December 19, 2014

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Proposed national market system ("NMS") Plan to Implement a Tick Size Pilot Program ("Plan"); File No. 4-657

Dear Mr. Fields,

The Security Traders Association ("STA")[1] offers comment on the national market system plan ("Plan") to implement a targeted 12-month pilot program that will widen minimum quoting and trading increments ("tick sizes") for certain stocks with smaller capitalization. This Plan was filed on November 3, 2014 in response to the June 24, 2014 Securities and Exchange Commission ("Commission") order directing the Exchanges and the Financial Industry Regulatory Authority to submit a tick size pilot plan (Release No. 34-72460). Data gathered from the Plan will enable the Commission to study the impact of wider quoting and trading increments on the trading of certain small capitalization stocks.

The STA's unique and focused comments on issues related to market structure come from our roles as practitioners in the markets. STA membership does not represent any specific business model, but rather encompasses a broad range of industry participants. It is from this broad based membership that STA seeks to build bottom-up consensus regarding issues that relate directly to the U.S. securities markets.

Background and General Beliefs

STA believes that the majority of publicly traded companies have reasonable or ample liquidity with narrow spreads, low transaction costs, opportunities for price improvement and certainty of execution, which are all benefits that accrue to investors.

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[1] STA is a trade organization founded in 1934 for individual professionals in the securities industry. STA is comprised of 26 Affiliate organizations with 4,200 individual professionals- most of who are engaged in the buying, selling and trading of securities. The STA is committed to promoting goodwill and fostering high standards of integrity in accord with the Association's founding principle, **Dictum Meum Pactum** – *"My Word is My Bond"*.

The subject of decimalization with no minimum price variation ("MPV's") and its impact on overall liquidity and capital formation is a topic on which the STA has commented on in the past[1]. We believe that strong secondary trading markets are essential to private capital formation because investors are less likely to participate in initial public offerings without a reasonable expectation that an active secondary trading market will develop for the securities thereafter. In addition, companies rely on strong secondary markets to raise additional capital through secondary offerings. STA believes that introducing MPVs could help with the overall amounts of liquidity available in smaller companies; therefore, we continue to recommend a Pilot be conducted.

In a letter to the Commission, dated April 30, 2013[2] STA wrote:

> *We as an industry association with a diverse membership as measured by geography and business model believe there is broad consensus that today's market structure does not serve emerging growth companies or their potential investors well and that pilot study should be conducted. To be clear, the debate among our committees and Board is strictly limited to "how" a pilot study should be conducted. The question of "should" a pilot study be conducted has universal support.*

STA gathered input from our Board of Governors, four (4) trading issue committees and affiliate presidents that represent a broad section of investors and their agents. These committees are:

- Institutional Advisory Committee, which is comprised of traders from asset managers;
- Market Structure Analyst Committee;
- Retail Advisory Committee, which is comprised of the agents for retail investors; and
- Listed Options Committee, which is comprised of market makers, agents and exchange representatives.

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[1] STA Comment Letter to Elizabeth Murphy; September 23, 2014, available at: http://www.securitytraders.org/wp-content/uploads/2014/09/TickSizeFINAL.pdf.
STA Comment Letter; "Tick size study mandated by the Jumpstart our Business Startup Act of 2012" July 16, 2012, available at: http://www.securitytraders.org/wp-content/uploads/2011/02/TickStudyFinal.pdf.
STA Comment Letter to SEC Small Business Advisory Committee, April 30, 2013 , available at: http://www.securitytraders.org/wp-content/uploads/2013/04/FinalLetter.pdf.
STA Letter to Chairman Schapiro; November 20, 2012, available at: http://www.securitytraders.org/wp-content/uploads/2014/04/SchapiroFinal.pdf
Testimony before Capital Markets & Government Sponsored Enterprise Subcommittee, Committee on Financial Services U.S. House of Representatives; June 20, 2012, available at: http://financialservices.house.gov/uploadedfiles/hhrg-112-ba16-wstate-jtoes-20120620.pdf.

[2] STA Comment Letter to Elizabeth Murphy; Re; SEC Small Business Advisory Committee; April 30, 2013, available at: http://www.securitytraders.org/wp-content/uploads/2013/04/FinalLetter.pdf.

In addition, the STA relied on data provided by SEC Staff in its report titled; "A characterization of market quality for small cap capitalization US equities" published September 2014 by Charles Collver[3]. The report studied characterizations of:

> *….some aspects of market quality for small and mid capitalization stocks during 2013. First, it tabulates some widely-used summary market quality measures such as quoted and effective spreads and trading volume. Then it describes the aggregate displayed depth of the limit order book for these stocks.*

While the views represented in this letter are consistent with past comments STA has provided on the subject of tick sizes for companies with small capitalizations, we highlight one revision.

