



December 10, 2014

Chair Mary Jo White  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20548-1090

Re: Governance of the NMS Plans Concerning Securities Information Processors and the Consolidated Audit Trail

Dear Chair White:

IEX Services LLC ("IEX") appreciates the opportunity to share its views with the Commission on an important and timely topic: the operation and administration of our National Market System ("NMS") Plans for the Consolidated Trade Association ("CTA") and Unlisted Trading Privileges ("UTP") Securities Information Processors (each, a "SIP"). Particularly, IEX is writing to express its view that the market as a whole and the public good would benefit from reformation of the mechanisms of governance of these central elements of the national market system. Further, although this letter focuses primary attention on the governance of the SIPs, certain of the suggestions offered below, and the underlying concerns that motivate them, are equally pertinent to all of the national market system plans filed under Rule 608 of Regulation NMS.

IEX currently operates a non-displayed alternative trading system for US equities. IEX offers a simplified and transparent market structure designed to eliminate many of the conflicts that are currently present in the financial markets. Also, with investor-centric order types and advanced technology and architecture, IEX has sought to neutralize on its trading platform certain negative effects of structural inefficiencies in the national market system. IEX intends to apply for registration as a national securities exchange in the near term.

#### Background

The operation and administration of the SIPs are critical contributors to the resilience and reliability of our equity market infrastructure, on which a broad range of participants – market makers, agency brokers, full-service brokers, traders, and institutional and retail investors – rely. Two recent examples highlighting the importance of the SIPs to investors and other market participants are the August 22, 2013 market-wide halt in NASDAQ-listed securities due to an extended interruption of service from the UTP SIP, and the October 30, 2014 disruption of the CTA SIP for NYSE- and other-exchange listed securities, which resulted in a number of venues halting trading, as well as confusion among some market participants related to referencing trade prices to certain regulatory and clearly erroneous price thresholds.

More broadly, we share the concern of many market participants about the consequences of the fact that SIP feeds are significantly slower than proprietary exchange market data feeds, which you addressed in your speech last June on equity market structure.<sup>1</sup> Specifically, a firm utilizing each exchange's

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<sup>1</sup> See speech by Chair Mary Jo White at Sandler O'Neill & Partners, L.P. Global Exchange and Brokerage Conference



proprietary market data feed could likely determine the best bid or offer (BBO) across all exchanges in a significantly shorter timeframe than the SIP, including accounting for network propagation delays. While we recognize there have been improvements in recent years, they have not been uniform across the SIPs, nor in our opinion, adequate.

We appreciate the efforts that the Commission has made in motivating plan participants to enhance the robustness and resilience of the SIPs since the August 22 UTP SIP incident.<sup>2</sup> However, we believe that public confidence in the management of the SIPs requires a higher level of accountability and transparency than is required or has been demonstrated under the current NMS plans. Recent published reports detailing the efforts to name a new operator for the Nasdaq/UTP SIP, including use of executive sessions that exclude current advisory committee members, the voting participation of SROs that are currently not operating US equity venues, and which, when all was said and done, resulted in the same operator, highlight the need for a different framework.<sup>3</sup>

When taken together, we see these issues of integrity, performance, and process, along with pricing of SIP fees and exchange proprietary data feed fees, as being inextricably tied to conflicts of interest. These conflicts are particularly evident in the distribution of market data feeds. The self-regulatory organizations (“SROs”), which sit as the governing body of the NMS Plans managing the consolidated market data feeds provided by the SIPs, are also selling proprietary data feeds, some of which are similar in data level, such as best-price, or ‘top of book’ feeds, some which are more robust, such as full depth of book feeds, and some of which are explicitly sold as alternatives to compete with SIP feeds. Indeed, often the same exchange personnel, with access to participant data on the use of the SIP feeds, are engaged in marketing both consolidated and proprietary data.

