May 21, 2010

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

RE: File No. S7-02-10; Concept Release on Equity Market Structure

Dear Ms. Murphy:

Lime Brokerage LLC[1] ("Lime") welcomes the opportunity to provide comment on the wide range of topics contained in the Concept Release on Equity Market Structure (the "Release"). Lime applauds the Commission for undertaking a reasoned, thoughtful approach to implementing regulatory initiatives that could have a significant impact on the operation, quality and competitiveness of the US Equity markets.

We first address some general topics that are critical to any evaluation of the US Equity market structure. We then comment on some specific areas of the Release on which the Commission has requested feedback.

I. General Topics

A) Core Principals

The Commission restates in the Release the mandated objectives for the national market system as defined by Congress, including efficient execution of transactions, fair competition among markets, price transparency, best execution of investor orders, and the interaction of investor orders when consistent with efficiency and best execution. It also notes that the Commission's mission includes the protection of investors and the facilitation of capital formation. While all of these objectives remain critical components of an effective US Equity market structure, Lime also believes there are additional criteria against which current and proposed market structure should be evaluated.

Lime suggests that the hallmarks of the US Equity market, and key elements of its current vibrancy and efficiency, are principals of fairness, competition and innovation. These principals reflect key attributes of the founding principals of the United States: capitalism, innovation and the "American Dream" of opportunity for each according to ability or achievement. Recent constructs such as Regulation ATS and Regulation NMS have promoted these principals. We urge the Commission, when proposing regulations, to attempt to minimize any impact that would diminish the incentives that currently exist for market participants to innovate around market structures, trading strategies, or operational efficiencies. Finally, Lime urges the commission to

[1] Lime Brokerage LLC is a technologically advanced brokerage firm that caters to a diverse and sophisticated customer base. Lime's clients include professional traders, hedge funds, asset managers and other broker-dealers. Our customers rely on Lime's robust and advanced technology to execute equities transactions on multiple exchanges, ECNs and trading venues.

continue its past practice of not taking a position when crafting regulation as to what market models or trading strategies are subjectively "better" than others.

B) Conflicts of Interest between Proprietary Trading and Client Order Execution

The conflict-of-interest issue we describe here impacts transparency, price discovery and execution quality for long-term investors, and is an area we believe deserves further scrutiny by the Commission. Institutional broker-dealers that operate both proprietary trading operations, either traditional trader-based or automated "dark pools", and handle client orders are faced with a conflict every time they receive and handle a client order. This conflict stems from the best interest of the broker-dealer firm being served by "matching" that trade internally, either against proprietary positions held by the broker-dealer or, more optimally, against an order originating from another client of the broker or against liquidity at a venue that will pay that broker for that order. Execution costs to the broker are significantly lower if an order is internalized instead of routed to an external venue that will charge the broker to access the liquidity resident in that environment.

In order to maximize the potential that a given order will be executed at a preferred cost, many institutional broker-dealers have implemented automated systems that will "flash" an order to multiple internal execution opportunities (proprietary desks, internal dark pools) as well as to select external parties via Indications of Interest. External parties will generally include a select subset of "preferred" clients that the broker-dealer believes may have an interest in a given transaction, as well as external dark liquidity pools.

The result of this practice is that orderflow, often of significant size and therefore price discovery value, is held out of the public information flow for some amount of time (measured in seconds). During the time the order remains hidden from public view, various internal and external execution venues have an interaction opportunity with these orders. Only after the order has failed to match against any of these venues will it find its way into the "lit" market, where it will either execute against resting liquidity, or become part of the price feeds available to the market at large.

Certain aspects of this behavior have been addressed by the Regulation of Non-Public Trading Interest[2] proposal regarding Actionable IOI's. However, Lime believes that additional steps are required beyond requiring the public disclosure of the IOIs that are sent from a broker-dealer to external counterparties. As much of the exposure of an order may occur wholly within the confines of a broker-dealer, it would, even under the proposed rules, remain hidden from the public. We believe what is necessary to address this issue is to provide the originator of orders with sufficient transparency into these practices, and control over how their orders are handled.

