1/20/2012

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

RE: (Release No. 34-66065; File Nos. SR-BATS-2011-038; SR-BYX-2011-025; SR-BX-2011-068; SR-CBOE-2011-087; SR-C2-2011-024; SR-CHX-2011-30; SR-EDGA-2011-31; SR-EDGX-2011-30; SR-FINRA-2011-054; SR-ISE-2011-61; SR-NASDAQ-2011-131; SR-NSX-2011-11; SR-NYSE-2011-48; SR-NYSEAmex-2011-73; SR-NYSEArca-2011-68; SR-Phlx-2011-129)

Dear Ms. Murphy:

ModernIR appreciates the opportunity to comment on the proposed system of market-wide circuit breakers for circumstances of extraordinary volatility in securities markets. We are an analytics firm that provides mathematical market intelligence on trading behaviors to publicly traded companies.

One preamble: Public companies have not been included in these discussions in a coordinated fashion. Issuers should be surveyed for their views on transformational rules affecting exchanges and markets where their shares trade. The listing exchanges might lead that effort. Each could communicate with its listings constituency, summarizing proposals and requesting views.

Markets benefit from an orderly system for pausing activity during periods of marked uncertainty. But proposals thus far only hope to halt contagion, and offer no path for blunting aftershocks and restoring vibrancy. Avoided again is the elephant in the room: Current market structure crafted by rules is the root cause of systemic risk. To sustainably diffuse risk, the system must be disaggregated. Instead, recommendations thus far move the opposite direction – giving rise to grave concern.

The reason for risk of systemic contagion is the existence of a system. If a panic occurs at Safeway in the canned-goods aisle, it doesn't spread to the fresh-foods section at Kroger. No system links all grocery stores by law. But in trading markets, by rule, all SROs must be connected to facilitate compliance with Reg NMS rules. All protected quotes are automated, all order types conformed to Reg NMS protocols, all markets conjoined by order-routing requirements. We have created such a monstrosity that a metaphorical instance of minor varicosity could become an aortic aneurysm.

If a household appliance were to go awry, the logical response would be to unplug it. Why not create a process, simultaneous with market pauses, that disconnects markets and suspends Reg NMS bid/offer and trade-through rules after a Level 3 Halt? What should stabilize free, unimpeded markets – requisite language we paraphrase from The Act – is human thought – call it a natural nexus of fear and greed. We daresay that in today's automated, time-priority, maker-taker and payment-for-order-flow fueled trading markets, there is rarely if ever a natural nexus of fear and greed. Prices are contrived.

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Contrived prices are antithetical to capital-formation. Public companies strive to distinguish themselves. The premise behind trading publicly is to create value for shareholders through unique effort and achievement. This increasingly is a Sisyphean pursuit not because businesses are all the same but because market structure forces money to follow the crowd or arbitrage minute divergences.

The problem lies with using rules to pervasively prevent bad things, unwittingly fostering tail risk. It's analogous to fire-prevention practices in national forests decades ago. By stamping out natural cleansing mechanisms, forests were subjected to monumental and unnatural risk, producing catastrophic fires and sweeping beetle infestations.

In similar fashion, trading markets cannot heal themselves. And public companies derive no benefit from a synthetic environment that forces value money out and remands price-setting authority to transient intraday intermediaries.

Rules for crises should foster sustainable recovery, not shove lurking chasms under rugs. A Level 3 Halt could hand the Commission a golden opportunity to simplify a regulatory structure that arguably has wrought greater adverse consequences than the ones rules aimed to remedy.

Here's the opportunity: Suspend core trading rules in response to crisis. Objective: To attract money that cannot under existing rules enter markets with size and authority because intermediation instantly dissolves orders and pricing. If trading and investment take on greater vibrancy, the SEC has reason to permanently remove certain rules without compromising what we might call "pride of ownership" in the current rule-structure.

This is the elephant in the room – an architecture construed by arcane regulation rather than natural and free behavior coalescing around simple ground rules for all. What makes the vibrant interaction of millions of sentient beings engaged in sorting one person's treasures from another's trash a rigorously stable and vital enterprise is its lack of conformity.

Consequences? These steps may produce delays and disruptions in consolidated-tape data. Fine. Exchanges routinely deal with post-trade-processing issues involving massive electronic complex-trade executions and short volume. Some delay in TAQ data is a small price for encouraging robust price-discovery.

A concluding word on public perception: Imposing complex controls in markets will not instill the public with confidence. On the contrary, the populace at large may conclude that market function has become so byzantine, the fear of structural failure so great, that they stop participating. By contrast, regulations that look not only to prompt a market to "take a breath," but which also genuinely examine and let go of failed rules send the message that money should return.

That is the message we all – especially public companies – hope will be emphasized. The original purpose of The Act was to create a fair and unimpeded marketplace for capital formation. With proper preparation, the next inevitable crisis in trading markets may offer a path for return to the original purpose.

Yours very truly,

Timothy Quast
Managing Director