SIFMA
Securities Industry and Financial Markets Association

October 12, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File No. 265-26; Joint CFTC-SEC Advisory Committee
SIFMA Proposal to Prevent Price Swings Due to Liquidity Gaps

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association ("SIFMA")[1] believes that the events of May 6th illuminated the critical need for the U.S. securities markets to utilize better and more advanced methods for limiting destabilizing price moves and preserving fair and orderly markets. SIFMA commends the Securities and Exchange Commission ("SEC") and self-regulatory organizations ("SROs") for their expeditious efforts to address market conditions through the application of the single stock circuit breakers and revised clearly erroneous trading policies. In light of our experience with these policies over the last few months, the concerns described in the recent report of the SEC/CFTC Staff to the Joint Advisory Committee on Emerging Regulatory Issues on the events of May 6th, and the Committee's request for comments, SIFMA recommends consideration of a hybrid approach that would rely on a combination of the most effective, industry-proven mechanisms for protecting the price discovery process, including limit up/down protection, price collars and, where necessary, trading halts. Specifically, SIFMA advocates the consistent market-wide application of the following proposal to enhance market quality, eliminate erroneous trades and minimize halts in trading:

- Price Band. Preventing trades from occurring outside acceptable pre-determined price ranges calculated and disseminated to all market participants on a periodic intraday basis;
- Bid/Offer Wanted Period. Establishing a mechanism for alerting market participants to the need for additional liquidity within the acceptable price range to avoid unnecessary price swings; and
- Trading Halt. Providing for trading halts only when absolutely necessary to promote proper price discovery.[2]

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association ("GFMA"). For more information, visit www.sifma.org.

[2] The efficacy, costs and benefits associated with single stock circuit breakers should be assessed closely after the SEC has had experience with the limit up/limit down and other proposals set forth herein.

SIFMA believes that these safeguards would prevent the extreme price swings we observed on May 6th due to gaps in available liquidity. In addition, the changes would virtually eliminate clearly erroneous and "busted" or "adjusted" trades, and preserve normal trading activity except in the most extreme circumstances. It is important to note that this proposal is entirely dependent on timely and accurate market data being disseminated from the quoting market centers. Ensuring the availability of such data will be part of another industry dialogue.

A more detailed outline of the proposal is set forth as an Appendix to this letter. We recognize, of course, that our proposal requires several threshold decisions (*e.g.*, how to calculate and publish the acceptable price ranges). SIFMA looks forward to working with the SEC and other market participants to shape the proposal to best serve the needs of investors.

*** * * * ***

If you have any comments or questions, please do not hesitate to contact me at 202-962-7300 or avlcek@sifma.org.

Sincerely,

Ann L. Vlcek

Ann L. Vlcek
Managing Director and
Associate General Counsel
SIFMA

cc: Mary L. Schapiro, Chairman
Luis A. Aguilar, Commissioner
Kathleen L. Casey, Commissioner
Troy A. Paredes, Commissioner
Elisse B. Walter, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
Gregg Berman, Senior Advisor to the Director of the Division of Trading and Markets
James Brigagliano, Deputy Director, Division of Trading and Markets
David Shillman, Associate Director, Division of Trading and Markets

APPENDIX
Detailed Description of Proposed Solution

Set forth below is a more detailed description of SIFMA's proposed solution.

Applicability. This proposal would apply to all trading centers (as defined in Regulation NMS) trading any NMS stock, including ETFs. The proposal would not extend to the options or futures markets;[3] those markets would continue to impose their own requirements for volatile markets.[4]

Components of Proposal. The proposal would operate as follows:

Part 1: Calculation of Acceptable Trading Price Range. Trading would only be permitted within a specified uniform, market-wide acceptable price range,[5] the outer bands of which would be calculated as 10% limit up/down of the trailing 10 minute volume weighted average price ("VWAP") for the security.[6] In establishing an optimal formula for the calculation of the acceptable price range, it will be necessary to take into consideration how the formula would need to vary to accommodate, among other things, illiquid stocks,[7] large block trades,[8] and lower priced stocks. The acceptable trading price range at the open or after the commencement of trading after a trading halt would be determined using the open or reopening price (as applicable) as a reference price until there has been sufficient trading to permit calculation of a VWAP-based trading range. Once the acceptable price range is established, any trades that occur within that range could not be viewed as erroneous or busted.

Part 2: Dissemination of Acceptable Price Range. In order to prevent trades from occurring outside the acceptable trading price range, the acceptable price range must be disseminated to all trading centers. Because of the cost and technical difficulties associated with continuous data feed updates, and the limitations associated with using a static price range throughout the trading day, we propose the periodic dissemination of the acceptable price range.

---

[3] Although not the subject of this letter, given their interconnectedness, we recognize that coordinated efforts between the equities, options and futures markets may be beneficial and look forward to discussions in this regard.

[4] While not the subject of this letter, we also believe that market-wide circuit breakers could be improved, for example, by looking at the percent of S&P 500 names that are seeking liquidity or in a halted state, rather than solely consulting movement in the overall index.