Armed with detailed information about exactly how an order is processed by a given broker-dealer, and then provided with the ability to "opt-in" or "opt-out" of interaction with various execution and/or execution points, investors can ensure that orders are handled in a manner they deem will provide them with the "best" possible execution taking all factors into consideration. We believe that this could be partially achieved through expanding Rule 606 reporting to include internal order handling practices; or through a similar type of mechanism. However, given the lag in publication of Rule 606 data, we believe that additional real-time information and control is necessary. One possibility could be the creation of order types or attributes on orders sent to

[2] Securities Exchange Act Release No. 60997 (November 13, 2009), 74 FR 61028 (November 23, 2009).

broker-dealers that would provide the originator of the order with the ability to designate specific instructions on how the order is to be handled.

II. Specific Areas Noted in the Release

A) Market Structure Performance

i) General

The US Equity markets have gone through tremendous change in recent years, most substantially due to the increasing role of technology in every aspect of the trading lifecycle. As noted by James Angel, Lawrence Harris and Chester Spatt in their recent study "Equity Trading in the 21st Century"[3], innovations in these markets have provided individual investors with "better service at a lower cost from financial intermediaries than previously". During the stresses in late 2008 and early 2009, the Equities markets operated effectively and efficiently.

As markets have evolved, they have become increasingly intertwined. Lime believes that any review of US Equity markets must also encompass trading in related asset classes such as Options, OTC Derivatives, and other markets that did not perform as effectively or efficiently as the US Equity markets during the downturn in 2008/9.

Lime believes that while there are certain micro-structural issues that need attention, we do not see large-caliber problems with the equities market structure that would require large-scale modification. We reiterate our concern that "fixing" a market structure that isn't actually broken by implementing additional regulation may stifle innovation and create a "race to the bottom", eliminating the benefits that have been realized by individual and institutional investors alike, and making the US Equity markets uncompetitive versus other global markets.

ii) Metrics

Lime supports efforts to revamp certain execution quality metrics, such as Rules 605 and 606, to better reflect the characteristics of trading in today's automated environment. Increased transparency can only lead to better decisionmaking by investors. Additionally, as described above, investors should have more information regarding the internalization practices of broker-dealers and should have tools at their disposal for controlling the level of exposure of orders to the various proprietary trading operations to which they are often "flashed" in the course of processing.

B) High Frequency Trading

i) General

There is much debate in the industry about what is meant by the term "High Frequency Trading". The reality is that many of the issues discussed around this topic relate to all forms of computer-assisted trading. The use of technology in trading is the natural evolution of our industry and is done in some form by just about every market participant. Investors leveraging computer assistance to trade should not be penalized for their investments in these tools.

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[3] James J. Angel, Lawrence E. Harris, Chester S. Spatt: "Equity Trading in the 21st Century" (February 23, 2010)

Implementing any type of regulation that would limit the tools or the effectiveness of automation available for use by any class of investor in the name of "fairness" would turn back the clock on the US Equity market and undo years of innovation and investment. Lime would strongly oppose suggestions such as minimum order durations prior to cancellation. Similarly, we believe placing limitations on certain behaviors that do not violate any rules but are rather subjectively viewed to be "undesirable" would be a slippery slope and put the Commission in the untenable and unsupportable position of passing judgment on participants' trading strategies.

ii) Co-Location

Co-Location is not a new concept. In the past when stocks were traded manually on the floor of the New York Stock Exchange, member firms invested in seats on the exchange in order to ensure they had physical presence on the floor of the exchange to be closest to where trades were occurring. Today's computerized trading environment has transformed the desire for proximity to the physical location of trading engines as close to the matching engine provided by automated exchanges.