These conflicts concerns are particularly acute where, as here, private sector entities occupy a monopoly position in providing a utility function to collect and distribute consolidated market data, which was intended to serve as the “heart of the national market system”, by enabling investors to know about and have access to the best displayed prices for NMS stocks, wherever traded, and to monitor execution prices for compliance with best execution obligations.<sup>4</sup>

Our comments are not directed to any presently pending rule filing relating to SIP governance, but are timely with respect to the governance provisions contained in the National Market System Plan Governing

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New York, N.Y., “Enhancing Our Equity Market Structure” (June 5, 2014) (See <http://www.sec.gov/News/Speech/Detail/Speech/1370542004312#.VH9y8hBT5FM> )

<sup>2</sup> See Statement of Chair White on Meeting with Leaders of Exchanges (September 12, 2013), available at <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539804861>; Speech by Chair White, “Enhancing Our Equity Market Structure”, at the Sandler O’Neill & Partners, L.P> Global Exchange and Brokerage Conference, available at <http://www.sec.gov/News/Speech/Detail/Speech/1370542004312>

<sup>3</sup> See letter from Theodore R. Lazo, Managing Director and Associate General Counsel, SIFMA, to Thomas P. Knorring, Chairman, Nasdaq/UTP Plan Operating Committee, dated October 14, 2014, avail at <http://www.sifma.org/issues/item.aspx?id=8589951622>.

<sup>4</sup> See Concept Release on Equity Market Structure, Exchange Act Release No. 61358 (January 14 2010), at 20, available at <http://www.sec.gov/rules/concept/conceptarchive/conceptarch2010.shtml>.



the Consolidated Audit Trail (the “CAT Plan”). Further, we understand that additional proposals related to governance under the Nasdaq UTP Plan may be forthcoming.

We offer the following suggestions for consideration by the Commission, the plan participants, and the industry as ways to enhance the operation of the SIPs and contribute to the improvement of governance of NMS Plans in general, and the SIPs in particular.

- Transparency of Proceedings and Economics.
- Expand Voting Representation to Include Other Stakeholders.
- Alternative/Competitive Models for Securities Information Processors.
- Addressing Conflicts of Interest.

We believe it is important that the NMS plans under which the SIP governance arrangements are established be amended to provide for voting representation by investors and broker-dealers, in order to assure that the interests of these stakeholders are represented in the management of these critical components of our securities market infrastructure. In addition, we believe that the voting representation of exchanges on the SIP Operating Committees should be reformed to more rationally reflect the actual, and currently operational, stake in these systems by each exchange group and should better address conflicts of interest when one or more members of the committees have a unique interest in the outcome of a particular decision. Governance changes also would help to address and counter the potential use of the SIP infrastructure to advance the commercial interests of the operating exchanges – a prime example of which was the use of the Tape A SIP to support and promote the adoption of a special category of “retail liquidity provider” designed to attract retail order flow to the exchange.<sup>5</sup> These concerns also have resonance for the governance arrangements under various other national market system plans filed under Rule 608 of Regulation NMS, and, as noted, to the plan for the Consolidated Audit Trail under Rule 613 of Regulation NMS (“CAT Plan”).<sup>6</sup>

Indeed, we believe that the governance changes described below would provide fresh perspectives and a healthy level of transparency within the SIP Operating Committees that would help to promote further discussion of more fundamental changes and could help to fashion additional recommendations for consideration by the Commission. Even more broadly, changes to the governance structure could promote a better degree of accountability and transparency in other areas, including, for example, decisions about the setting by the exchanges of fees charged to market participants for market data, and transparency of the books and records and costs related to the aggregation and dissemination of such data. Indeed, governance changes would better account for the fact that the data processed by the SIPs is generated by non-exchange participants, since exchanges by definition do not generate orders and trades themselves.

