

U.S. Securities and Exchange Commission  
Equity Market Structure Advisory Committee

April 5, 2017

Statement of Thomas Gira, Executive Vice President, FINRA

Good afternoon. My name is Tom Gira and I am responsible for FINRA's Market Regulation and Transparency Services Department. I would like to thank the Commission, Committee members, and SEC staff for inviting me to participate in today's Equity Market Structure Advisory Committee meeting to discuss the critically important issue of the surveillance of our markets. In particular, I would like to share FINRA's thoughts regarding regulatory centralization given FINRA's experience providing regulatory services to U.S. equity and options exchanges and comment on the preliminary recommendations of the Trading Venues Regulation ("TVR") Subcommittee concerning regulatory centralization.

By way of background, FINRA first started providing regulatory services to exchanges when the International Securities Exchange became the first electronic options market back in May of 2000. Since then, FINRA commenced providing regulatory services to the Nasdaq family of markets, the NYSE family of markets, the CBOE family of markets, IEX, MIAX and BOX. At the present time, FINRA provides regulatory services to 19 SROs operating 25 markets; 10 that trade equities and 15 that trade options.

By combining data from FINRA's Order Audit Trail System ("OATS"), client exchanges, and the over-the-counter market, FINRA launched a cross market surveillance program in August of 2012 that makes today's highly fragmented markets seem like one, integrated market for surveillance purposes. On average, we process 50 billion market events a

day. We presently cover 99% of the listed equity market and 65% of the listed options market in our program. This is important because market participants engaging in improper conduct increasingly try to spread their activity across multiple markets in an attempt to avoid detection. We run surveillance patterns across this data that look for 180 different threat scenarios and 75% of the alerts generated involve activity on more than one market and 60% of the alerts involve trading activity flowing through more than one broker dealer. Many of these alerts would not have been generated but for FINRA's cross market surveillance program and some of the abusive algorithms we look for only work if the activity is spread between at least two markets. Another significant component of FINRA's cross market surveillance program is the regulatory intelligence that we receive from our client exchanges. Since 2015, FINRA has received over 1,100 referrals from its client exchanges resulting from the exchanges' surveillance and monitoring of their own markets, tips, and complaints. Our cross market surveillance program has been highly successful. Since 2015, FINRA made over 800 referrals to the SEC concerning abusive trading algorithms on behalf of FINRA and its exchange clients. These referrals and others in prior years have resulted in numerous actions by the SEC. In addition, FINRA and our exchange clients have brought many cases against firms and individuals within our jurisdiction.

FINRA believes that the regulatory ecosystem for cross market regulation created by FINRA and its client exchanges can serve as a strong foundation for surveillance in a post-Consolidated Audit Trail ("CAT") world. At the same time, it is very appropriate and timely that the TVR Subcommittee and the EMSAC are considering centralized regulation because, with CAT, necessary surveillance data will become ubiquitous and, as a result, there is a greater chance for regulatory duplication, regulatory gaps, and inefficiency.

Accordingly, I have two comments on the TVR Subcommittee's preliminary recommendations. First, I completely agree with the Subcommittee's recommendation that the SEC should make clear what the regulatory expectations are with respect to cross market regulation in a post-CAT world. I would ask that the Commission go even further and articulate expected standards with respect to cross-product regulation (i.e., trading abuses that can span asset multiple classes, such as equities and options). Just as we have seen market participants spread their activity across multiple markets for the same instrument to avoid detection, it is highly probable that they will do the same across with synthetic equivalents or related products, particularly when there is leverage involved. FINRA presently has a few surveillance patterns that look for cross product abuses and in 2014 we brought a case on behalf of our options exchange clients against a firm and an individual for manipulative equity and options trading, but the significantly enhanced options audit trail data that will be available in CAT will enable FINRA and the exchanges to take cross product surveillance to a new level that will better protect investors.

Second, the TVR Subcommittee recommended that there does not necessarily have to be a single SRO conducting cross market surveillance, but that there should be a single entity conducting inquiries, investigations and disciplinary functions related to cross market regulation. While I believe the Subcommittee's recommendation strikes a reasonable balance between the need to avoid regulatory duplication and promote regulatory innovation, I believe regulatory consolidation at the surveillance level is a more desirable solution than regulatory coordination. Among other reasons, having multiple surveillance providers could impede efficiency in the feedback loop of investigative findings informing improvements to surveillance patterns; it could result in unnecessary duplicative efforts, particularly when the surveillance patterns are comparable; multiple surveillance system would increase costs to the industry; it could foster an

unhealthy race by surveillance providers to submit as many alerts as possible to show their value versus other providers; and investigative teams could be put in the position of pursuing edge cases to be perceived as neutral to all surveillance providers. As a result, FINRA submits that it would be more desirable to have the exchanges and FINRA operate one cross market surveillance platform that reflects ongoing collaboration and partnership between the SROs, as is the case today.

In closing, while there can be different points of view about the efficacy of a single-provider model for cross market and cross product surveillance versus a multiple-provider model, I believe it is important for the Commission and the SROs to keep the following guiding principles in mind as we seek to leverage the much-improved audit trail data that will be available post-CAT to enhance the protection of investors and promote market integrity.

- Conduct comprehensive and uniform surveillance across all markets;
- Maintain a “community policing” environment where the knowledge and experience of each SRO is leveraged and the SROs collaborate routinely about surveillance patterns, problematic firms, cases and other matters;
- Promote innovations in surveillance methodologies and techniques;
- Minimize duplication and other unnecessary burdens for firm;
- Provide consistent outcomes for firms based on the totality of their activity across all markets;
- Ensure there are sufficient resources devoted to cross market regulation – our markets are the envy of the world and deserve high quality oversight;
- Promote effective SEC oversight by minimizing the fragmentation of functions;

- Promote operational efficiency of cross market regulation programs by, among other things, shifting to multilateral arrangements across the SROs instead of the current bilateral agreements; and
- Promote cost mutualization.

Thank you and I look forward to discussing these issues with you and my fellow panelists.