



Securities Industry Association

1401 Eye Street, NW • Washington, DC 20005-2225 • (202) 296-9410, Fax (202) 296-9775

November 21, 2001

By Hand and Via Electronic Mail

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

Re: SEC Concept Release: Request for Comment on the Effects of Decimal
Trading in Subpennies [Securities Exchange Act Release No. 44568; File
No. S7-14-01]

Dear Mr. Katz:

The Securities Industry Association ("SIA")¹ is pleased to provide the U.S. Securities and Exchange Commission ("Commission") with comments regarding the impact on the U.S. securities markets and investors of trading and potentially quoting equity securities in an increment of less than a penny ("subpenny"), as requested in the above-referenced concept release ("Concept Release").²

The minimum price variation ("MPV") for consolidated quotations in equity securities became a penny when the securities industry completed its conversion from fractional to decimal pricing on April 9, 2001.³ Some market centers, however, are

¹ The Securities Industry Association brings together the shared interests of nearly 700 securities firms to accomplish common goals. SIA member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift, and pension plans, and generates \$358 billion of revenue. Securities firms employ approximately 760,000 individuals in the United States. (More information about SIA is available on its home page: <http://www.sia.com>.)

² Securities Exchange Act Release No. 44568 (July 18, 2001). The original deadline for submitting comments, September 24, 2001, was extended until November 23, 2001 in light of the September 11, 2001 terrorist attacks and disruption to the U.S. securities markets. See Securities Exchange Act Release No. 44845 (September 26, 2001).

³ The Commission ordered the national securities exchanges and the National Association of Securities Dealers, Inc. ("NASD") to complete the conversion to decimal pricing by April 9, 2001, and to individually or jointly submit a report to the Commission on the impact of decimal pricing on their market's systems capacity, liquidity and trading behavior by June 8, 2001. See Securities Exchange Act Release No. 42914

trading in increments of less than a penny pursuant to Commission-approved pilot programs or no action letters.⁴ In the Concept Release, the Commission questions whether the use of different price increments for trading and quoting securities by market participants causes confusion for investors and securities professionals and adversely impacts market transparency, the operation and effectiveness of Commission and self-regulatory organization (“SRO”) rules that are dependent on trading or quoting price differentials, and automated systems.⁵

In exploring these questions, SIA member firms took into account the impact of decimalization on investors and the U.S. securities markets. Although the conversion to decimals was accomplished smoothly and has provided certain benefits, member firms believe that there also have been a number of adverse consequences for the securities industry and investors. Firms considered all of these factors in formulating their conclusions on the use of subpenny increments.

Executive Summary

The consensus of SIA member firms is that the Commission should not permit the trading (for purposes of this letter, this term refers to the pricing of orders and trades) of equity securities in subpenny increments, and that the Commission or Congress should establish a MPV for the trading and quoting of equity securities that is not less than a penny.⁶ At least one member firm does not oppose the use of subpenny increments in the trading or quoting of equity securities.

Most SIA member firms believe that the trading and quoting of equity securities in subpenny increments would undermine the benefits of decimalization by causing confusion for investors and securities professionals in the purchase and sale of equity

(June 8, 2000). This latter date was extended on May 22, 2001 by Commission order until September 10, 2001. See Securities Exchange Act Release No. 44336 (May 22, 2001) (“Commission Order of May 22, 2001”).

⁴ The Nasdaq Stock Market, Inc. (“Nasdaq”) market makers, Chicago Stock Exchange (“CHX”) specialists and market makers, and certain electronic communication networks are handling orders in subpenny increments while quotations are maintained in penny MPVs without rounding indicators, pursuant to certain parameters approved by the Commission that preserve the benefits of certain Commission rules. Of note is the fact that subpenny pricing is not that prevalent in the industry overall. The Commission’s Concept Release points out that the Commission’s Office of Economic Analysis found that “subpenny prices accounted for approximately 5.7% of the trades and 4.2% of the dollar volume in [Nasdaq securities]” for the week of April 9-12, 2001. (See page 3 of the Concept Release.) The Commission also noted in the Concept Release that the percentage of subpenny trading appears to be minimal for exchange-listed securities. (See footnote 9 in the Concept Release.)