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<sup>5</sup> See SEC Order Granting Approval to Proposed Rule Changes, as Modified by Amendments Nos. 1 and 2, Adopting NYSE Rule 107C and Adopting NYSE Amex Rule 107C to Establish a Retail Liquidity Program for NYSE-Listed Securities on a Pilot Basis Until 12 Months From Implementation Date, and Granting Exemptions Pursuant to Rule 612(c) of Regulation NMS, SEC Release No. 34-67347; File Nos. SR-NYSE-20111-55ISR-NYSEAmex-2011-84 (July 3, 2012) (Available at [www.sec.gov/rules/sro/nyse/2012/34-67347.pdf](http://www.sec.gov/rules/sro/nyse/2012/34-67347.pdf))

<sup>6</sup> See “Filing and amendment of national market system plans”, 17 CFR 242.608 and “Consolidated audit trail”, 17 CFR 242.613.



### Transparency of Proceedings and Economics

Absolutely fundamental to an adequate governance structure is clear and appropriate levels of transparency. We recommend requirements to make publicly available the CTA and UTP meeting minutes, voting records and any other recordings or reports of proceedings that are not explicitly required to be treated confidentially, such as proposals or communications from third parties not acting in a direct governance capacity. Basic transparency standards should also be applied to fully disclose economics of cost, including revenue, fines and revenue disbursement and/or cost allocation, for those Plans which have such elements.

### Expand Voting Representation to Include Other Stakeholders

We believe that the most important substantive change that should be made is to ensure voting representation by investors and broker-dealers on the respective Operating Committees, thereby ensuring that these stakeholders have visibility into, and a voice in, the operation of these committees. This step is critical to achieve the desired level of transparency and accountability. Representation on a SIP advisory committee, as exists presently, is not an adequate substitute. Experience has shown that advisory committee members are consulted only when and as the voting representatives determine to do so, and the critical negotiations and decisions take place among the voting representatives with actionable responsibility. Further, the fact that SIP advisory committee members are selected solely by voting representatives undercuts their ability to serve as a strong independent voice in affecting the decisions ultimately taken.

We see no impediment in existing legislation or Commission rules that would prevent the amendment of current NMS plans to accomplish this goal. Section 11A of the Securities Exchange Act of 1934 gives authority to the Commission, by rule or order, “to authorize or require self-regulatory organizations to act jointly with respect to matters as to which they share authority...in planning, developing, operating, or regulating a national market system.”<sup>7</sup> This language empowers the Commission to set the terms under which NMS plans, including those pertaining to the SIPs, may be approved; it does not preclude the ability of such plans in their governance structures to provide for representation of investors and other stakeholders. Indeed, such representation is wholly consistent with national market system goals, including the “economically efficient execution of securities transactions,” “fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets”, and “the availability to brokers, dealers, and investors of information with respect to quotations for and transactions in securities...”<sup>8</sup> Similarly, Rule 608 of Regulation NMS authorizes SROs to act jointly in filing or amending NMS plans and provides that the Commission may propose amendments to such plans; it does not prescribe or limit the range of stakeholders that may be represented on the respective governing committees.<sup>9</sup> The existing limitation of the governing committees to SROs is particularly inapt in an era in which most of those entities operate as part of for-profit, publicly-traded holding companies, rather than under the industry utility model that prevailed at the time the plans were first approved. If, however, the Commission determines that the proposed

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<sup>7</sup> See “Filing and amendment of national market system plans”, 17 CFR 242.608.

<sup>8</sup> See “National market system for securities; securities information processors. 15 U.S.C. sec. 78k-1(a)(1).

<sup>9</sup> See “Filing and amendment of national market system plans”, 17 CFR 242.608.



change would require legislative action, we would support, and would urge the Commission to support, a targeted legislative change to accomplish this objective.

There are various options that could be considered in prescribing how representatives of non-SRO stakeholders could be selected. For example, investor and broker-dealer representation could be based on nominations by broad-based industry associations that represent the particular constituencies, with plan participants making the final decision from among such nominees.

Ideally, the governance structure would allow for multiple representatives for retail investors, institutional investors, and broker-dealer constituencies (including integrated multi-service firms and exclusively agency broker-dealers). Our overall interest, however, is not in mandating a particular standard of relative voting strength as compared to SRO representation, but instead, assuring that there is a reasonable method for enabling independent representation of the affected constituencies.