The fact that exchanges today provide broader access to co-location facilities makes the playing field significantly more "level" today than in the days of manual trading. As long as access to these facilities is fair and exchanges do not discriminate in how space is provided, either by pricing or by availability, co-location provides significant benefits to a broad range of market participants. We support the imposition of fair access standards to govern the allocation of co-location space provided by exchanges to ensure that the playing field remains even, taking into consideration that there are finite limits on the space that can be made available.

We also recommend that the concept of "fair access" encompass the quality of access that participants that do not choose to locate equipment within a market center's co-location facility receive when delivering orders to the exchange matching engine. It is vital that market centers not introduce any additional network latency that effectively penalizes members for not locating machines within their facility, through the insertion of additional network switches or other impediments. As an example, if co-located members' orders pass through a single network switch before entering the exchange system, orders submitted by members whose order placement hardware is physically located outside of the co-location facility should also pass only through that single switch.

Suggestions of limiting the capabilities of co-located trading by batching of orders or other restrictions would unduly harm the markets. Batching of orders submitted by co-located trading engines, for example, would effectively turn continuous markets into auction markets – a structure which has proven to be less than desirable by US market participants.[4] Placing affirmative or negative obligations on these participants would place an asymmetric burden on them.

We would also note that if undue burdens are placed on co-location facilities provided by exchanges due to regulation, the market will likely turn instead to private, unregulated entities that can obtain space within close physical proximity to the exchange facilities.

[4] We note the experience of the Arizona Stock Exchange, an auction-based market that failed to gain traction in the US market.

iii) Data Feeds

As a provider of low-latency market data, Lime has extensive experience with performance of both direct and consolidated data feeds. Lime has observed significant latencies in data provided by SIPs vs. direct feeds from exchanges; in one case we have seen as much as 10 times the latency. However, it is important to understand that different market participants require different performance levels. Forcing direct feeds to slow down to match the performance of the consolidator forces the industry into a one-size-fits-all model that does not account for the fact that a screen-based trader does not necessarily require the level of performance of a trading algorithm.

Rather than focus on sub-second differences, Lime encourages the Commission to focus on more broadly felt impediments to effective price discovery. The 90-second reporting rule, for example, is grossly out of synch with the capabilities of today's systems. It is possible that, for example, the lack of transparency into activity on dark pools is further hampered by the fact that they can report transactions up to 90 seconds after they occur.

Lastly, Lime would support a change in the transaction reporting rules to mandate reporting of odd-lot transactions. As fragmentation has increased and trade sizes have fallen, odd lots have become increasingly prevalent. Transparency is harmed by the lack of inclusion of this information into the public domain.

iv) Systemic Risk

Although much is still not known about the events that transpired on May 6th leading to the dramatic drop and bounce-back of the Dow Jones and several individual securities, Lime was in a position to observe the behavior of its clients during that afternoon. Relative to many of the areas noted in thc Release as possible contributors to systemic risk, Lime believes that its High Frequency Trading client base was instrumental in dampening the impact of the sharp drop in prices. Lime saw its clients' activity increase dramatically after 2:40pm; clearly the High Frequency community was an important source of liquidity during this difficult situation.

C) Undisplayed Liquidity

Lime generally supports the approaches outlined in the Regulation of Non-Public Trading Interest[5] proposal regarding Actionable IOI's. A long-standing conflict has existed between public price discovery and private information leakage. Institutional broker-dealers have nearly always engaged in the practice of "flashing" orders to select segments of their client base. Dark pools have facilitated the leakage of order information to numerous audiences prior to submission in to the public markets and price discovery flow.

As described above, Lime believes that a key element of addressing this conflict should be transparency. Investors should have information regarding the path an order will take through an institutional broker, and possibly out of that broker into one or more dark pools, prior to routing to an exchange or other "lit" market center. Clients should also have the ability to control to whom their orders are exposed during the order handling process.

[5] Securities Exchange Act Release No. 60997 (November 13, 2009), 74 FR 61028 (November 23, 2009).