⁵ Of note is the fact that CHX has stated that “...it does not generally consider the benefits of subpenny trading to outweigh the possible risks and shortcomings articulated by the Commission in its [Concept Release]...” CHX further explains that it sought the Commission’s approval of its pilot program to engage in subpenny trading only for competitive reasons. Letter from Paul B. O’Kelly, Chief Operating Officer, CHX, to Jonathan G. Katz, Secretary, Securities and Exchange Commission, dated September 24, 2001.

⁶ Several member firms in this group believe that there should be an exception for average price calculations that extend beyond two decimal places. In addition, some firms suggest that the Commission consider an exception permitting subpenny trading for non-Nasdaq securities that trade for less than a dollar.

securities, and would not contribute to the maintenance of stable and orderly markets as called for by our national market system.⁷

The consensus of SIA member firms is that using a minimum increment of less than a penny for the trading or quoting of equity securities would contribute to the adverse effects on our markets brought on by the conversion to decimal pricing. Specifically, SIA member firms believe that the use of subpennies would:

- o adversely impact market transparency, particularly by:
 - contravening decimal pricing's goals of providing greater simplicity and clarity in the purchase and sale of securities, and of harmonization of pricing among U.S. markets and globally;
 - contributing to the incidence of "flickering" quotes, which makes it difficult for broker-dealers to comply with best execution responsibilities and impacts other market rules;
 - contributing to the production of less meaningful quotes, and decreased market depth and liquidity;
- o adversely impact certain order priority rules that govern which orders are filled first in our markets;
- o encourage the practice of "stepping-ahead" and other strategies that take advantage of a very small price increment, thus causing further reduction in the display of customer limit orders and liquidity;
- o make it more difficult to comply with existing short sale regulations due to the significantly more frequent quote updates; and
- o cause firms to expend considerable funds, efforts and staff time to redesign automated systems (for internal operations, screen displays, and capacity) with no real benefit to investors or the U.S. securities markets.

Background

In discussing this Concept Release with member firms, several firms commented that the SROs also found that decimalization had produced certain adverse consequences for the securities industry and investors. The SRO findings are included in their reports on the impact of decimal pricing submitted to the Commission in September.

In general, the SROs found that the conversion to decimal pricing had an adverse impact upon market transparency, dramatically reduced quotation and effective spreads in both exchange-traded and Nasdaq securities, increased the number of quotations (although without as much volatility as expected), and decreased display size. The SROs also believe that there has been a significant drop in the display of limit orders and in

⁷ See S. Rep. 94-75, 94th Cong. 1st Sess. 7 (1975).

liquidity and that, overall, securities professionals find it more difficult to execute large trades.

Several SROs believe that, in the long run, decimalization could have significant negative effects on automated systems and investors, and that there will be greater transaction costs to investors. Finally, most of the SROs recommend in their reports that the minimum trading and quoting increment remain at least at a penny. The SROs are required by the Commission to submit rule filings by January 14, 2002 to establish their MPVs for quoting equity securities and options on their markets.⁸

Discussion

Most SIA member firms believe that trading and quoting in subpenny increments would not contribute to the maintenance of stable and orderly markets, a primary objective of Congress in mandating the national market system. Although the conversion to decimals did bring certain benefits to investors and the U.S. securities industry, member firms believe that the adverse effects of permitting the use of subpennies would outweigh any additional benefits to be derived.

A. Impact of Subpenny Trading on Transparency

As the Commission noted in the Concept Release, "...market transparency plays an essential role in linking dispersed markets and improving the price discovery, fairness, competitiveness, and attractiveness of U.S. markets." SIA member firms believe that the trading and quoting in subpennies would have an adverse impact on this critical component of the U.S. securities markets. They provide the following, specific comments on this point:

Price Clarity: By mandating decimal pricing, legislators and regulators sought to bring greater clarity and simplicity to the process of purchasing and selling securities. Investors can readily understand consolidated quotes based on dollars and whole pennies as opposed to fractions, and can easily compare prices among U.S. market centers and globally. The consensus of member firms is that subpenny pricing in the trading and quoting of securities would seriously undermine these goals, and that the lowest increment should be not less than a penny.