In our letter to the Commission dated July 16, 2012, STA wrote:

> *STA recommends the Commission initiate a pilot program utilizing a statistically significant number of emerging growth companies and an appropriate period of time to study the impact on the secondary markets of **quoting** MPVs ("Minimum Price Variations", aka "Tick Sizes") in increments of greater than one penny.*

Many of the characteristics of what we recommended in our July 12, 2012 letter are found in the Plan within Test Group One.

STA is revising our recommendation that in addition to an MPV of $0.05 for quoting, companies in the pilot be allowed to trade in $0.005 increments. STA believes that one pilot test group strikes a proper balance between complexity and costs, with an efficient design that yields robust data.

Recommendations Regarding the Plan

STA recommends that the Commission implement a pilot plan which would provide empirical data on the effects decimalization with no minimum price variations has had on the overall liquidity available to investors in companies with small capitalizations. STA understands the complexities of designing, implementing and studying such a plan. Therefore we offer both guiding principles and detailed recommendations in this letter.

Guiding Principles

- The Plan should balance costs and benefits in its design with creating the conditions which allow the variables to be tested efficiently.
- There should be one clearly defined primary goal for the plan. All other goals should be prioritized accordingly or omitted if they pose a conflict or risk to achieving the primary goal.
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[3] SEC Staff Report by Charles Collver – September 2014, available at: http://www.sec.gov/marketstructure/research/small_cap_liquidity.pdf.

- Securities with reasonable or ample liquidity which are trading efficiently in today's market structure should not be included in the Plan's Selection group.
- Terms and conditions of the Plan should apply to all market participants. Highly efficient markets allow investors of all types and their agents to interact with each other.
- The Plan needs to allow for two features, which all investors find meaningful when investing in companies, regardless of their capitalization: opportunity for price improvement and mid-point trading.
- Data which does not contribute towards measuring improvements or degradations of the primary goal should not be mandated.
- Insight into the Commission's response from specific results should be provided in the Plan's final design. Providing such information will enable Participants to understand what Commission defines as a positive or negative result in the data.

Detailed Recommendations

Primary goal should be improving overall liquidity available to investors.

STA continues to believe the primary goal of the Plan should be collecting data which measures overall liquidity, both natural and enhanced, available to investors in small capitalization stocks.

Natural liquidity, simply defined, is liquidity provided by investors and traded through publicly lit and privately unlit markets. Enhanced liquidity is liquidity that exceeds what is publicly and privately available in the market place. Enhanced liquidity could be the result of certain behavior by a sub-category of trading centers that commit capital and conduct secondary offerings or institutional block trades.

It is reasonable for the Plan to gather data for more than one purpose or goal. However, secondary goals should be clearly defined and prioritized. Doing so will ensure variables which may achieve data for secondary goals, but conflict with the primary goal are not implemented into the final design.

Data used for measuring improvements and degradations.

There are some widely used market quantitative measures that when used in conjunction would be effective in measuring improvements and degradations in overall liquidity available to investors:

- ***Publicly available float*.** Strong correlations exist between a company's publicly available float and the amount of liquidity available to investors. Companies with large publicly available floats tend to be more liquid. We recommend that changes in the amounts of publicly available floats as measured by shares be measured in the Pilot.

- ***Share turnover versus float ratio.*** Such a measure of stock liquidity is calculated by dividing the total number of shares traded over a period of time by the average number of shares outstanding (publicly available float) for the period. The ratio helps put a company's share volume in perspective as it relates to the company's available float.
- ***Quoted and effective spreads.***
- ***Overall Trading volume; both share and dollar.***
- ***Aggregate displayed depth of the limit order book***.
- ***Volatility.*** Providers of enhanced liquidity are more inclined to commit capital and more able to conduct block trading if the prices of the security the provider transacts in remains stable.

STA believes gathering data in these categories would provide the Commission robust data for measuring improvements and degradations in overall liquidity available. It is important to note that none of these measurements should be used alone to draw conclusions.

The above six (6) categories of data can be obtained by the Commission via its Market Information Data and Analytics System, "MIDAS". Requesting Participants in the Plan to provide this data would be duplicative and unnecessarily increase the costs of the Pilot.

Criteria in selection of Pilot Securities for Inclusion in the Tick Size Pilot Program

STA recommends additional liquidity measurement as criteria in the selection process.

The criteria for the selection group in the Plan is closely aligned with criteria used for determining the sample group which the SEC Staff studied in its report published September 2014.

