S7-02-10 #235
S7-27-09 sn#90
S7-11-10 sn#14

MEMORANDUM

June 9, 2010

To: File No. S7-02-10
File No. S7-27-09
File No.: S7-11-10

From: Gena Lai
Office of Commissioner Troy A. Paredes

Re: Concept Release on Equity Market Structure
Regulation of Non-Public Trading Interest
Consolidated Audit Trail

On June 9, 2010, Commissioner Troy A. Paredes, and Gena Lai, Counsel to the Commissioner, met with the following individuals:

O. Mason Hawkins, Chairman and CEO,
Richard Hussey, COO,
Andy McCarroll, General Counsel,
Doug Schrank, Senior Trader, and
Jeff Engelberg, Principal

The participants discussed generally developments in equities market structure and the Commission's proposed rulemakings concerning the regulation of non-public trading interest and a consolidated audit trail. Mr. Engelberg provided the attached presentation, titled "Comments and Analysis on Equity Market Structure."

SOUTHEASTERN ASSET MANAGEMENT, INC.®

Comments & Analysis on Equity Market Structure

Presentation to the Securities and Exchange Commission Commissioner Troy A. Paredes

Summer 2010

Southeastern Representatives

- **O. Mason Hawkins, CFA**
  Chairman, Chief Executive Officer, and Founder
  B.A. (Finance) University of Florida, 1970
  M.B.A. (Finance) University of Georgia, 1971
  Southeastern since 1975
- **Richard Hussey**
  Chief Operating Officer and Principal
  B.S. (Applied Economics and Business Management) Cornell University, 1991
  Southeastern since 1999
- **Andrew McCarroll**
  General Counsel and Principal
  B.A. (English) Vanderbilt University, 1990
  M.A. (Religious Studies) University of Chicago, 1993
  J.D. Vanderbilt University, 1996
  Southeastern since 1998
- **Jeffrey Engelberg, CFA**
  Senior Trader and Principal
  B.S. (Economics) University of Pennsylvania, 1998
  M.B.A. (Finance and Information Systems) University of Pennsylvania, 1999
  Southeastern since 2007
- **W. Douglas Schrank**
  Senior Trader
  B.A. (Political Science) Colgate University, 2000
  Southeastern since 2009

Office Contact Information: *Southeastern Asset Management, Inc. 6410 Poplar Ave, Suite 900, Memphis, TN 38119*
(901) 761 - 2474

Southeastern's Motivation

Southeastern asserts that:

1. The intent of the Securities Exchange Act of 1934 as provided for in its preamble is being twisted and abused for the benefit of gamblers and to the detriment of investors.
2. The markets are not "fair and honest."[1]
3. Securities prices are presently "susceptible to manipulation and control, and the dissemination of such prices gives rise to excessive speculation, resulting in sudden and unreasonable fluctuations in the prices of securities."[1]
4. The preceding three issues are fixable by the SEC.

[1]*See Addendum A: Securities Exchange Act of 1934*

US Equity Market Concern

- The US equity markets are meant to facilitate investors' allocation of capital to businesses, thus expanding production and improving the quality of life in America.
- The markets have strayed from this social purpose, and presently resemble casinos more than orderly markets. As a result, the economy is hindered, fewer jobs are created, and reasonable returns for true investors (not traders) are compromised.
- The property rights of creators of intellectual capital are being systematically and openly ignored by the exchanges and certain market participants. The order originator's hard work, ingenuity, and prospective returns are being taken and sold by those who did not create it.[1]
- Whereas trading was once a means with which to match long-term buyers and sellers of businesses, trading has now become an end in and of itself.

[1]*See Addendum B: Intellectual Property Theft Trade, Addendum C: NYSE Email Exchange*

About Southeastern

- Investment advisor founded in 1975; independent and employee owned
  - No affiliated broker/ dealer, bank, or other financial institution
- 57 employees in Memphis, TN (Headquarters), London, Tokyo & Singapore
  - 740,603 employees at our US portfolio companies
- Research-driven team-approach to portfolio management
- Assets Under Management: $33.5 billion (as of 3/31/10)
  - Advise 150,000+ accounts through the Longleaf Partners mutual funds
  - Advise 200+ separately managed accounts (primarily charities, pensions, endowments)
  - Investment mandates: Domestic Large Capitalization, Domestic Small Capitalization, International, and Global
- Selected Recent Accolades
  - 2009 "Kiplinger 25"
  - 2009 Nomination for "Domestic Stock Fund Manager of the Year," Morningstar
  - 2007 "Equity Manager of the Year," Foundation & Endowment Money Management and Alternative Investment News
  - 2006 "Domestic Stock Fund Manager of the Year," Morningstar
  - 2005 CEO Mason Hawkins "Lifetime Achievement Award", Fund Action

