

**From:** Menchel, Marc  
**Sent:** Wednesday, November 30, 2011 06:02 PM  
**To:** Ramsay, John; Shillman, David S.; Sanow, Nancy J.  
**Cc:** Dumont, Stephanie; Russell, Racquel  
**Subject:** SR-FINRA-2011-058--FINRA Rule Proposal 6433

The purpose of this email is to address some concerns with respect to the process for the consideration of comments in the course of rule filings that has arisen in the course of the above referenced rule proposal.

In sum, the proposal reduces both the number of tier sizes for quoting in the OTC unlisted market and reduces the quotes size. The purpose of the filing could not be simpler: smaller quote sizes will allow for greater use of limit orders by investors.

In response to the filing come two comment letters: one by Knight Capital Group, Inc. and another by OTC Markets Group, Inc. Knight avers that the proposal will reduce liquidity because of the reduction of mandatory quotes sizes and increase trading and clearing costs because more transactions will be needed to accomplish executions. On its face the comment letter is curious because it does not answer the question as to why market participants would reduce their quote size simply because the rule proposal provides that option but doesn't mandate smaller quote sizes; especially if it is uneconomic to market participants to process smaller size orders. In addition the idea of additional costs to process more orders is similarly curious. The clearing business in securities is predicated on the fact that once a firm has sunk costs to clear transactions, the incremental cost of each additional transaction becomes negligible. Indeed, it is probably difficult for a firm to actually quantify the exact incremental dollar cost of clearing additional trades, but even ascertaining that fact would be of little import because Knight leaves out that a commission or mark-up (down) attaches to each trade that compensates Knight beyond its costs.

OTC Markets letter is somewhat disjointed: "[w]e strongly oppose the reduction of minimum quotation sizes...without any supporting economic analysis...that such a move will improve liquidity or lower transaction costs for the majority of investors." The unsupported assertion as to liquidity is questionable. As noted in our filing, lower quote sizes would allow for greater limit orders to be displayed. A potential greater number of limit orders increases price competition in the marketplace and we are unaware of any market in which greater competition has led to less liquidity. In NMS securities the role of the market maker has been radically reduced yet liquidity in NMS securities appear intact. It is hard to believe that allowing investors to better protect the pricing of their orders would dampen liquidity in the unlisted OTC Market. As to transaction costs, OTC Market raises an issue that has no nexus to the this rule filing, limit orders allows the investing public to control the prices at which they execute their transactions not their execution costs. FINRA's Mark-up rule governs the level of execution costs and its terms are unaffected by this rule. In any event, OTC Markets then asks an office of the SEC to undertake this economic analysis and we understand that RiskFin has decided to engage the request.

FINRA has engaged in the public comment process over course of its existence. We not only support its role in the federal securities laws but we routinely publish our rule proposals in Regulatory Notices seeking public comment before any filing with the Commission. Nevertheless, we think the question remains what is the standard of review by the Commission as to public comments? In this case, two commenters make unsupported, at points unrelated and somewhat vague comments that on their face raise questions and one of the commenters ask the Commission to do the commenter's homework. After all, no SRO is required to undertake an economic analysis of its rule proposals, but it is charged with not burdening competition with rules that are not in furtherance or in conformity with the Securities Exchange Act. FINRA takes that charge very seriously. Nonetheless, there is no statutory or Exchange Act Rule requirement to undertake an economic analysis because a commenter makes such demand and we are unaware of any requirement on the part of the Commission to oblige such commenters. Rather, it would seem that commenters should bear some burden beyond naked assertions that a rule would have a deleterious effect when those assertions are neither supported by reasoned argument and/or devoid of factual data.

In our conversations with Commission staff on this filing, FINRA was told that "people in the building are interested in this". We are certain that cannot be the standard for giving undue weight to comment letters such as these as that process would be ad hoc, an ad hoc process by definition is arbitrary and therefore unreasonable. But the even larger point here is that if we cannot move forward in the rule proposal process because of the vague and unsupported comment that some unintended consequences awaits us, then the bar for giving deference to comments is so low that the rule making process may be rendered futile. And the potential for that outcome is made worse when credence is given to such commenters' demands that an economic refutation is mandated to trump their ill-defined concerns. Of course FINRA will file a more formal responsive letter to the commenters' letters as this email is intended to address the larger issues noted here.