The SEC Staff[4] report stated that using such criteria:

> *Stocks are included in the daily sample if the closing price…is greater than or equal to $2.00 and the market capitalization is less than $5 Billion. On average, there are 2,814 stocks in the sample during a typical trading day in 2013.*

It is STA's view that there is reasonable or ample liquidity and efficient trading in a subsector of securities that meet the selection criteria defined in the Plan and therefore including these securities is unnecessary. We recommend the Commission add additional criteria which measure liquidity to identify those securities. STA believes that adding an annualized share turnover versus float ratio measurement as additional criteria would be effective in achieving this goal. For comparison purposes, STA performed annualized share turnover versus float measurements for certain categories of NMS securities. The annualized ratios are for 2014:

- The largest 500 NMS securities as measured by market capitalization – 2.10x

[4] Ibid

- The largest 500 NMS securities as measured by publicly available float – 2.35x
- 1,900 securities in the Russell 2000 Index – 1.11x

STA recommends the Commission consider this criterion and determine a ratio which serves as a threshold for determining reasonable and ample liquidity.

Specifically, we recommend that the criteria for determining securities in the selection group of the Plan be NMS securities which have:

- A market capitalization of $5 billion or less on the first day of the Measurement Period;
- A closing price of at least $2 on the first day of the Measurement Period;
- An annualized company share turnover versus its public float ratio as determined by the Commission measured during the Measurement Period.

STA believes these criteria will be successful in identifying those securities which are most illiquid and will justifiably reduce the amount of securities in the selection group. Achieving this result will also reduce potential harm to investors as a consequence of wider spreads and unforeseen negative consequences.

Pilot Test Group

The Plan calls for three (3) simultaneous Test Groups of 400 securities which totals 1,200 companies, or over 40% of the selection group[5]. STA feels this percentage is too high and negates the key benefits of low risk and costs associated with conducting pilots.

STA believes the percentage of Pilot securities chosen to be tested should be the lowest possible rate which yields robust data. STA concludes that the rate should not exceed 25%.

STA Recommendations on the Pilot Design

Based on our aforementioned recommendations for additional criteria which would justifiably reduce the number of securities in the selection group and additional recommendations for determining the levels of securities eligible for testing, STA does not believe there are enough NMS securities to conduct three simultaneous pilots which yield effective data on each test group.

STA recommends one (1) test group categorized and divided equally by the various low, medium and high thresholds on share prices and volumes described in the Plan.

Securities will be quoted in $0.05 minimum increments, but may continue to trade in $0.005 increments. These criteria will allow for meaningful price improvement and mid-point trading for all market participants.

[5] Ibid

STA is interested to see if empirical data gathered from a Pilot with this recommended design shows improvements or degradations to aggregate displayed depth of the limit order book. The STA agrees with a conclusion made in the SEC Staff Report:

> *Depth increases at prices just a few cents away from the midpoint, suggesting that there is more to liquidity than the size posted at the inside spread. But this increase in depth is more apparent in larger stocks.*

However, we also believe that displayed liquidity and confidence that it can be accessed in a fair and reasonable way is critical to improving liquidity for companies with small capitalization.

In our testimony at a Roundtable on U.S. Market Structure hosted by House Capital Markets Subcommittee Chairman Scott Garrett on July 28, 2014 we noted that three (3) factors contribute positively to the existence of enhanced liquidity. One of these factors was:

> ***Quote quality.*** *Improvements to displayed liquidity need to focus on size and ensuring that what is publicly displayed is accessible in a fair and reasonable way.*

STA's opposition to more than more test group is also due to the additional level of programming and operational risk from having multiple test groups. The level of complexity with the "trade-at" provision in Test Group three is most concerning to us. The change in execution logic to facilitate compliance with depth of book price protection is highly complex and we believe this complexity will discourage many market participants from participating in the Plan.

In addition, having one (1) test group of securities versus three (3) groups of 400 each (a total of 1,200 securities) will better protect investors from potentially additional costs as a result of caused by wider spreads.

Implementation

The Plan should be implemented on a one-year pilot basis. It should be applicable during and outside of regular trading hours.

The Commission should assess data and make public its findings from the first six months of the Pilot at a reasonable time thereafter.

Termination of the Pilot

STA believes the Commission needs to strike a balance between flexibility and certainty in a termination process for the Pilot. Achieving such a balance will lower the possibilities of technological risks and costs to the industry for operating in the Pilot regime.

STA recommends the Pilot continue to operate during the Assessment Period described as occurring no later than six months after the end of the Pilot period. STA believes there are unnecessary risks and costs associated with ending the Pilot after twelve months, only to then perhaps re-introduce it after the assessment period. STA views it is equally critical that the Pilot have a defined end date as well. We recommend that absent any decision by the Commission the Pilot end three months after the assessment period.

Conclusion

The STA appreciates the opportunity to comment on the Plan. We also wish to acknowledge and thank the Commission and all the staff responsible for designing the requirements for which the Plan seeks to address.

John Daley
Chairman of the Board

James Toes
President & CEO

Addendum - General Questions-proposed by the Commission

Question*:* What are the anticipated costs for implementing and operating the proposed Pilot? Are any components of the Pilot structure particularly costly? If so, please describe which market participants could be impacted.