Southeastern Invests for the Long-Term

- Philosophy
  - We are value investors. The funds seek to achieve superior long-term performance by acquiring equity securities of financially strong, well-managed companies run by capable managements at market prices significantly below our assessment of their business value. We sell stocks when they approach our appraisal. By partnering with business managements and purchasing equities at prices substantially below their intrinsic worth, capital is protected from significant permanent loss and will appreciate substantially once the market recognizes the company's economic value.
- Governing Principles
  - We will treat your investment in Longleaf as if it were our own.
  - We will remain significant investors with you in Longleaf.
  - We will invest for the long term, while always striving to maximize returns and minimize business, financial, purchasing power, regulatory and market risks.
  - We will choose our equity investments based on their discounts from our appraisals of their corporate intrinsic values, their financial strengths, their management, their competitive positions, and our assessments of their future earnings potential.
  - We will concentrate our assets in our best ideas.
  - We will not impose loads, exit fees or 12b-1 charges on our investment partners.
  - We will consider closing the Funds to new investors if closing would benefit existing shareholders.
  - We will discourage short-term speculators and market timers from joining us, the long-term investors in Longleaf.
  - We will continue our efforts to enhance shareholder services.
  - We will communicate with our investment partners as candidly as possible.
- Code of Ethics
  - All employees must limit their investments in publicly traded equities to Longleaf Partners Funds.
  - The employees and affiliates of Southeastern are collectively the largest owner across the three Longleaf Funds.

Southeastern's Investors

Mutual Funds ($13.2B as of 3/31/2010)

- 2009 US Mutual Fund Statistics[1]
  - 87 million Americans hold $12 trillion in assets through US mutual funds.
  - Individual investors hold 84% of mutual fund assets; 94% say that saving for retirement is their primary goal.
  - 66% of individual investors hold more than ½ of their financial assets in mutual funds.
  - 51% of DC retirement plan assets (e.g. 401k, 403b, 457) are in mutual funds.
  - 157,000 workers are employed by US mutual funds.
- Longleaf's investor base is primarily comprised of "ordinary" Americans seeking to plan for their futures.

[1]*Investment Company Institute, 2010 Investment Company Fact Book*

Separately Managed Accounts ($20.3B as of 3/31/2010)

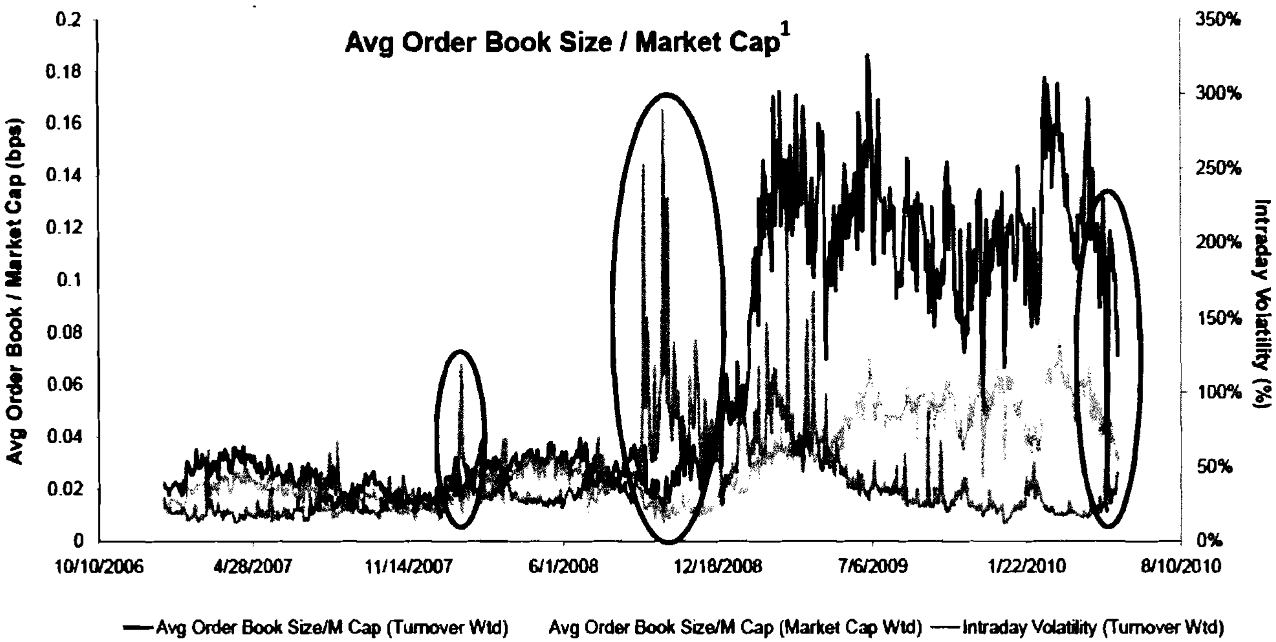
- Characteristics
  - 184 of 214 accounts are non-taxable
  - 78 private-company, employee-benefit plans
  - 11 public, employee-benefit plans
  - 49 endowments
  - 28 foundations
  - 5 mutual funds (in addition to Longleaf)
- Southeastern's institutional investor base is primarily comprised of non-profits seeking either to pursue noble charitable objectives and/ or assist in employees' financial security (i.e. retirement savings).

