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May 5, 2015

Ms. Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, N.W.
Washington, D.C. 20006-1506

> Re: Regulatory Notice 15-06

Dear Ms. Asquith:

IEX Services LLC ("IEX") is pleased to provide comment on Regulatory Notice 15-06, which generally proposes to require that persons primarily responsible for the design, development, or significant modification of equity algorithmic trading strategies or for supervision of such activities be registered with FINRA as an equity trader ("the Proposal"). IEX endorses the proposal and believes it will better help to ensure that persons involved in these increasingly important functions are fully aware of and educated in the regulatory and compliance implications of algorithmic trading. As discussed below, we suggest that FINRA clarify two issues of application of the proposal.

Background

As FINRA notes in the Proposal, algorithmic trading strategies have assumed a critical and growing importance in today's trading markets. Algorithmic trading is especially important to handling orders of institutional investors, in order to try to limit information leakage about large-sized orders and to navigate the allocation of such orders among the existing multitude of exchange and alternative trading venues. The way that algorithms are used also is important to the satisfaction of broker-dealers' best execution responsibilities and can be important to institutional clients in exercising effective direction over how their orders are handled.

Further, experience has shown the significant risks that can arise from improperly designed or implemented algorithms, both in terms of risk management of broker-dealers' market exposures, as well as their compliance with regulatory obligations. IEX believes that the Proposal if adopted would serve as a useful complement to SEC Rule 15c3-5, which concerns the risk management of so-called "direct market access" arrangements, and which is also heavily focused on financial and regulatory risks from algorithmic trading strategies.[1] The

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[1] See Securities Exchange Act Release No. 63241 (November 3, 2010), avail. at www.sec.gov/rules/final/2010/34-63241.pdf, at 8-11.

Proposal would also be consistent with and complementary to Chair White's call for measures to enhance firms' risk management of trading algorithms generally.[2]

However, enhanced risk management controls will not by themselves assure that algorithms are constructed and implemented in ways that achieve compliance with legal and regulatory requirements. Apart from helping to assure compliance with specific regulatory requirements, such as Regulation NMS or Reg SHO, registration may also help to limit the potential that algorithms will be used in ways that result in manipulation of prices.[3] FINRA members are, of course already required to implement policies and procedures that are reasonably designed to assure compliance with securities laws and regulations but, as in many other areas, requiring that individuals directly involved in key aspects of the securities business meet training and continuing education standards can help to better accomplish that goal.

Requests for Clarification

IEX recommends that FINRA clarify the scope and application of the proposal in two specific contexts. The first of these relates to the application to order routers and routing strategies. In the Proposal, FINRA states that the term "algorithmic trading strategy" would be deemed to cover "any program that generates and routes (or sends for routing) orders (and order-related messages, such as cancellations) in securities on an automated basis." Specifically with respect to order routing, FINRA states that the Proposal would cover "order routing strategies used to determine the price, size and destination for routed orders, the use of 'parent' and "child' orders, and displayed versus non-displayed trading interest". However, FINRA further states that "an order router alone would not constitute an algorithmic trading strategy; for example, a standard order router that routes retail orders designed to comply with best execution and be Regulation NMS compliant would not be an algorithmic trading strategy. Nor would an algorithm that solely generates trading ideas or investment allocations, but that is not equipped to automatically generate orders and order-related messages to effectuate such trading ideas into the market...."[4]

IEX recommends that FINRA better clarify the application of the Proposal to order routers. For example, the "smart order router" that IEX makes available to subscribers routes orders

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[2] "Enhancing Our Equity Market Structure", Address by Chair Mary Jo White at the Sandler O'Neill & Partners, L.P. Global Exchange and Brokerage Conference (June 5, 2014, avail. at http://www.sec.gov/News/Speech/Detail/Speech/1370542004312,: "I have further instructed the staff to prepare recommendations for the Commission to improve firms' risk management of trading algorithms and to enhance regulatory oversight over their use. Given the overwhelming dominance of trading algorithms, it is time that our regulatory regime is updated to take better account of the risks when they are poorly designed or operated."

[3] See, e.g., In the Matter of Athena Capital Research, LLC, Securities Exchange Act Release No. 73369, October 16, 2014, avail. at www.sec.gov/litigation/admin/2014/34-73369.pdf, concerning the manipulation of prices through trading in response to closing imbalance messages in various Nasdaq-listed stocks.
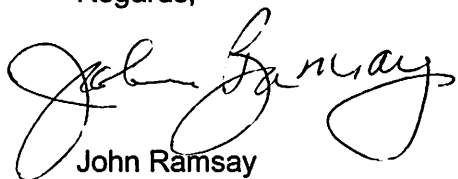
[4] FINRA Regulatory Notice 15-06 (March 2015), at 3-4.

received from subscribers in whole or through "child" orders to various exchanges based on objective factors that determine the best sources of liquidity for a particular security at a moment in time.[5] If the intent is to capture a router of this type, we would not object, but in either event, we believe that the intent should be clarified in a Regulatory Notice if and when the rule change is adopted.

We also recommend that FINRA clarify the application of the Proposal to supervisors. The Proposal by its terms would apply to persons "primarily responsible for the design, development, or significant modification of an algorithmic trading strategy...." and to persons who supervise such activities. With respect to supervisors, the Proposal states that a "senior or lead developer's supervisor would not be required to be registered under the proposal if that person is not involved in the day-to-day supervision or direction of the development process" – for example where the lead developer reports to the firm's Chief Technology Officer.[6] IEX agrees with the apparent intent of this language, i.e., that only persons directly engaged in algorithm design and development should be required to register and that senior-level supervisors who are removed from ongoing or daily supervision of algorithm design and development should not be required to register. IEX recommends that this intent be more clearly reflected in the rule text itself – specifically, that subparagraph (B) be revised to apply to persons "(ii) responsible for day-to-day supervision or direction of such activities."

Please feel free to contact the undersigned at 646.569.2366 if you have any questions concerning these comments.

Regards,

John Ramsay
Chief Market Policy Officer, IEX

Cc: Richard Ketchum, Chairman and Chief Executive Officer
        Robert L.D. Colby, Chief Legal Officer

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[5] As a result, IEX is able to obtain fill rates for orders routed in this way to approximately 98%.
[6] FINRA Regulatory Notice 15-06 (March 15) at 5 and footnote 9.