D) Trade-At Rule, Depth-of-Book Protection

Lime views the potential imposition of both a trade-at rule and a depth-of-book protection rule as overly extreme responses to the dark pool issue. Both would effectively create a CLOB market structure. With a CLOB structure, the market is effectively held hostage to the slowest participant.

Additionally, we urge the Commission to carefully review the implications of the "trade at" rule, and the similarities of the requirement to route orders as ISOs to other market centers to "flash" order handling procedures that the SEC has opposed to the point of proposing that they be banned[6]. As described in the Release, under the suggested rule a trading center that was not displaying at the NBBO at the time it received an incoming marketable order could either (1) execute the order with significant price improvement (such as the minimum allowable quoting increment (generally one cent)); or (2) route ISOs of the full displayed size of NBBO quotations and then execute the balance of the order at the NBBO price. We believe that the result of this process would be what the Commission calls undesirable in the Flash Order Release: the creation of "a two-tiered market in which the public does not have access, through the consolidated quotation streams, to information about the best available prices for U.S.-listed securities". An example may be helpful to illustrate:

* Market Center A receives an order priced at the NBBO, but is not currently displaying the NBBO price. Exchanges B and C are displaying the current NBBO.
* Market Center A sends ISO orders to Exchanges B and C and executes the residual amount, and reports the transaction to a TRF for publication in the public data stream as well as reports a partial fill back to its client.
* Exchange B executes the incoming ISO order and reports the transaction to the public market as well as back to Market Center A. Market Center A reports the additional partial fill back to its client.
* Exchange C does not have sufficient liquidity to execute the inbound ISO order, and notifies Market Center A.
* Market Center A now executes the shares it had sent to Exchange C (assuming it is still possible under Reg NMS to do so) and reports the transaction to the public market and to the client.

The overall result of this scenario is (a) delayed, fragmented transaction reporting to the public with information flowing privately between Market Center A and the Exchanges; (b) greatly increased time during which the client has received only a partial execution; (c) a possible degenerate case whereby upon receipt of the "nothing done" on the ISO from Exchange C, market conditions have changed, requiring additional routing of the order due to Reg NMS requirements, further delaying the execution to the client.

E) Regulation of ATSs

Generally, Lime believes that the practice of internalization by a broker-dealer (whether via an ATS or more traditional proprietary trading operations) must be tightly regulated to ensure

[6] Securities Exchange Act Release No. 60684 (September 18, 2009), 74 FR 48632 (September 23, 2009) ("Flash Order Release")

customer orders are receiving the "best" possible execution. As noted above, we recommend increased transparency of order handling practices to address this issue.

Although not yet at a level that impedes public price discovery, migration of orderflow to dark pools could become sufficient to have a detrimental impact. We believe the Commission should monitor the situation closely. We also support the lowering of the display threshold to 0.25% as a measure to address this risk. We urge the Commission to also lower the threshold for the Fair Access requirements of Regulation ATS in Rule 302(b)(5) to the same 0.25% level.

Finally, we also believe that transparency around pricing, access criteria and membership of dark pools should be required. Exchanges are required to provide this information and as Dark Pools take on more and more liquidity and become subject to display and access requirements similar to those of exchanges, we believe investors have the right to this type of related information.

CONCLUSION

The obligation of a broker-dealer to provide best execution of client orders has been muddled by different forms of electronic flow interaction. The best approach to address the current situation is to go back to the core principles of best execution. The most effective environment to ensure best execution is one with full transparency into the broker's handling of an order, as well as choice as to if or how an order will be exposed to various internal and external parties prior to submission into the public markets.

At the same time we must preserve the elements of the US Equity market structure that makes it efficient, effective and competitive on the world stage. Innovation must not be stifled; investment must not be penalized. A race to the bottom in the name of fairness will not serve the investing public.

We applaud the Commission's thoughtful approach to analyzing our complex market environment, and we look forward to a continued dialogue on these critical topics.

Sincerely,

Jeffrey S. Wecker
CEO, Lime Brokerage LLC