High-Frequency Trading Misconceptions

HFTs provide valuable liquidity to an otherwise fragmented marketplace.	WRONG[1]	• HFTs add and cancel quotes in milliseconds (ms). These quotes are not real and accessible. • HFTs hold positions briefly and end the day "flat." This is a mirage, not true liquidity. • HFTs time arb venues using structural advantages. This penalizes traders that are only 10ms slower.
HFTs offer investors price improvement by narrowing the spread.	WRONG[1]	• HFTs crowd out true liquidity providers (investors). Investor costs are increased. • HFTs step in front of larger displayed orders. This hides true supply/ demand. • Time arbitrage is not price improvement, it is stealing.
HFTs provide stability when other participants are overly emotional.	WRONG	• HFTs contribute to a lack of public market depth. This results in less confidence and more volatility. • HFTs are not obligated to provide markets. May 6, 2010! "HF STOP: sell everything, and shutdown."[2]
HFTs trade in milliseconds to ensure best execution for investors.	WRONG	• HFTs trade in milliseconds when it suits them. Their speed advantage gives them the option. • Why does anyone need executions sub 1 second? This encourages speculation, not sound investing. • How does this help capital formation or create jobs?

[1]*See Addendum D: False Liquidity Trade*
[2]*"Speedy New Traders Makes Waves Far From Wall St.," Julie Creswell, The New York Times, May 16, 2010.*

Unnecessary Liquidity - Only When Convenient



Average order book size was estimated using level 1 of minutely-binned intraday tick data

- The red line represents liquidity weighted by how heavily a stock is traded. The more trading action in a stock, the more it will be weighted. This is measured on the left axis.
- The yellow line represents liquidity weighted by the size of the company. The larger the company, the more it will be weighted. This is measured on the left axis.
- The blue line represents intraday stock volatility and is measured on the right axis.

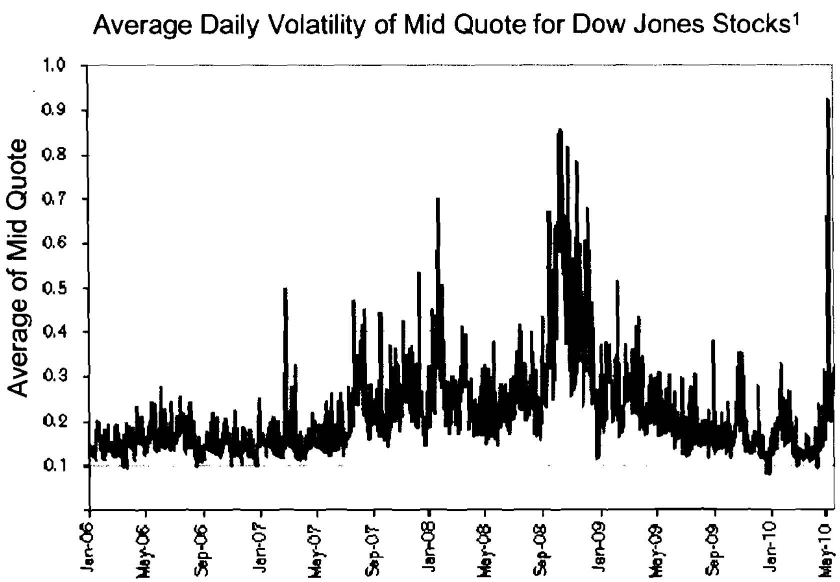
➢ Comparing the red line to the yellow line shows that more liquidity is provided in stocks with more "action."
  - HFTs are providing liquidity in places where extra liquidity is unnecessary, but potential profits are most attractive because more opportunities to insert themselves between buyers and sellers exist.

