NASDAQ Opening Statement

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Equity Market Structure Advisory Committee

Market Quality Subcommittee Panel

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Good morning members of the Commission, staff, Committee and my fellow panelists. It is an honor to be here today to represent Nasdaq. I am the head of market regulation for our eleven trading venues in the United States and Canada. I have had the privilege of being involved in the securities industry for twenty-five years. It actually goes back further if I could be allowed one personal story. My father, a former stock broker, taught me how to read the newspaper stock tables and let me to buy a few shares in a company I picked on my own. Now in my case that stock was Pan Am, which went bankrupt soon after. This is probably why I became a lawyer and not an investment advisor, but the story is a reminder of the key role markets play in the lives of every American young or old.

Nasdaq has always viewed our highest priority to be operating well-regulated markets that serve the needs of investors, market participants and our 3,700 listed companies around the globe that contribute so much to the growth of the world economy. We've been a leader in real-time surveillance of equities markets, giving us a unique perspective on the operation of our complex and interconnected marketplace. It is from this perspective that we join you today to discuss the recommendations of the Market Quality Subcommittee.

As we've stressed on previous panels, there can be no doubt of the need to reassess U.S. markets to ensure that they continue to provide accurate price discovery coupled with efficient and effective trade executions, to serve the needs of the broader economy.

The subcommittee's recommendations are tentative steps in this direction—focused on market disruptions. Indeed, since the 2010 Flash Crash, the Commission and the self-regulatory organizations, with substantial input from the industry, have adopted a number of safeguards, including first single stock circuit breakers, then Limit Up-Limit Down; Regulation SHO circuit breakers; and updated market-wide circuit breakers. Yet the disruptions on August 24, 2015 demonstrated that further modifications are needed. Many stocks had downward corrections before recovering or unnecessary Limit Up-Limit Down halts while other stocks did not open on time on their primary listing market.

Nasdaq, as chair of the committee administering the National Market System Plan to Address Extraordinary Market Volatility, took a leading role in coordinating input from market participants to address these concerns. This culminated in implementation within three months after SEC approval of the proposal, of a plan to reduce the number of Limit Up-Limit Down halts triggered around the open. The change established a new initial reference price in the event the primary exchange opens without a trade, as is sometimes the case with smaller issuers without enough order activity to trigger an auction. The new reference price is based on the closing price on the primary listing market, rather than potentially less reliable opening quoting activity. It's still early days, but in the first week under the new reference price, Limit Up-Limit Down halts dropped by approximately 75% for securities listed on the two major listing exchange groups.

The work will not stop there. Exchanges have begun implementing a change to activate Limit Up-Limit Down protection immediately after a security emerges from a trading pause, eliminating the risk of a gap in protection. Participants in the plan are also looking at harmonizing clearly erroneous executions with the Limit Up-Limit Down bands, which is consistent with one of the subcommittee's recommendations, and standardizing the resumption process from trading pauses. Indeed, these market structure changes highlight the valuable role played by national market system plans in fostering collaboration among the exchanges and market participants and allowing experimentation in a more flexible way than would be the case by relying solely on SEC rulemaking. We thank the Commission for supporting this process.

While we have not had sufficient time to fully assess the subcommittee's recommendation to eliminate trading halts in favor of "pre-open" states, we welcome this idea as an additional option for consideration in this important market structure debate. Before adoption of this recommendation it will be critical to understand how the resumption in trading would work to ensure uncertainty and volatility are not exacerbated. Considerable testing and input from market participants are essential for any changes.

The Nasdaq listing exchange processes all opening auctions immediately at 9:30 a.m., and we strongly agree with the subcommittee's recommendation that all stocks listed on US exchanges open as close to 9:30 a.m. as technically possible. August 24th illustrated the risks when underlying securities do not open on time on the primary listing market, impacting users who rely on data from the primary market and making it difficult to assess the value of individual companies and the market as a whole. This can also impact derivative products including exchange traded products on which many retail investors rely. While steps have been taken to reduce this problem, trading on the day after Britain's vote to leave the European Union indicates that this problem persists. As we argued recently in another context, while participants benefit from choice in market models, those models should not impede overall market efficiency and price discovery.

The subcommittee's comments on market-wide circuit breakers also merit attention. Circuit breakers remind me of oxygen masks on an airplane, comforting to know they exist, but likely to cause panic when deployed. The subcommittee is right to recommend review in light of recent experience to ensure that they only deploy when needed. Although we are still reviewing the subcommittee's recommendation regarding the reference index, we have some initial concerns about the use of S&P futures contracts as the measure because these instruments insert a potential risk of contagion since they represent a different asset class than equities.

One note of strong dissent, Nasdaq is disappointed with the subcommittee's unwillingness to consider recommendations on ways to improve the trading of small and mid-cap companies. It appears from the recommendations that, while the subcommittee solicited feedback from the trading and investment community, it never actually asked smaller issuers for feedback. If this is correct, the subcommittee ignored the community most familiar with the problem. As we've previously stated, the one-size fits all market structure we suffer with today has not served these issuers and their investors well and puts the capital formation engine of our country at risk. In fact, Congress has focused most of its review of market structure in the context of the needs of small companies, and this Committee owes these companies a similar focus.

As the listing venue of choice for many emerging growth companies, Nasdaq believes there are indeed solutions that can improve the market for emerging growth companies, or "EGC"s. These include:

1) Reducing fragmentation in EGCs by limiting or eliminating unlisted trading privileges to create a single center of liquidity where the vast majority of supply and demand can meet.
2) Related to the previous proposal, allowing directed orders in EGCs so brokers can ensure the execution quality experience of their customers.
3) Considering order delivery for EGCs to reduce the risk associated with posting quotes and orders across multiple markets. In other words, relaxing auto-execution where necessary to encourage market participants to post more marketable volume.

On a broader level, Nasdaq encourages the subcommittee—and the Commission—to accelerate its consideration of the wide range of market structure issues before us. We need to find a faster way to experiment with and ultimately implement needed changes. The UK's Financial Conduct Authority recently announced that it will encourage product innovation through its "regulatory sandbox" initiative and we think this concept could be extended to market structure initiatives. We've also advocated using market simulations to expedite consideration of some proposals.

It is through the audacity to challenge the market structure status quo that we will ensure that the benefits of equity ownership are clear to the next generation of young investors seeking to put their savings into the market.

I thank the Commission, the staff and the Committee for their time and I look forward to a fruitful discussion of these important issues.