Accurate Quotes: If subpenny orders are placed and available for execution, the consolidated quotation should ideally reflect such orders in order to be completely accurate and to reflect the true trading interest in the market. As mentioned earlier, some market centers are currently accepting orders in subpenny increments, but are not reflecting them in their quotations pursuant to Commission-approved programs. Most member firms would prefer that the pricing of orders be in increments of not less than a penny, which would produce more accurate quotations if the quoting increment is the

⁸ Commission Order of May 22, 2001. On September 25, 2001, the Commission extended the original deadline of November 5, 2001 for submission of these rule filings until January 14, 2001. See Securities Exchange Act Release No. 44846 (September 25, 2001).

same MPV. Although member firms explain that it is not impossible to redesign their systems to include subpennies in the quote, they strongly believe that it would be impractical to do so and that such efforts would not provide any real benefits to investors or our securities markets.

Flickering Quotes: SIA member firms state that quoting in decimals has contributed to rapidly changing quotations, commonly referred to as “flickering” quotes. This phenomenon makes it difficult for firms to comply with their best execution obligations because the quotes are essentially inaccessible. Member firms believe that, if subpennies were used in the quote, this problem would dramatically worsen. Flickering quotes also impact other market rules, particularly those quoting and trading rules based on meaningful quoting increments.⁹

Market Depth and Liquidity: Since the conversion to decimals, member firms have experienced dramatically narrowed spreads, a decrease in market depth, and more trades being executed outside of the national best bid and offer (“NBBO”).¹⁰ Market professionals find it more difficult to determine market depth at or near the NBBO and therefore how long it will take to complete an order.¹¹ The NBBO, consequently, has become less effective in reflecting true trading interest.

One of the Commission’s stated goals for the national market system is to encourage “...the deepest, most liquid markets possible...”¹² Member firms are concerned that subpennies would not further this goal, and instead reduce market liquidity even more. As one firm noted, if the industry used subpenny increments out to four decimal places, there will be 10,000 price points in a dollar. Under this scenario, its customers would undoubtedly receive more multiple fills at multiple prices with multiple confirms. This firm believes that, as a result, their customers may be surprised by the price(s) they receive when buying or selling securities, which could reduce their confidence in the fairness of the markets.

⁹ These rules include those pertaining to “locked” and “crossed” markets and the Intermarket Trading System Plan’s “trade-through” provisions.

¹⁰ We note that one SIA member firm, Midwood Securities, submitted a separate comment letter to the Commission in response to the Concept Release that contained the results of a survey they conducted of senior traders at more than 600 institutional investment management firms. Midwood reported that more than 15% of those surveyed responded, with the overall conclusion that decimalization had adversely impacted market liquidity and transparency and, in turn, negatively affected execution quality. Midwood also reported that a large number of those responding have altered their trading strategies because of decimalization, that the respondents saw greater volatility, and that more than half of the respondents reported an increase in trading costs. Letter from Terry L. March, President and CEO, Midwood Securities, Inc., to Isaac Hunt, Commissioner, Securities and Exchange Commission, dated October 11, 2001 (“Midwood Letter”).

¹¹ Some market centers, such as the New York Stock Exchange, Inc. (“NYSE”) and Nasdaq, have taken steps to provide more information on market depth. The NYSE has recently attached a depth indicator to quotations that notes the presence of liquidity a few MPVs away from the NBBO. Nasdaq’s SuperMontage is planning to display three levels of quotations instead of just the NBBO.

¹² Securities Exchange Act Release No. 43084 (July 28, 2000).

Although narrower spreads and lower transaction costs were one of the expected benefits of decimal pricing, member firms believe that any added benefits to be derived from a further narrowing of spreads would be outweighed by certain negative consequences to the stability and efficiency of our markets and investors.