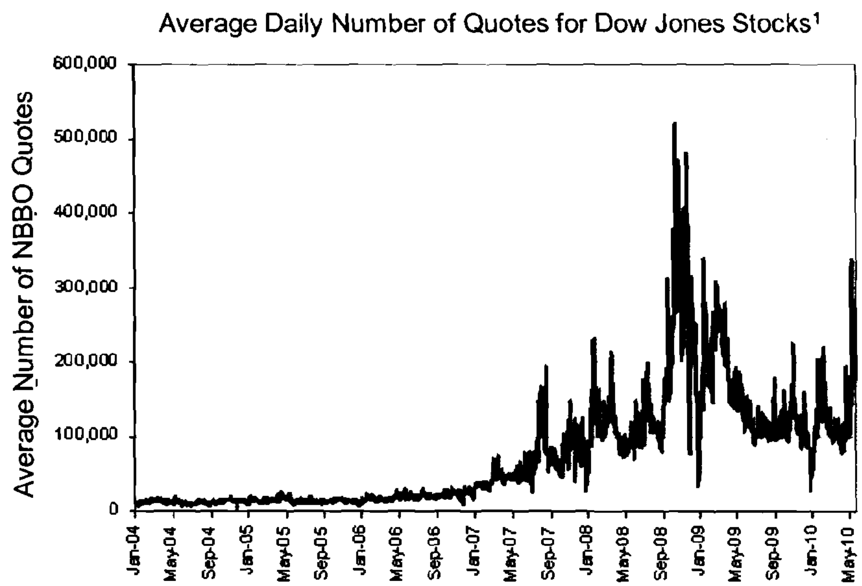
➢ Comparing the blue line to the red and yellow lines shows that as volatility increases, liquidity diminishes.
  - HFTs provide liquidity when the environment is calm, but disappear when liquidity is needed.

➢ The green ovals – Bear Stearns, subprime debacle, "flash crash" – show volatility spikes and liquidity droughts.
  - If HFTs thrive on volatility, then where are they during highly volatile periods?
  - HFTs will trade when it is beneficial for them. They are for-profit enterprises who are not altruistically motivated.

[1]*Nomura Quantitative Advisory, green ovals added by Southeastern Asset Management, Inc.*

HFT Volume Has Not Helped the Market





- HFTs claim to add stability, but at best appear to have no effect on true intraday price volatility.
- Intraday quote volatility has not decreased since HFTs have come to dominate quoting and trading.

- Can any true investor determine what is real when the quote changes 600+ times each minute?
- Average quote duration has gone from well over 1 second in 2004 to 0.1 second or less in 2010.

[1]*Credit Suisse*

Other Empirical Data

- 70% of the market is high-frequency trading[1]
- 71 exchange messages to 1 execution in 2009 vs. 9 to 1 in 2000[2]
- More than 30 cancellations for each exchange execution[3]
- Only 13% of trading volume was blocks in 2009[4] vs. 43% in 2000[5]
- Citadel reaped $1bln from high-frequency trading in 2008[6] from a $21.8bln pie[7]
- A recent broker proprietary study has shown a 50% increase in displayed market fill rates with the creation of a new smart order router designed to account for market structure inefficiencies. This study also showed a 108% increase in fill rate over a traditional cost effective order router.

