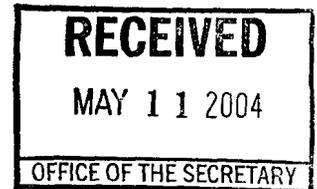


May 10, 2004

The Honorable William H. Donaldson
Chairman
United States Securities and Exchange Commission
450 Fifth Street, N.W.
Washington D.C. 20549



Re: Proposed Regulation NMS - File No. S7-10-04

Dear Chairman Donaldson:

We appreciate the opportunity to express our views and comments on the Commission's recently proposed Regulation NMS. At the outset, we commend the Staff and the Commission for this broad review and analysis of our securities markets in the context of an increasingly technological world. As the sponsor of an ECN we have particular interest in those aspects of Regulation NMS which relate to the access fees charged by ECNs and Market Makers. We believe the proposed changes are unwarranted and will have a deleterious effect on the market as a whole. Moreover, we believe that this aspect of the proposed regulation would also violate existing law. Accordingly, while we agree with and would support many aspects of the proposed regulation, we are constrained to oppose those aspects of the proposal which would fix access fees. Our specific comments follow:

Proposed Regulation NMS would violate the Exchange Act.

When the federal securities laws were amended in 1975, a hallmark of the changes to the Securities Exchange Act of 1934 (the "Exchange Act") was to ensure that competition existed at all levels of the securities industry. In part, this resulted in the elimination of fixed brokerage rates. However, almost as important to the investing public, the Exchange Act was amended (and particularly by the adoption of Section 11A) to require that there be fair competition at all levels of the securities industry, not merely among broker dealers.

Accordingly, so-called market responsibility rules of self-regulatory organizations were reviewed and limited and tying rules of markets to their captive clearing organizations eliminated. In fact, Section 11A required that the Commission consider, as a statutory goal, the encouragement

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of competition among new and emerging markets – specifically electronic markets. Regulation ATS, adopted under authority of Section 11A provides a regulatory framework to ensure that the operation. Since 1975, numerous electronic markets have developed. Competition among and between these new markets and established markets has produced a number of significant benefits to the investing public, including the narrowing of spreads and improved transparency within the “national market.”

It would be the height of irony were the Commission, under color of Section 11A effectively regulate the entire ECN industry out of existence by price fixing. It is inimical to the mandate of the Exchange Act for the Commission to adopt the predatory pricing methodology of traditional markets which existed prior to the 1975 Act Amendments for the purpose of creating fixed prices for marketplaces.

The Government Should Avoid Setting Rates, If Possible.

Beyond the questionable (as best) legal footing for this aspect of Proposed Regulation NMS is a matter of public policy: While the government regulates pricing in a handful of industries, conventional wisdom suggests that in a market economy, pricing regulation should be a tool of last resort. Even in areas where companies have a complete monopoly, the government has been headed toward deregulation in the last few decades, letting the marketplace dictate the rates. So it would stand to reason that the situation would have to be dire for the government to implement new pricing regulations.

The situation surrounding access fees and securities markets is not dire, however. ECN and other market fees have, in fact, dropped substantially over the last few years. Most recently, the fees have been capped at 3 mils by Nasdaq. There is no monopoly to fear; in fact, ECNs have cropped up and provided very healthy competition for Market Makers. Spreads are a fraction of what they were ten years ago, making a more efficient market that is better for investors, large and small. We find it hard to believe that the government feels the situation is so grave that it must come in and change the rules of the marketplace.

Removing “Rebate Traders” Means Removing Liquidity.

Capping the fee an ECN can charge at 1 mil effectively removes the rebate incentives which ECNs offer to attract so-called "Rebate Traders." Although they may be disparaged by community of so-called Market Makers, Rebate Traders play a role in the liquidity of the OTC marketplace, furnishing a measurable and significant percentage of the OTC market's volume. Market Makers furnish far less liquidity than they used to. When rebate traders no longer place their limit orders, spreads will no doubt widen considerably. This would be wonderful news for Market Makers but for no one else.

Capping Access Fees and Allowing Market Makers to Charge Will Doom ECNs

The SEC proposal has a double dose of bad news for ECNs—the capping of the fees and the determination to allow Market Makers to charge access fees. While we feel both changes are extremely unfair, we shall generally leave aside the issue of fairness and focus on the effects the marketplace will endure when ECNs go away. However, before leaving this topic, we must note that Market Makers, like any group of "dealers" in securities, make money by determining which securities to make markets in and where to set their markets. In short, they determine when to trade, in what volume and at what prices. If they make good business decisions, they profit. To provide all Market Makers with a regulatory lifeboat to protect them financially from their own bad business decisions appears to serve no public or regulatory purpose.

While everyone can argue about how quickly certain ECNs will perish and which ones will survive, it is beyond argument that the ECN landscape will change drastically if the proposal is adopted as is. Smaller ECNs, such as Track ECN, will almost certainly cease operations fairly quickly. Some of the larger firms may be able to hang on a while longer, doing far less volume than they do now.

We believe the net result of this changed landscape will be less competition for Market Makers and much larger spreads. It would be a return to the pre-1997 days when Market Makers felt confident that even with wide spreads, they would still attract appreciable volume and generate fat profits. Once again, this would be wonderful news for the Market Makers, and no one else.

On the other side of this entire argument, of course, are the people who argue that the changes proposed are necessary to prevent locked markets. We have a simple rebuttal to this argument. Even if you accept *arguendo* all the negatives attributed to locked markets, they are simply

not bad enough to warrant the regulatory actions proposed. The proposed cure and its side effects are far worse than the disease. Indeed, in certain circumstances, locked markets are a positive. For example, suppose a NASDAQ stock is locked at 24.50 x 24.50, rather than what would have been 24.50 x 24.51 if locked markets were prohibited. For the retail investor seeking to buy 1000 shares of this stock, a \$10.00 savings is realized. (ECN access fees and NASDAQ fees are already built into customer commission charges and would be the same regardless of the trade occurring at 50 or 51 cents.) The party that placed the offer at 24.50 did not intend to lift the bid at 24.50 and therefore would not were he forced to do so by placing a 24.50 offer. Accordingly, saying that the market is inefficient because these two trades fail to execute against one another is incorrect. And, a 24.50 sell from a 3rd party who is willing to lift the bid will still have the same opportunity as they would have had the market not been locked. There is no detriment to the bidding party. But, there is a benefit to someone seeking to buy the stock. Not only is there simply no downside, but there is an upside. So, despite generally accepted notions, locked markets can be good for the investor.

In summary, while we applaud the Staff and the Commission for this substantial review of current markets, we believe that proposed Regulation NMS would represent an untoward and statutorily unauthorized death knell for the ECN industry and would impose limitations on competition to the detriment of investors generally.

Thank you again for the opportunity to present our views on this important topic. If we can be of any assistance on this matter please contact Roderick Covlin, Executive Vice President of TrackECN at (718) 522.0222.

Sincerely yours,



Roderick Covlin
Executive Vice President

cc: Jonathan G. Katz, Secretary
The Hon. Cynthia Glassman, Commissioner
The Hon. Harvey J. Goldschmid, Commissioner
The Hon. Paul S. Atkins, Commissioner
The Hon. Roel C. Campos, Commissioner

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