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March 29, 2010

Elizabeth M. Murphy
Secretary
United States Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Exchange Act Release No. 61379; File No. S7-03-10; Risk Management Controls for Brokers or Dealers with Market Access

Dear Ms. Murphy:

Jane Street Holding, LLC and its affiliated companies ("Jane Street") appreciate the opportunity to comment on the Commission's rule proposal titled "Risk Management Controls for Brokers or Dealers with Market Access"[1] (the "Sponsored Access Proposal"). Jane Street is a proprietary trading group that conducts business through both regulated broker-dealer and unregulated entities. Much of Jane Street's trading is conducted through proprietary trading systems focused on quantitative and latency-sensitive strategies. Some of that trading is conducted via sponsored access provided by both affiliated and unaffiliated broker-dealers.

The Sponsored Access Proposal would, among other things, require sponsoring broker-dealers to institute a system of pre- and post-trade financial and regulatory checks and controls, and require that such controls be in the "direct and exclusive control" of the sponsoring member. We share the Commission's concern that the growth in sponsored access has created the potential for serious financial and regulatory risks. However, we respectfully suggest that such checks will restore major barriers to entry based on technology and pricing, and that a reversal in recent trends toward market efficiency, competitive parity, market accessibility, and reduced costs is likely. If the sponsored access user is unregulated, the benefits of increased oversight and risk reduction likely justify any adverse effects on market quality. However, in the common case in which the sponsored access user is a regulated broker-dealer, the proposal would require the sponsor's controls on top of the broker-dealer's own financial and risk controls. This second layer of control would provide minimal gains from increased oversight, whereas its anti-competitive effect in slowing down the broker-dealer's order flow would have substantial adverse effect on market quality.

Accordingly, we suggest that, to achieve the Commission's goal of ensuring proper controls on order flow, while avoiding the anti-competitive effect of a dual layer of controls, the controls provided for in proposed Rule 15c3-5 apply to a broker-dealer's access to markets, whether direct or through a sponsor, and that a sponsor be required to maintain independent controls only with respect to sponsored flow of an unregulated entity.

1. Market Motivations for Sponsored Access

One widely understood motivation for the use of sponsored access is the reduction of latency. Latency is most often discussed in the context of unregulated entities, which, lacking the prerequisite of broker-dealer status, are unable to become exchange members and therefore cannot connect directly to markets. However, many small broker-dealers, despite their regulated status, are not in a position to incur the significant connectivity and other costs associated with direct membership. In our estimation, this latter category of sponsored access users has grown significantly in the post-Regulation NMS world, as market fragmentation has dramatically driven up the cost of marketwide coverage. However, despite the market forces driving small broker-dealers away from exchange memberships, these firms (particularly those

[1] Exchange Act Release No. 61379, 75 FR 4007 (January 26, 2010).

engaged in market making and other liquidity provision strategies) still must operate in a trading environment that increasingly rewards the lowest possible latency. In such a framework, only those trading parties with direct access to the markets can compete effectively and, in the absence of cost-prohibitive exchange connectivity, sponsored access provides a viable solution to the issue of access.

A second major driver of the growth of sponsored access is tiered pricing structures. This motivation is not often discussed in the context of sponsored access; however, it is crucially important to the issue. Market fragmentation has introduced tremendous competition among the exchanges for trading volume. As a result, exchanges, to attract and retain order flow, have introduced pricing tiers that favor those members that provide the greatest volumes. By their nature, these pricing tiers provide a decisive advantage to the larger broker-dealers, which have outsized customer and proprietary order flows that can benefit from the best pricing, resulting in reduced trading costs. In contrast, smaller broker-dealers generally have insufficient order flow to obtain the same favorable pricing. Many of these smaller broker-dealers are capable of maintaining exchange memberships and low-latency connectivity on their own behalf, but they participate in sponsored access to aggregate their flow with that of others to reach the most favorable fee tiers and overcome the handicap of uncompetitive pricing. (Jane Street falls into this category.) In the particular case of high-volume liquidity provision, the difference in exchange fees from the lowest to the highest tier can easily be of the same order as the per-share profits that liquidity providers seek to earn.