[1] *Comment Letter in reference to SEC File No. S7-27-09. Tabb Group, December 8, 2009.*
[2] *Trading Talk, "An In-Depth Look at High-Frequency Trading." Rosenblatt Securities, Inc., September 30, 2009.*
[3] *NASDAQ ITCH data provided by Knight Capital Group.*
[4] *Compiled from data via NYXdata.com, May 27, 2010.*
[5] *"Block Trades Disappear as Volatility, Losses Increase." Bloomberg News, November 24, 2008.*
6 *"High-Frequency Gain: Citadel Unit's $1 Billion." Jenny Strasburg, Scott Patterson, and Lavonne Kuykendall. The Wall Street Journal, October 5, 2009.*
7 *"High-Frequency Traders Say Speed Works for Everyone." Edgar Ortega, Jeff Kearns, and Eric Martin. Bloomberg News, July 28, 2009.*

Empirical Data Desired

- How much accessible volume is available at the inside quote relative to the past?
- How much damage is inflicted on investors from inappropriate order detection strategies? Is any amount acceptable?

Requested SEC Action

- Forbid and prosecute the theft of trading decisions, which represent the actionable cumulative value of a manager's intellectual property by stating that:
  - The creator of trading information is the owner of such information.
  - Brokers have a fiduciary obligation to protect such information of their clients.
  - Exchanges cannot repurpose such information for their own benefit without the express consent of the information's originator.
  - Exchanges and brokers must furnish the information that is released regarding an order to the order's originator.[1]
  - Investors may opt to relinquish this intellectual property right, but, the default would be in favor of protecting information. No market participants can discriminate based on another party's elections.
- Mandate that all investors receive the same market data at the same time by:
  - Amending Regulation NMS Rule 603 to prohibit "single exchange data feed[s]" and require an exchange or national securities association to provide any quotation or last sale data for an NMS stock to any investor only as part of a consolidated display of all quotation data and all last sale data from all markets.
  - Banning an exchange or national securities association from providing "Order ID" or any other identifying market data that allows participants to determine whether specific quotes or executions are linked.
- Mandate that any order on an exchange or national securities association have a minimum duration of 1 second prior to any cancelations/ amendments taking effect. Alternatively, institute 1 second duration auctions during which all exchange transactions must occur.
- Eliminate maker/ taker pricing rebates by:
  - Expanding the ban on excessive access fees in Regulation NMS Rule 610 to ban a trading center from offering rebates as they provide perverse incentives when order routing.

[1]*See Addendum C: NYSE Email Exchange*

Fat Tails

- In statistics, fat tails (kurtosis) describe how often "outlier" events occur. The cliché "a once-in-a-lifetime catastrophe seems to occur every other week," is a commonplace reference to fat tails – extraordinary, unexpected events occurring more often than predicted.
- Fat tails are important in the financial markets as investors and regulators calibrate systems and expectations for the steady, normal state. When the abnormal occurs, most participants are caught off guard and find themselves in peril.
- After most fat tail events, a review of the contributing factors results in culpable parties explaining how their models could not have predicted what actually *did* happen.
  - 1987 Black Monday, portfolio insurance
  - 2007 Subprime Mortgage Crisis, exceptional default rates
  - May 6, 2010, DJIA temporarily falls nearly 1000 points, what was high-frequency trading's role?
- Questions for market regulators, legislators, and participants:
  1. Is the current market structure robust and resilient? Or,
  2. Do market regulators permit too many "tricks" amongst market participants?
  3. At the macro level, in a normal environment, do these "tricks" go unnoticed? But,
  4. In a fat tail event, will these "tricks" effect catastrophic outcomes?
  5. Are we wholly confident that the odds we place on extraordinary events – market shocks – are correct?
  6. Are market participants being consistently and effectively regulated, and are those strategic, tactical, and systemic risks being understood?

Media Coverage

- "But on the afternoon of May 6, as the stock market began to plunge in the 'flash crash,' someone [at Tradeworx] walked up to one of those computers and typed the command **HF STOP: sell everything, and shutdown**...The founder of Tradebot, in Kansas City, Mo., told students in 2008 that **his firm typically held stocks for 11 seconds. Tradebot, one of the biggest high-frequency traders around, had not had a losing day in four years**, he said...What all high-frequency traders love is volatility – lots of it. 'It was like shooting fish in the barrel in 2008. Any dummy who tried to do a high-frequency strategy back then could make money," said Manoj Narang, the founder of Tradeworx...**Showing a computer chart to a visitor, Mr. Narang zeroes in on one stock that had recently been a winner for the firm. Which stock? Mr. Narang clicks on the chart to bring up the ticker symbol: NETL. What's that? Mr. Narang clicks a few more times and answers slowly: 'NetLogic Microsystems.' He shrugs. 'Never heard of it,' he says."**
  - According to this citation, Tradeworx typically buys and sells 80 million shares a day.
  - Julie Creswell, "Speedy New Traders Makes Waves Far From Wall St.," May 16, 2010, The New York Times