Rounding and Inclusion Scenario, and Related Questions #1-14: The Commission asked in the Concept Release for commentators to address two scenarios, the Rounding and Inclusion Scenarios, and related Questions #1-14 if they believe the exchanges and Nasdaq should accept orders in subpenny increments. Because the consensus of SIA member firms is that orders in subpenny increments should not be accepted, responding to Questions #1-14 is unnecessary.

Rounding Scenario: If the exchanges and Nasdaq accept orders in subpenny increments, should they round the quotations to display the orders in whole penny increments?

Inclusion Scenario: Alternatively, if the exchanges and Nasdaq accept orders in subpenny increments, should they display consolidated quotes in subpenny increments?

SIA member firms believe that the exchanges and Nasdaq should not accept orders in subpenny increments; therefore, neither scenario should be implemented in the interests of furthering market transparency.

If the exchanges and Nasdaq accepted orders in subpenny increments but the quotes were still in penny increments, quotations displaying the orders would have to be rounded. Firms, however, are concerned that rounding would not contribute to market transparency and may cause display difficulties, particularly for market data vendors. Although it is possible to place a rounding indicator on quotes that have been rounded (similar to the indicator placed on average price trades), discussions with member firms indicate that clarity and simplicity in quotes should prevail over accepting orders in subpennies and using rounding indicators.

If orders are accepted in subpenny increments, member firms do not believe that consolidated quotes should be displayed in subpenny increments. Such quotations may be technically possible and would reflect the market's true trading interest, but it would be impractical and confusing to include numerous decimal places in quote displays, both electronically and on paper, and most likely cause systems and capacity difficulties.

B. Order Priority

Member firms believe that the use of subpenny increments would have a negative impact on certain priority rules that govern which orders are filled first in our securities markets. As the Commission notes in the Concept Release, “[h]istorically, traders were required to make an economically significant contribution to the price of a security to

gain priority over other traders.” The Commission raises two questions relating to this issue:

Question 15. Should there be a minimum trading increment that requires a trader to make an economically significant change to the quoted price of a security in order to obtain priority over another order? If so, what should that increment be? Should all market participants be subject to the same trading increment?

Member firms believe that, to obtain priority over another order, a trader should be required to improve on a quoted price of a security by a minimum trading increment of at least a penny. There is already concern in the industry that even a penny is not sufficient price improvement. All market participants should be subject to this same trading increment to eliminate confusion and promote fair competition.

Question 16. Should the minimum increment used to establish priority over other orders be dependent upon the security price or quotation spread?

To ensure simplicity and uniformity in transactions, member firms believe that the minimum increment used to establish priority over other orders should be the MPV, which should be not less than a penny.

C. Effects of Subpenny Trading on Other Price Dependent Rules

Member firms believe that subpenny trading would negatively impact certain Commission and SRO price dependent rules, particularly those that offer protection of customer limit orders and regulate short sales.

1. Customer Limit Order Protection

The customer limit order protection rules offer protection for customer limit orders by giving them priority over specialist and market maker orders at the same price on the exchanges and on Nasdaq.¹³ The Commission has recognized since 1975 when Congress mandated the national market system that the display of limit orders was an important component of this system.¹⁴

For most market centers, the minimum price increment to trade ahead of a customer limit order is a penny.¹⁵ Member firms have found, however, that decimal pricing has discouraged the display of limit orders because of the added risks of “pennying” or “stepping-ahead,” which has in turn reduced liquidity. Although some market centers are introducing systems that encourage the display of limit orders,¹⁶ firms are concerned that trading in subpenny increments would contribute to the decline in the display of limit orders and thus liquidity.

¹³ 17 CFR 240.11a1-1(T). See also NYSE Rule 92(b) and NASD IM-3220-2.

¹⁴ Securities Exchange Act Release No. 37619A (August 29, 1996).

¹⁵ For those market centers discussed in footnote 4, the stepping-ahead increment is a subpenny for certain orders.

