line of precedent has established that an agency action is arbitrary when the agency offer[s] insufficient reasons for treating similar situations differently") (internal quotation marks omitted). IEX's competitors would have standing to challenge any such discriminatory decision with respect to the implementation of "speedbumps" as well as any other Commission action that afforded IEX an unfair competitive advantage over other market participants. *See*, *e.g.*, Comment of IEX Group, Inc., SEC Release No. 34-77441 (Apr. 15, 2016) (opposing a proposal from NYSE Arca, Inc. to copy the "Discretionary Peg Order" that IEX included in its own application).