- **"If they want to grab a piece of the profits in price movements that take place in thousandths and millionths of a second, they must put their trading engines under the same roof as the venues' order-matching engines.** Otherwise, they will suffer the indisputable laws of distance and physics. They won't execute trades fast enough."
  - John Dodge, "Keys to Success for Remote Traders: Co-Location and More Co-Location," May 3, 2010, Securities Industry News

- "Yet high-frequency specialists clearly have an edge over typical trader, let alone ordinary investors... 'This is where all the money is getting made,' said William H. Donaldson, former chairman and chief executive of the New York Stock Exchange...**'If an individual investor doesn't have the means to keep up, they're at a huge disadvantage.'"**
  - Charles Duhigg, "Stock Traders Find Speed Pays, in Milliseconds," July 23, 2009, The New York Times

Media Coverage (continued)

- "'**If you have no contractual obligation to make a market, and something happens, as a trader, you step away until things trade themselves out** ...You just know these markets, you just internalize these markets: How do I know that guy over there is sitting on pocket aces? Because he's sweating; and the way he held his chips; and the way he check-raised me. You know what I mean? All of a sudden, on the board, on the river, he check-raised me, and the board is like ace, three, three, seven, nine? And this guy's played tight all night long and now all of a sudden he's all in on the river and he check-raised me. What do you think he has?'"
  - Quote by John Netto, of M3 Capital, a high-frequency trading firm
  - Max Abelson, "The High-Frequency Talker," June 1, 2010, The New York Observer
- "At a court appearance July 4 in Manhattan, Assistant U.S. Attorney Joseph Facciponti told a federal judge that Aleynikov's alleged theft poses a risk to U.S. markets... 'The bank has raised the possibility that **there is a danger that somebody who knew how to use this program could use it to manipulate markets in unfair ways.'"**
  - David Glovin and Christine Harper, "Goldman Trading-Code Investment Put at Risk by Theft," July 6, 2009, Bloomberg
- " 'So far we're contending with the hackers and criminals and those that want to exploit us, and we're not being attacked by someone who wants to destroy us," he said. But, **the next financial catastrophe could well be launched by "a group that would want to destroy something.' "**
  - Quote by Mitch McConnell, former director of the National Security Agency
  - Tom Steinert-Threlkeld, "SIFMA OPS 2010: Market Swing 'Highlights Vulnerability' to Attack by Extremists, Former NSA Director Says," May 7, 2010, Securities Industry News

Wall Street Journal, June 4, 2010

The ability to estimate price moves ahead of the national best bid and offer price, which is consolidated electronically from exchanges, can give traders an advantage of about 100 to 200 milliseconds over investors who use standard market tools, according to a November 2009 report on such trading activities by Jefferies & Co.

An advanced look at exchange data and order flow can provide firms "the ability to forecast future prices" and "make adjustments to their orders in the market or send new orders which are based on this information," the report found.

Some investors are searching for ways to protect themselves. Rich Gates, co-founder of TFS Capital LLC, started becoming concerned about latency arbitrage in early 2009 after a Wall Street bank pitched the trade to his firm.

In hundreds of tests, TFS has found that some of its trades were getting picked off by firms exploiting the time-delay wrinkle. That was costing the firm money.

To learn more, TFS, which manages about $1.1 billion in mutual funds and hedge funds, devised a method to essentially bait firms into engaging in the trade. In effect, TFS proved that some traders were wise to a movement in a stock's price before it happened.

On a March afternoon, a TFS trader sent an order to a broker to buy shares of Nordson Corp., a maker of fluid dispensing equipment. The trader sent an instant message to the broker: "please route to broker pool #2," a request to send the order to a specific dark pool.

The trader told the broker not to pay a price higher than the midpoint between what buyers and sellers were offering, which at the time was $70.49.

Several seconds after the dark pool order was placed, the market price didn't change. Then the TFS trader set a trap: he sent a separate order into the broader market to sell Nordson for a price that pushed the midpoint price down to $70.47.

Almost immediately, TFS was sold Nordson for $70.49—the old, higher midpoint—in broker pool No. 2, which didn't reflect the new sell order. TFS got stuck paying two cents more than it should have, suggesting that some seller knew the higher price was a good deal to nab quickly.

Such trades are "unusually suspicious," said Mr. Gates.

