MEMO# 28967

May 12, 2015

ICI Letter on Issues To Be Discussed at SEC Equity Market Structure Advisory Committee Meeting

[28967]

May 11, 2015

TO: EQUITY MARKETS ADVISORY COMMITTEE No. 8-15 RE: ICI LETTER ON ISSUES TO BE DISCUSSED AT SEC EQUITY MARKET STRUCTURE ADVISORY COMMITTEE MEETING

The SEC will hold the first meeting of the newly formed Equity Market Structure Advisory Committee on Wednesday, May 13. The meeting will focus on Rule 611 of SEC Regulation NMS, i.e., the "Order Protection Rule" or "Trade Through Rule." ICI filed a letter in advance of the meeting; the most significant aspects of the letter are summarized below.

I. Trade Through Rule

The letter continues to support a trade through rule for the equity markets. The letter acknowledges that since its adoption, Rule 611 may not have achieved all of its objectives, particularly rewarding the display of limit orders by increasing their likelihood of execution. Nevertheless, the letter states that ICI does not see the benefit to investors, and the equity markets in general, of eliminating the trade through rule and permitting the execution of trades on one venue at prices that are inferior to publicly displayed quotations on another venue.

The letter also do not agree with some of the criticisms placed on Rule 611, particularly that the trade through rule alone has harmed institutional investors that need to trade in large size by forcing them to access small-sized quotations and thereby signal their trading intentions to short-term proprietary traders. The letter states that a number of market structure developments since Rule 611's adoption have contributed to institutional investors accessing small-sized quotes and that placing the blame on the trade through rule alone would be unfair.

Finally, the letter states that given the significant changes to the structure of the equity markets since the rule was adopted, certain modifications to the trade through rule may be warranted or, at the very least, worthy of examination. Specifically, the letter states that ICI would support linking protected quotation status under the trade through rule to a certain volume threshold.

II. Liquidity Rebates and Access Fees

The letter states that the issues surrounding Rule 611 cannot be viewed in a vacuum and that any changes to the trade through rule must be looked at in the context of conflicts of interest that exist in the markets when orders are routed, particularly those surrounding liquidity rebates and access fees. Specifically, if the current incentives for making routing decisions based on the availability and amount of liquidity rebates offered, and access fees charged, by trading venues are reduced or eliminated, a number of benefits to the markets would be brought to bear.

The letter continues to recommend that the SEC work with market participants to establish a pilot program where a certain set of securities would be prohibited from being subject to liquidity rebates. The letter also supports a corresponding examination of, and reduction in, access fees.

III. Locked and Crossed Markets

The letter notes that in the context of examining Regulation NMS, some have suggested that rules prohibiting locked and crossed markets should be eliminated. The letter continues to support rules that reduce the incidence of locked and crossed markets. The letter states that locked and crossed markets can have a negative impact on the securities markets and can be a sign of an inefficient market structure. The letter also notes that many incidences of locked and crossed markets can be attributed to the proliferation of access fees and liquidity rebates. Therefore, if the SEC were to address the issues surrounding access fees and rebates, many of the issues relating to locked and crossed markets would be eliminated and an elimination of the prohibition on locked and crossed markets can be revisited.

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Attachment