[5] Our proposal would not prohibit quoting outside the acceptable trading price range.

[6] We believe that the use of the VWAP as a reference price is preferable to (1) using the open or previous day's closing price because the open and closing prices are not dynamic, and (2) using the last sale price for a security because the last sale price necessarily follows trading for the security.

[7] For example, for stocks that do not have at least 25 trades in the last 10 minutes, the formula could require a look-back further in time until there are at least 25 trades to calculate the VWAP.

[8] For example, large block trades could be adjusted so they do not account for more than 10% of calculation.

Specifically, we recommend that the securities information processors ("SIPs") calculate and publish the acceptable price range for each security approximately every 30 seconds.[9]

Part 3: Policies and Procedures to Prevent Trades Outside of Acceptable Price Range. To promote compliance with the price banding requirements, each trading center would be required to adopt policies and procedures reasonably designed to prevent trades from occurring outside of the acceptable trading price range. Similar to the Order Protection Rule of Regulation NMS, enforcement of the pricing band requirements would be conducted based on a trading center's policies and procedures, and based on the range as understood by the relevant market center at the time of a trade. Moreover, FINRA and other SRO rules implicated by this proposal would need to be amended. For example, trading centers will need to modify their erroneous trade rules to make it clear that trades occurring within the acceptable price range will not be busted. Similarly, current SRO rules related to the handling of held orders will need to be amended or clarified so that trading centers have flexibility with respect to how they intend to handle orders which otherwise would cause executions outside the current acceptable pricing band.[10]

Part 4: Seeking Additional Liquidity: Posting Limit Down(Up) Offer(Bid) for the Bid/Offer Wanted Period. The goal of the five second Bid/Offer Wanted Period is to avoid unnecessarily triggering trading halts by providing trading centers with the opportunity to introduce additional liquidity within the acceptable price trading band. To do so, trading centers must be able to indicate when they have marketable orders in an amount which exceeds posted liquidity within the current trading band. Under our proposal, trading centers seeking additional liquidity within a price band or that wish to trade outside of the acceptable price range must first post a limit down(up) offer(bid) at the low(high) end of the acceptable price range (*i.e.*, similar to a "bid wanted" or "offer wanted" communication). The publication of such a limit down(up) price would commence a five second countdown period during which additional liquidity would have a chance to replenish within the current price band. If a new acceptable price range is received during this five second period that the limit down(up) price is published, then the trading center can adjust its posted price accordingly. In addition, subject to the normal application of Regulation NMS, trading would be permitted at or above(below) the limit down(up) offer(bid).[11]

Part 5: Imposition of Trading Halt. Trading halts should be imposed only when absolutely necessary to reestablish fair, orderly and liquid markets. Under the proposal, if an execution(s) exhausts all size at the limit down(up) offer (bid) and if there is a trade or posted bid(offer) above(below) the limit down(up) price, the countdown period would stop and normal trading would continue. Otherwise, if both of these conditions are not met before the end of the

[9] Alternatively, to further limit the market data necessary for this proposal, the re-dissemination of the acceptable price range could be limited to those circumstances in which there has been a 1% price move in the acceptable price range.

[10] Examples of such flexibility would include delaying, re-pricing, or rejecting held orders or stop loss orders outside the band.

[11] However, it should be noted that the countdown period would not start if the limit down(up) quote results in a crossed market. Trading centers should have policies and procedures in place to minimize this from occurring.

five second countdown period, a halt would ensue similar to how it occurs under the current single stock circuit breaker rules. As discussed above, a new acceptable trading price range would need to be disseminated upon the recommencement of trading based on the reopening price for the stock, until such time that a VWAP-based trading price range could be calculated and re-disseminated.

Example. The following describes two examples of how the proposal would operate in practice.

Scenario 1 – The Rebound.

10:50:00	Stock at around 10.00 per share
	VWAP price band 9.00/11.00
10:52:00	Customer places order to sell 100,000 shares
	VWAP price band remains unchanged from 10:50:00
10:52:01	Stock trades from 10.00 down to 9.00 with 30,000 left unexecuted
10:52:02	Receiving trading center blocks sales below 9.00 and posts the 30,000 shares at 9.00 (*i.e.*, the lower level band price)
	All markets and market participants are alerted that the price band trigger has been hit and that the 5 second countdown period has begun for that stock
10:52:04	Market participants, using the countdown period to refresh quotes, generate new buy interest and take the 30,000 offered at 9.00
10:52:05	Stock begins rebound with 9.00 trade and new higher bids are generated which begins the process of bringing the stock back up above 9.00 (without ever having to halt the stock)

Scenario 2 – the Halt. Facts are the same as above up to 10:52:02, but the 30,000 share 9.00 offer posted at 10:52:02 does not generate buy interest at 9.00.

In this case, after 5 seconds from the time of the 9.00 offer, all markets halt the stock for 5 minutes. Thereupon, it reopens at a new price which begins a new series of price band disseminations and 10% limit blocks.