¹⁶ For example, the NYSE is proposing its OpenBook service to provide additional limit order information. See Securities Exchange Act Release No. 44962 (October 26, 2001).

The Commission requested comment on the following questions:

Question 17. *Is price improvement by less than \$0.01 an economically sufficient amount for specialists or market makers to be able to "step-ahead" of customer limit orders? If not, what amount of price improvement would be considered economically sufficient in order to "step-ahead" of a customer limit order?*

Most SIA member firms believe that specialists or market makers should not be able to “step-ahead” of customer limit orders at an increment that is less than a penny, and that price improvement by an increment of not less than a penny would be economically sufficient for “stepping-ahead” of such orders.¹⁷

Question 18. *Should the minimum price improvement increment for "stepping-ahead" be dependent upon the minimum trading or quoting increment in a market? If so, how should this minimum increment be determined? Alternatively, should the "stepping-ahead" increment be dependent upon the security price or quotation spread?*

According to member firms, the minimum price improvement increment for “stepping-ahead” should be dependent upon the minimum trading *and* quoting increment in a market, which should be a uniform, consistent, increment of not less than a penny.

Question 19. *Who should the "stepping-ahead" minimum increment apply to, e.g., specialists, market makers, floor brokers, or other market participants? Would imposing a minimum "stepping-ahead" increment on these individuals benefit non-professional customers?*

SIA member firms believe that the “stepping-ahead” minimum increment should apply to all market participants, and that non-professional customers would benefit from this uniformity.

Question 20. *If "customer first" provisions continue to incorporate the minimum pricing increment in each market, will customers seek alternative means of displaying their orders to avoid "stepping-ahead" activity or will they use automated systems which do not display orders? Will these reactions cause or result in greater market fragmentation, i.e., the trading of orders in multiple locations without interaction among those orders? Will customer responses differ between market structures?*

SIA member firms believe that all market participants should be subject to the same minimum trading increments to avoid market fragmentation. Disparate provisions would lead to greater fragmentation and not contribute to market efficiency.

2. Effect of Trading in Subpennies on Short Sale Regulation

¹⁷ Of note is the fact that the Midwood Letter reported that “[s]ome 60% of those responding believe that \$.05 should be the minimum price improvement required for specialists and market makers to outbid a limit order.”

The SIA understands that the Commission has been reviewing the short sale rule, Rule 10a-1, to determine whether it should be revised or repealed.¹⁸ Accordingly, the SIA has discussed short sale regulation with its member firms on several occasions over the past few years to ascertain their views. Some SIA member firms believe that the rule may still serve a useful purpose, but perhaps should be revised to provide greater flexibility. Other firms question whether the short sale rule is still necessary, and suggest that the rule's original regulatory and market surveillance objectives can be met either through existing Commission anti-fraud and anti-manipulation rules or through the vast array of sophisticated regulatory and market surveillance mechanisms prevalent in today's markets. SIA member firms, in general, advocate that any revised short sale rule not further complicate a firm's ability to comply and that it apply uniformly to all market participants and to all securities.

The Commission requested comment on the actual or potential impact of subpenny trading on short sale regulation, as follows:

Question 21. Would short sale rules that operate off a minimum price increment, such as Rule 10a-1 and NASD Rule 3350, be less effective if the minimum up "tick" or up "bid" required were less than a penny? If so, would these rules be sufficient to protect investors?

Question 22. Should the minimum price increment used for short sale regulation be dependent upon the minimum trading or quoting increment? If so, how should this minimum increment be determined? Alternatively, should the increment used for short sale regulation be dependent upon security price or quotation spread?

Question 23. Would subpenny trading increase the frequency of price changes, i.e., rapid trade and quote changes, and make it more difficult to effect a short sale on the proper "tick" or "bid?" If so, what steps should be taken to address the problem?

