THE BANK OF NEW YORK
NEW YORK'S FIRST BANK – FOUNDED 1784 BY ALEXANDER HAMILTON

ONE WALL STREET, NEW YORK, NY 10286

JOSEPH M. VELLI
SENIOR EXECUTIVE VICE PRESIDENT

January 26, 2005

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Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

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

Dear Mr. Katz:

The Bank of New York[1] ("BNY") appreciates the opportunity to comment on the Commission's reproposed Regulation NMS. As stated in our comment letter to the Commission's original proposal,[2] BNY strongly supports the Commission's goal of further strengthening the national market system. We focus here on the amended proposals related to a uniform trade-through rule (the "Trade Through Rule") and access fee limitations (the "Access Fee Cap").

We believe the Commission's reproposed Trade Through Rule addresses some of the shortcomings in the original proposal, for example, by focusing on automated quotes rather than automated market centers and by eliminating the opt-out exception, ensuring that automated quotes will be protected. We also support the amended Access Fee Cap,

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1 The Bank of New York is the oldest bank in the United States. It was founded in 1784 by Alexander Hamilton and was the first corporate stock to be traded on the New York Stock Exchange in 1792. Together with its parent company, The Bank of New York Company, Inc., The Bank of New York has a distinguished history of serving clients around the world through its five primary businesses: Securities Servicing and Global Payment Services, Private Client Services and Asset Management, Corporate Banking, Global Market Services, and Retail Banking. The Bank of New York Company, Inc. is a global leader in securities management services operating in more than 100 markets and servicing issuers, institutional investors and broker-dealers. The Company plays an integral role in the infrastructure of the capital markets safekeeping over $8 trillion in investor assets. Through its 23,000 employees, the Company provides quality solutions for global corporations, financial institutions, asset managers, governments, non-profit organizations, and individuals.

Over the past several years, The Bank of New York has greatly enhanced its brokerage and clearing capabilities through both targeted acquisitions and internal growth, and grouped these businesses in BNY Securities Group. This focused strategy is part of The Bank's continued efforts to provide clients with the resources and highly personalized service required to succeed in the investment marketplace. BNY Securities Group's core business lines include institutional agency brokerage, clearing and financial services outsourcing businesses. The broker-dealers within the Group have a total of 18 NYSE seats, over 1,300 institutional clients and over 1,000 correspondent clearing clients. We believe that, collectively, we are the largest institutional agency brokerage in the industry and, through Pershing LLC, the largest correspondent clearing organization in the industry.

2 Letter from Joseph M. Velli, Senior Executive Vice President, BNY, to Jonathan G. Katz, Secretary, Securities and Exchange Commission (June 30, 2004) *available at* http://www.sec.gov/rules/proposed/s71004.shtml.

proposed limitation on locked and crossed markets, will permit markets to compete without allowing access fees to distort market behavior.

1. Trade Through Rule

We believe a uniform trade-through rule of appropriate scope would enhance the transparency, efficiency and fairness of the national market system. A trade-through rule must balance the interests of investors of all types and market participants in a way that ensures our markets remain fair, robust, and innovative. In its reproposed Regulation NMS, the Commission has addressed many of the shortcomings in the original proposal. In this letter, we will respond to the Commission's requests for comment on the scope of trade-through protection.

Reproposed Regulation NMS contains two alternative proposals regarding the scope of protected quotations. Under the top of book alternative (the "TOB Alternative"), the best bid and offer ("BBO") of each exchange, Nasdaq and the ADF would be protected so long as such quotations are automated and accessible. The depth of book alternative (the "DOB Alternative"), on the other hand, would extend trade-through protection to all quotations that markets voluntarily disseminate in the consolidated quote. For the reasons set forth below, we believe the TOB Alternative would better balance the interests of investors and market participants, and would contribute to the long-term vitality of the national market system.

We believe non-marketable limit orders ("NMLOs") are the lifeblood of the national market system. Indeed, NMLOs provide the "market" for a security. Like a poker player unwilling to tip her hand, however, certain investors are concerned that displaying NMLOs transmits information about their intentions that can be used by others to their detriment. The Commission should adopt policies that encourage, but do not mandate, the use of NMLOs by mitigating the risks of information leakage. We also believe the Commission must provide incentives for market participants to continue to compete for NMLOs. The Commission, therefore, must strike a delicate balance to avoid the significant risk that the national market system becomes turgid and inflexible.

We believe the TOB Alternative provides the appropriate balance, at least as a starting point. Any investor whose interest represents the BBO of a major market center deserves to have that interest protected. Doing so will encourage investors to submit NMLOs. They will know that if their bid or offer is the best, it will be filled before inferior priced orders. The TOB Alternative will also encourage market centers to compete for NMLOs, using enhanced systems and services, because of the market-driven incentive to attract volume and, therefore, revenue.

The DOB Alternative, by contrast, suffers from two significant shortcomings. First, the DOB Alternative would transform the national market system into a monolithic bureaucracy. In the short term, we believe most market centers would react to customer demand by choosing to submit their depth of book for trade-through protection. For a time, investors would benefit by having all NMLOs protected by the Trade Through Rule. In the long term, however, the national market system would become a virtual central limit order book, something the Commission has for good reasons rejected in the past. Market centers would not have sufficient incentives to improve their systems or services beyond the minimum required by the Trade Through Rule. In other words, there would be no incentive to compete for NMLOs because every market center would, by regulation, provide the same service in the same way. Investors would be left with a fundamentally flawed market structure.

Second, the DOB Alternative simply is not feasible. It would require extensive study merely to identify the technological changes required to implement it. Market centers would have to collect massive amounts of quotation data and develop systems and connectivity to act on such data. We believe the costs of implementing the DOB Alternative, combined with the long-term detrimental effects noted above, argue strongly against its adoption.

2. Access Fee Cap

We reiterate our view that the Commission should encourage the development of strong unbiased linkages between all market centers. The combination of electronic connectivity and market incentives to compete for NMLOs serves the best interests of investors. Market centers should be free to charge for access so long as they do not unreasonably impair investors' ability to obtain best execution. The reproposal to cap access fees at $.003 per share seems consistent with these objectives.

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We appreciate your consideration of BNY's positions. Please contact the undersigned if you would like further information.

Very truly yours,

Joseph M. Velli

cc: Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
Commissioner Harvey J. Goldschmid
Annette L. Nazareth
Robert L.D. Colby