- Scott Patterson, “Fast Traders’ New Edge,” June 4, 2010, Wall Street Journal

Addendum A: Securities Exchange Act of 1934

- For the reasons hereinafter enumerated, transactions in securities as commonly conducted upon securities exchanges and over-the-counter markets are affected with a national public interest which makes it necessary to provide for regulation and control of such transactions and of practices and matters related thereto, including transactions by officers, directors, and principal security holders, to require appropriate reports, to remove impediments to and perfect the mechanisms of a national market system for securities and a national system for the clearance and settlement of securities transactions and the safeguarding of securities and funds related thereto, and to impose requirements necessary to make such regulation and control reasonably complete and effective, in order to protect interstate commerce, the national credit, the Federal taxing power, to protect and make more effective the national banking system and Federal Reserve System, and **to insure the maintenance of fair and honest markets in such transactions**:

- **Frequently the prices of securities on such exchanges and markets are susceptible to manipulation and control, and the dissemination of such prices gives rise to excessive speculation, resulting in sudden and unreasonable fluctuations in the prices of securities** which (a) cause alternately unreasonable expansion and unreasonable contraction of the volume of credit available for trade, transportation, and industry in interstate commerce, (b) hinder the proper appraisal of the value of securities and thus prevent a fair calculation of taxes owing to the United States and to the several States by owners, buyers, and sellers of securities, and (c) prevent the fair valuation of collateral for bank loans and/or obstruct the effective operation of the national banking system and Federal Reserve System.

Addendum B: Intellectual Property Theft Trade

Public Data Feed			
Buyers		Sellers	
Quantity	Price	Price	Quantity
		$24.03	200 shrs
		$24.02	100 shrs
		$24.00	100 shrs
500 shrs	$23.99		
600 shrs	$23.98		
900 shrs	$23.96		

Direct Exchange Data Feed							
Buyers				Sellers			
Accumulated[1]	Order ID	Quantity	Price	Price	Quantity	Order ID	Accumulated[1]
				$24.03	200 shrs	#285	123,000 shrs
				$24.02	100 shrs	#128	5,800 shrs
				$24.00	100 shrs	#092	2,084,000 shrs
3,000 shrs	#394	500 shrs	$23.99				
0 shrs	#067	600 shrs	$23.98				
1,900 shrs	#591	900 shrs	$23.96				

1. Looking at the public data feed, would you buy or sell? (Buy) With the additional information that high-frequency traders (HFTs) pay the exchanges for directly, would you buy or sell? (Sell) Observe how HFTs may use this direct exchange data feed information to front-run the $24.00 seller.
2. Additionally, the direct data feed alerts subscribers when a public order changes limits. This functionality exists both to allow HFTs to rebuild and follow every step of an order without the order originator realizing they are being tracked and disadvantaged and to provide an opportunity for the HFT to front-run the limit-order change.
3. Combining the use of direct data feeds with co-location services gives HFTs an unfair and inappropriate opportunity to detect and disadvantage long-term investors.
4. The exchanges should have no right to track and publish a customer's order information and activities (i.e. intellectual property) to anyone, let alone a small subset of paying subscribers, unless the information must be made public by law or regulation. At the very least, for-profit exchanges must be required to furnish the information that is released regarding an order to the order's originator.[2]

[1]*Consistent customer tracking of order ID enables tracking of accumulated shares*
[2]*See Addendum C: NYSE Email Exchange*

Addendum C: NYSE Email Exchange (part 1)

May 21, 2010

Janet Kissane
Corporate Secretary
NYSE
11 Wall Street #7
New York, NY 10005-1974
Email: jkissane@nyse.com

Re: Data Feeds

Dear Ms. Kissane

Southeastern Asset Management, Inc. is a $33 billion asset manager which invests in equities globally. In the normal course, we access execution venues via broker/dealers or their electronic offerings. Should you wish, a check with any of your bulge-bracket, broker-dealer participants will confirm our standing in the market.

The purpose of this letter is to request that you provide to us information related to any data on orders, trades, and/or other market data which you make available which is a field other than anonymous and non-trackable (1) unhidden order side, (2) unhidden order size, (3) unhidden order limit, (4) time of trade, (5) trade size executed, and (6) executed price. Further, please describe and provide the market share of each order type you make available to users of your venue.