Answer:

There are explicit and incremental technology costs for implementing each of the three tests groups. In addition incremental technology costs associated with compliance and data capture will accrue. STA recommends that only data which measures improvements or degradations of the primary goal be mandated and where possible should obtained by the Commission.

Question: Could investors of the small capitalization securities included in the Pilot be harmed by the widening of quoting and trading increments?

Answer:

Investors who initiate either a long (buy) or short (sell) position in a Pilot Test security during the Pilot period should not be harmed because they have reasonable information about the characteristics of the Pilot securities at the time they make their initial investment decision. Investors who are either long or short shares in a Pilot Test security prior to the Pilot beginning could be harmed when they close out that position. These investors may not know which companies are in the Pilot until they decide to close out their position. A way to limit this risk is to limit the number of securities considered eligible for testing. STA recommends that one test group of securities would limit this risk to investors.

Question: Is the proposed one-year Pilot Period too long or too short? Should the Pilot Period be different? Is it appropriate that the proposed Pilot is structured to end before completion of the assessments by the Participants?

Answer:

The twelve (12) month Pilot Period is adequate. As noted in our letter, we strongly recommend that the Pilot continue to operate during the Assessment period, described as six (6) months. Equally as important is a requirement which clearly states an end date. STA believes that absent any decisions by the Commission, the Pilot should end no later than three (3) months after the assessment date ends.

Question: What is the risk of unintended consequences from the Pilot? What might they be?

Answer:

There is risk that one group of securities receives an incremental benefit or harm due to the trading regime created in its respective test group. Unintended consequences could be failures in technology and the ability for the industry to respond to such events, should the events occur in multiple Test Groups.

Question: Will the Pilot lead to changes in trading behavior by market makers or other market participants?
Answer:
STA believes changes in behavior are required in order for improvements to the levels of liquidity to improve. Predicting specific changes in behavior is extremely difficult. STA is interested to see if investors use more non marketable limit orders for buying and selling Pilot securities. A change in this behavior could lead to greater displayed size.

Question: The Participants have proposed to exclude securities that have recently completed an initial public offering from the proposed Pilot. Should these securities be included?
Answer:
STA believes that securities that recently completed an initial public offering experience higher levels of volatility and volume as compared to levels which they experience months later. Therefore we agree that they should not be included in the Pilot as they could potentially skew the data.

Question: Should the proposed Pilot exclude any other small capitalization securities? For example, should small capitalization securities that are cross-listed in another jurisdiction be excluded from the Pilot?
Answer:
Allowing dually crossed-listed securities could result in regulatory arbitrage with meaningful order flow either entering or leaving the U.S. STA believes such an occurrence would skew the data and we therefore recommend dually listed securities should not be included.

Question: Should companies whose securities are included in the Pilot be allowed to **opt-out** of participating in the Pilot? If so, how should such an opt-out work and what impact would it have on the ability of the Commission and others to analyze the Pilot?
Answer:
Allowing companies to opt out could affect the data. Therefore STA recommends that companies not be allowed to opt out during the Pilot Period. STA believes that it is unlikely that any harm to a company in a test group would only be specific to that company. Therefore if harm resulted, ending the Pilot immediately for all companies would be a prudent response from the Commission.

Question: The Commission generally requests comment on the advisability of testing a trade-at requirement as part of the Pilot. Are exceptions to the trade-at requirement set forth in the Order appropriate?
Answer:
Exemption requests should be considered in situations where major enhancements and incremental costs are required to comply with the Plan.
For example:
The NBBO for Pilot Security ABC is $20.00 x $20.10. Trading Center 1 is displaying a 100-share protected bid at $20.00. Trading Center 2 is displaying a 100-share protected bid at $20.00. Trading Center 2 also

has 300 shares hidden at $20.00. There are no other protected bids. Trading Center 2 receives an incoming order to sell for 400 shares. Under the proposal, Trading Center 2 may execute 100 shares against its full displayed size at the protected bid at $20.00. To execute the 300 shares hidden at $20.00, Trading Center 2 must respect the protected bid on Trading Center 1 at $20.00, even though Trading Center 2 can satisfy the entire 400 shares. The change in execution logic for Trading Center to facilitate compliance under the Plan is highly complex. Therefore, STA recommends that passive bids and offers be provided an exemption which allows them to satisfy incoming orders which fill both their displayed and non-displayed prices.

Question: Is market maker profitability data necessary to analyze the effect of the Tick Size Pilot Program and to reach a conclusion about the tradeoffs associated with increasing the quote increment in certain small capitalization securities? Are there better ways to collect such Pilot data?

Answer:

Market Maker profitability does not measure improvements or degradations to liquidity and therefore should not be mandated. In addition, mandating its reporting to any parties would deter participants.