SIA member firms believe that, because a MPV of less than a penny would result in significantly more frequent quote updates and substantially increase the universe of prices at which transactions in listed securities could occur, compliance with the bid and tick tests would become more difficult. Although automated trading systems have enhanced the trading abilities of many market participants, it remains difficult for traders to effect short sales, either on behalf of clients or for proprietary accounts, in volatile markets. Flickering quotes and prints make it nearly impossible in some instances for a human trader to determine the appropriate point at which a legal short sale may be effected.

¹⁸ The NASD has its own short sale rule, Rule 3350, which prohibits short sales by NASD members in Nasdaq National Market securities at or below the current best bid as shown on the Nasdaq screen when that bid is lower than the previous best bid (this is commonly referred to as the "bid test" as distinguished from the "tick" test under Rule 10a-1). A short sale, therefore, must be effected at a price at least \$0.01 above the current best bid in a declining market.

SIA member firms recommend to the Commission, therefore, that it maintain consistency between the MPV for trading and quoting securities and the minimum increment used for short sale purposes, as this would be the most effective approach because of its ease of application. Most especially, member firms recommend that the minimum increment used for short sales not vary on a security-by-security basis depending upon price, spread, or other metric, as it would be more difficult for market participants to understand and comply with the short sale rule.

D. Automated Systems Issues

When the industry converted to decimal pricing for equity securities and options, no significant problems were experienced by major broker-dealers, the securities markets, clearing organizations, or vendors with their automated systems or capacity. Some firms note, however, that trading volumes contracted in the past year due to the slowdown in the economy. These firms believe that the industry's trading systems and networks have not fully tested the conversion to decimals, and are concerned about the impact of decimal pricing in a normal-to-high volume period. Firms also believe that Nasdaq's SuperMontage and the NYSE's OpenBook systems must be taken into account when analyzing present systems and capacity, as these new systems could greatly increase message traffic rates when implemented.

In order to address specifically the Commission's questions relating to automated systems, the SIA conducted an informal survey of member firms, SROs, clearing organizations, and vendors to determine the industry's readiness to trade and quote securities in subpennies. The views of these entities are summarized below; their opinions relate to the following narrow set of questions and should not be interpreted to mean that they advocate the use of subpennies. It is also our understanding that many of the non-member firm participants in the survey may be responding separately to the Commission's Concept Release.

Question 24. Are the automated systems at the exchanges, Nasdaq, the clearing organizations, broker-dealers, and vendors currently capable of handling trading, reporting, or quoting stocks and options in subpennies? If not, how long would it take to prepare these systems for subpennies?

Question 25. If system changes need to be made to accommodate subpenny trading, reporting, or quoting, what types and scope of changes would need to be made (e.g., hardware and software) and how much time would be required? What are the associated costs and benefits?

Question 26. What is the anticipated impact on industry systems capacity associated with trading, reporting, or quoting of stocks and options in subpennies?

The participants in the SIA informal survey indicated that, during the conversion to decimals, most market participants made adjustments to their automated systems and capacity that could, to varying degrees, accommodate the use of subpennies. For those

participants that would need to expand their systems and capacity, it was estimated that it would take them anywhere from six months up to two or three years to do so.

Most SROs stated that their automated systems could handle four-to-six decimal places and, in one case, even twelve decimal places. Most, however, believe that, if subpenny increments were permitted, there should be a limit on the number of decimal places used and that four-to-six decimal places would be best. With regard to capacity, some SROs indicated that they would have to expand. Finally, regarding display systems, several SROs offered that they are not ready to handle multiple decimal places; moving beyond two decimal places would require major systems redesign in their display and peripheral systems that would take some six-to-24 months.

Vendor representatives stated that their display capabilities vary, with four decimal places being the more common barrier but some being limited to displaying two or three decimal places. Capacity is also an important concern of vendors. One vendor explained that they are particularly worried about the advent of SuperMontage because, unlike with Options Price Reporting Authority traffic where they have many opportunities to filter out data considered unnecessary, there may be no filtering possibilities with SuperMontage. As a result, the message rates per second with SuperMontage will be a real issue. One service bureau stated that they can handle four decimal places; anything beyond that would require major systems redesign.