Would you please provide us with these data field names, a description of each field, the products in which they are offered, and, the cost of such products? We would greatly appreciate receipt of this information by June 4, 2010. Please send the information to samdatause@llpf.com. Please contact me at 901 818 5185 with any questions. Thank you very much for your time and attention to this matter.

Sincerely,

Andrew R. McCarroll

Andrew. R. McCarroll
VP & General Counsel

Addendum C: NYSE Email Exchange (part 2)

1

From: Andy McCarroll
To: Janet Kissane
Date: 05/21/2010 04:01 PM
Subject: Letter from Southeastern Asset Management, Inc.

Dear Ms. Kissane:

Attached please find a letter from Southeastern Asset Management requesting information on data feeds at the NYSE.

Please contact me with any questions.

Sincerely,

Andy McCarroll
VP & General Counsel
Southeastern Asset Management, Inc.

2

From: Janet Kissane
Sent: Wednesday, May 26, 2010 10:03 AM
To: Andy McCarroll
Subject: Re: Letter from Southeastern Asset Management, Inc.

Mr. McCarroll, Thanks for your letter and for answering my questions last week.

All of the publicly available specifications regarding our data feeds can be obtained by visiting :
http://www.nyxdata.com/Docs/Market-Data/Technical

Thanks,

Janet M. Kissane
SVP - Legal & Corporate Secretary
Legal & Government Affairs

3

From: Andy McCarroll
To: Janet Kissane
Date: 05/26/2010 02:22 PM
Subject: RE: Letter from Southeastern Asset Management, Inc.

Dear Ms. Kissane:

Thank you very much. I passed this on to my traders and they asked me if there was someone who could help decipher this for us. Is there someone who understands these technical issues that could answer the questions in our letter? I am happy to put my traders with the appropriate technicians on your side if that would help. Also, I assume that any data you make available (for free or for sale) to the public would be discussed in some way in public documents. Is that correct?

Thank you.
Andy McCarroll

4

From: Janet Kissane [mailto:JKissane@nyx.com]
Sent: Wednesday, May 26, 2010 2:51 PM
To: Andy McCarroll
Subject: RE: Letter from Southeastern Asset Management, Inc.

You should feel free to research our SEC rule filings describing our market data products; these are publicly available on our website and in some instances, the SEC's website as well. We are not able to otherwise satisfy your request at this time. Thanks,

Janet M. Kissane

Addendum D: False Liquidity Trade

Pre High-Frequency Trading					
Buyers			Sellers		
Participant	Quantity	Price	Price	Quantity	Participant
			$24.07	200 shrs	Charity #2
			$24.05	300 shrs	Retail #2
			$24.04	1200 shrs	Endowment #2
			$24.02	4100 shrs	Mutual Fund #2
			$24.01	3200 shrs	Hedge Fund #2
Mutual Fund #1	2500 shrs	$23.98			
Pension Fund #1	1300 shrs	$23.97			
Endowment #1	1000 shrs	$23.95			
Retail #1	500 shrs	$23.92			
Charity #1	1300 shrs	$23.91			

Currently (with HFT)					
Buyers			Sellers		
Participant	Quantity	Price	Price	Quantity	Participant
			$24.04	100 shrs	Mutual Fund #2
			$24.03	100 shrs	Hedge Fund #1
			$24.02	100 shrs	HFT #1
			$24.01	200 shrs	HFT #3
			$24.00	100 shrs	HFT #2
HFT #1	100 shrs	$23.99			
HFT #2	100 shrs	$23.98			
Mutual Fund #1	200 shrs	$23.97			
HFT #3	100 shrs	$23.96			
Retail #1	500 shrs	$23.95			

1. Exchanges pay rebates (no more than $0.30 per 100 shares) to traders that post orders and charge investors that cross the spread and take liquidity. This new pricing scheme makes it very profitable for HFTs to buy and sell stock at the same price within one second and capture the rebate.
2. When considering how shallow (i.e. less quantity at each price) and fleeting the market has become, tighter spreads are a superficial and misleading metric for market quality.
3. Increased volume is simply a mirage created by HFTs churning in search of rebates.
4. True investors have been crowded out by HFTs. Counter to the argument that investors save money by paying smaller spreads, true investors actually lose money because they are front-run.
5. Retail investors once displayed the smallest public bids and offers. Unfortunately, retail investors have not changed their tactics to account for HFT rovers and are now displaying larger orders relative to other market participants on average. This results in the retail investor being disadvantaged.

Disclosure

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