2. Effects of the Sponsored Access Proposal

When examined from the perspective of these two drivers, sponsored access ultimately serves to level the playing field between smaller and larger market participants, and thus to bring more competition to the marketplace. We believe that any structure that increases the level of competition among market participants will yield direct and tangible benefits to both the retail and institutional clients served by these participants. In our view, competition in the equity markets has caused a significant increase in the liquidity and overall efficiency of the U.S. capital markets, including tighter spreads, deeper markets, reduced commissions and greater choice among providers of trading services.

We respectfully disagree with the contention that sponsored access providers could institute the checks and controls contemplated by the Sponsored Access Proposal while maintaining a competitive level of latency. In the current marketplace, competition is sufficiently intense that any latency increase, no matter how small, would noticeably tilt the playing field. We believe this would be particularly true for broker-dealers engaged in high speed liquidity provision, which are among the largest current users of sponsored access. Similarly, the competitive imbalance caused by exchanges' price tiers cannot be overcome without the aggregation effect that sponsored access allows. We therefore believe that the Sponsored Access Proposal will lead to small liquidity providers, which have been a primary force for innovation and improvement, being driven from the market, to the advantage of larger firms but the disadvantage of retail and institutional customers alike.

3. Regulated versus Unregulated Entities

Notwithstanding our concerns with the Sponsored Access Proposal, we are acutely aware of the need to protect equity markets against risks caused by trading activity devoid of appropriate controls and oversight. However, any increase in systemic risk introduced by the sponsored access model is not, in our opinion, the result of its use by broker-dealer sponsored access users. Such users are already bound by their own obligations to maintain proper risk, financial and regulatory controls, and are further subject to direct regulatory oversight and examination. Broker-dealer users may even be members of the relevant exchanges, utilizing sponsored access only to achieve competitive pricing tiers.

To the extent the Commission wishes to increase regulation of sponsored access, we believe it appropriate for sponsoring members to serve in the "gatekeeper" role contemplated by the current proposal with respect to users that are not otherwise subject to the regulatory obligations and oversight that apply to broker-dealers.

In contrast, we contend that when the sponsored access user is a regulated broker-dealer, additional checks and controls at the sponsor's level are unjustified and will significantly harm the competitiveness of equity markets. We believe there are important reasons for drawing a distinction between regulated and unregulated users. First, broker-dealers are currently capable of obtaining direct access to various exchange venues, subject only to their ability to incur the membership, connectivity and associated costs of that access. Second, broker-dealers are subject to rules and regulations governing virtually all aspects of their activity, including capital levels, risk controls, order marking and trading activity. To subject them to a second level of checks and controls by a sponsoring member (of which many, if not all, will be duplicative of the broker-dealer's own controls) strikes us as both unnecessary and inefficient. We would, however, welcome clarification in Rule 15c3-5 that the risk management controls articulated in the rule should be maintained by every broker-dealer, whether its market access is direct to the market or through a sponsor.

We do recognize the regulatory responsibility placed on sponsoring members for resulting trading activity under established rule sets, regardless of the status of those they sponsor. Accordingly, in the absence of requiring a secondary level of largely duplicative controls, it would seem both reasonable and appropriate that a sponsoring member be required to predicate its grant of sponsored access to broker-dealers on the right to certification and periodic audit of users' control infrastructures. We believe that such a certification and audit process would provide adequate assurances to the sponsor that each user of sponsored access has sufficient controls over its own activity to minimize any potential risk posed by that activity.

Once again, we thank the Commission for allowing us to comment on this proposal and, by extension, this important market structure issue. We would welcome the opportunity to provide further input on this issue and invite you to contact us should you wish to discuss our comments.

Very truly yours,

Sandor G. Lehoczky
Managing Director

cc: Mary L. Schapiro, Chairman, SEC
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