

Congress of the United States
House of Representatives
Washington, DC 20515

June 15, 2020

The Honorable Jay Clayton
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chairman Clayton:

We write you regarding our concern for the state of displayed bid-offer liquidity at the US national stock exchanges. It appears that the current COVID-related crisis dramatically exacerbated preexisting trends of declining liquidity to alarming levels. According to industry experts, the level of displayed liquidity fell by two-thirds in just two months.¹

This follows more than ten years of constant decline.² Overall, a market with less liquidity is a more volatile market so we are concerned with this downward trend and its impact on the everyday American investor. Many believe, and we share their concerns, that the business of market making, the posting of bids and offers, suffers from a lack of competition and is a driving factor behind the declining liquidity trend.

We ask that the Commission consider innovative, free-market efforts to increase competition in market making – to enable the equity markets to benefit from sufficient posted liquidity to function most efficiently, and thereby help protect investors and issuers from excessive volatility and pricing dislocations that may result if this problem persists or grows.

As one example, we see that the Investors Exchange has a proposal in front of the Commission that would encourage greater participation from market makers by protecting displayed bid-offer quotes from latency arbitrage, a practice that the FCA predicts costs market participants nearly \$5 billion dollars per year.³ Virtu, one of the largest market makers in the world, writes of the Investors Exchange proposal:

¹ Figure 5AB, p.8, U.S. Equity Liquidity in the COVID-19 Crisis, BestEx Research, March 31, 2020, available at <https://bestexresearch.com/wp-content/uploads/2020/04/BestEx-Research-Market-Impact-Analysis-20200331.pdf>

² Buying or Selling Stocks? It Isn't Always Easy, WSJ, January 20, 2020

³ <https://www.wsj.com/articles/ultrafast-trading-costs-stock-investors-nearly-5-billion-a-year-study-says-11580126036>

We believe that IEX's proposal is a highly innovative, market-based solution that will mitigate the negative effects of certain predatory trading behaviors that have been spawned by the latency arbitrage that exists in today's lightning speed markets.

Regardless of investment horizon, passive order protection at the National Best Bid and Offer benefits everyone. In particular, the IEX proposal would enable market makers who would otherwise be exposed to the risk of adverse selection to provide narrower spreads and larger quotes.⁴

This protective mechanism proposed by the Investors Exchange would allow a broader and more diverse group of market participants to contribute to the displayed quote and would be an effective way to reverse the decline.

In the comment file for this proposal we are encouraged to see a broad spectrum of institutional investors, pension funds, highly reputable broker dealers, as well as several electronic market makers all supporting the IEX proposal. There is a small neutral camp and limited outright opposition. This strongly favorable balance confirms the anticipated value of the proposal.

We strongly support this much needed innovation that directly seeks to repair weaknesses in the current market structure so that our equity markets can continue to lead in capital formation. If we allow our markets to adhere too closely to the status quo and we stifle innovation from disruptive private companies, we risk losing our advantage as the best and most efficient markets in the world.

Given these thoughts, please comment on all actions the Commission is taking to understand the apparent decline in posted liquidity, the Commission's current view of the drivers of this decline, and the actions currently under consideration to repair the problem. Please also share, to the extent possible, studies by the Division of Economic and Risk Analysis that speak to these concerns.

Thank you for your strong leadership and consistent focus on efficiency, competition and capital formation.

Sincerely,



Alex X. Mooney
Member of Congress



Lance Gooden
Member of Congress

CC: Commissioner Hester M. Peirce
Commissioner Elad L. Roisman
Commissioner Allison Herren Lee

⁴ <https://www.sec.gov/comments/sr-iex-2019-15/sriex201915-6670178-203870.pdf>