#### Allocation of Voting Rights Among SROs

We believe another area of needed reform in voting representation within the SIP Operating Committees concerns the allocation of voting rights among the exchange groups. The existing “one exchange-one vote” model is distortive and inequitable given that the existing exchange operators hold separate exchange registrations, directly or indirectly, under a single holding company or similar corporate structure, primarily to account for alternative pricing structures while operating these entities as coordinated business enterprises. A more equitable method would be to allocate voting rights equally at the exchange group level, i.e., among each “exchange family”.

Similarly, voting rights should be limited to those exchanges that are presently engaged in equity securities business. Entities that hold an exchange registration but are not presently engaged in the equities business are fundamentally differently situated because they do not have a direct stake in the operation of the equities market infrastructure and do not bear responsibility for it.

#### Alternative/Competitive Models for Securities Information Processors

We do not mean to suggest that governance changes to the existing NMS plans pertaining to the SIPs would by themselves obviate the need for a broader reevaluation of the current SIP model. It is worth considering whether the operation of separate SIPs with the scope of responsibility divided by listing market continues to make sense in today’s marketplace. The illogical operation of the current system is highlighted by the practice of having meetings of the committees, which consist of many common members, conducted in close time proximity.

Allowing for the possibility of competing, registered securities information processors acting as consolidators of market data may yield a number of benefits. First, a multi-SIP model would limit the potential that any given SIP would act as a “single point of failure”; provided that this change could be accomplished in a way that retains the ability for market participants to continuously determine a single national best bid and offer. As an interim step, each of the current SIPs could be permitted to begin processing data that is now processed on an exclusive basis, adding resiliency and competition to the system. Further, allowing multiple processors might better motivate entities performing this function to better respond to the needs of market participants with innovations, improved service levels, and competitive pricing. At a minimum, ending the ability of exchanges to sell and disseminate private data



feeds in a way that results in faster receipt of such data as compared to the consolidated data feeds would better help to incentivize the operators of the SIPs to make the investments necessary to update and strengthen the consolidated data feeds.

#### Addressing Conflicts of Interest

Finally, it is important that the governance rules be amended to address basic conflicts of interest concerns and recusal requirements in a case where a participant has a unique stake in the outcome of a particular decision. Certainly, these provisions should apply to the question of the selection of a plan administrator, and to other potential issues where a specific participant has a vested commercial stake in the outcome. These concerns were addressed in the CAT Plan recently filed by the SROs, by providing for recusal on key decisions where a participant or an affiliated entity is a short-listed bidder, or one of the finalists, considered for selection as the initial plan processor.<sup>10</sup> This type of provision is a matter of basic sound governance principles, and the failure to account for such conflicts necessarily undermines the confidence of market participants in the governance of NMS Plans.

#### Application to the CAT Plan

Although the CAT Plan as filed by the SROs has not yet been published by the Commission for comment, we note, other than with respect to the conflict of interest provisions just mentioned, that the CAT Plan as filed by the SROs would duplicate the deficiencies identified above with respect to the SIP plans. Investors and other market participants are likewise vitally interested in the funding and operation of the consolidated audit trail, and we believe that a governance structure that operates as a “carbon copy” of that existing under other NMS plans would similarly undermine public confidence in that vital initiative.

Respectfully submitted,

A handwritten signature in black ink that reads "Donald Bollerman". The signature is fluid and cursive, with a long horizontal line extending to the right.

Donald Bollerman  
Head of Market Operations

cc: Commissioner Luis A. Aguilar  
Commissioner Daniel M. Gallagher  
Commissioner Kara M. Stein  
Commissioner Michael S. Piwowar  
Brent J. Fields, Secretary  
Nathaniel Stankard, Deputy Chief of Staff to the Chair  
Stephen I. Luparello, Director, Division of Trading and Markets  
David Shillman, Associate Director, Division of Trading and Markets

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<sup>10</sup> See letter to Brent J. Fields, Secretary, SEC from the parties to the National Market System Plan Governing the Consolidated Audit Trail, dated September 30, 2014, at 13-14 (Available at <http://catnmsplan.com/>).