SIA member firms also described different capabilities. Many firms' automated systems already have the capability to handle subpennies up to four-to-six decimal places; however, their systems would probably have to undergo a major redesign if subpennies are used beyond four-to-six decimal places – particularly with regard to screen display. Overall, these firms believe that subpenny increments would have a significant, additional impact on trading systems and industry networks, including the affirmation and clearing systems. The general consensus of member firms, therefore, is that redesigning their systems and building up their capacity to accommodate subpenny increments is possible from a technological standpoint, but that it would be impractical to do so and require considerable funds and staff time over the next few years with no real benefit to investors or contribution to market efficiency.

E. General Issues

The Commission also solicited comments on the following general questions regarding subpenny trading.

27. Are there any other market issues associated with subpenny trading that have not been addressed in this Release? If so, please provide a description of the issues and, where possible, provide specific examples of the trading behavior that gives rise to the issue.

Some of the participants in the SIA's informal survey raised other concerns that would need to be addressed if trading and quoting in subpennies were permitted. First, several participants advocated that, if subpennies were permitted, all market participants should be given sufficient time to develop the necessary trading and quoting capabilities

before subpenny trading and quoting actually begins in order to provide a level playing field. Second, several participants pointed out that, if there is substantially more quote traffic, communications bandwidth may have to be significantly upgraded.

In other discussions with member firms, some firms stated that, if subpenny increments were used, market centers may not be able to accurately determine current prices due to slow quote feeds, which would lead to investor complaints. These firms noted that a breakdown in market networks could have a negative effect on investor confidence, hinder efforts to raise capital, and ultimately serve as a brake on a recovering economy. Finally, some firms believe that the effects of using subpenny increments will make it more difficult to surveil trading practices.

28. If the minimum trading increment is less than a penny, should there be a limit on this increment? Is there a practical or logical limit to the number of decimal places in our trading market?

Member firms believe that there should be a limit on the number of decimal places if the minimum trading increment is less than a penny. Most firms suggest that four decimal places should be the limit.

29. One of the perceived benefits of decimal trading was that decimal prices would be easier for investors to understand than fractional prices. Would allowing trading and possibly quoting in very fine increments increase investor confusion?

Member firms believe that subpenny increments would be an impractical change that would cause investor confusion.

30. Would vendors and reporting services, i.e., newswires and newspapers, have the capability to handle such quotes or trades?

Member firms believe that vendors and reporting services would most likely need to develop greater capability in order to handle quotes and trades in subpennies.

Conclusion

The SIA appreciates the opportunity to explore this important topic of using subpenny increments for the trading and quoting of equity securities. For the reasons discussed above, most SIA member firms recommend that the Commission not permit the use of subpenny increments in the trading of equity securities, and that the Commission or Congress establish a uniform MPV of not less than a penny for both trading and quoting equity securities. Standardization of the trading and quoting increment at not less than a penny would eliminate the possibility of confusion among investors and securities professionals, and preserve the benefits of decimalization. Member firms therefore believe that standardization of such an increment would be appropriate in the public interest and consistent with the protection of investors, and contribute to the maintenance of fair and orderly markets as called for by our national market system.

The SIA also recommends that the Commission and the industry continue studying the impact of decimalization on our markets and all market participants to ensure that the benefits are preserved and that any adverse effects are ameliorated. In this regard, the SIA welcomes future opportunities to work with the Commission on this important issue.

If we can provide further information or clarification of the points made in this letter, please contact me or Ann Vlcek, Associate General Counsel, at 202-296-9410.

Sincerely,

Donald D. Kittell
Executive Vice President

cc: Annette L. Nazareth, Director, Division of Market Regulation, SEC
Robert L. D. Colby, Deputy Director, Division of Market Regulation, SEC
Belinda Blaine, Associate Director, Division of Market Regulation, SEC
Elizabeth King, Associate Director, Division of Market Regulation, SEC
James Brigagliano, Assistant Director, Division of Market Regulation, SEC
Alton Harvey, Chief, Division of Market Regulation, SEC