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The U.S. Securities and Exchange Commission

Public Hearing
on Proposed Regulation NMS

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INSTINET GROUP

REMARKS FOR TRADE THROUGH PROPOSAL

As you may know by now, I strongly support the complete elimination of the trade-through rule. But I also commend the Commission for proposing an opt-out provision in Regulation NMS. Making an opt-out provision available recognizes that the strict application of price priority rules (otherwise known as trade through rules), though well-intentioned, foster inefficiencies that ultimately harm investors. One thing that concerns me is how some have characterized this debate. Let me be clear - I agree with the New York Stock Exchange - nothing is more important than investors getting the best price. Some have inaccurately characterized this debate as one of speed versus price. Make no mistake, this debate is about investors getting the best price. Period.

And history shows that when market participants have the freedom to trade on the market of their choosing, the increased efficiency and competition produce better prices for investors. Due to the doomsday rhetoric used by some, however, an observer may think that eliminating the trade-through rule or providing an effective opt-out is a risky experiment. Fortunately, the experiment has already been conducted for the last 30 years. There is no trade-through rule for NASDAQ securities. The three largest ETFs have a de minimis exemption. The different environments allow us to compare securities traded with a trade-through rule to securities traded without a trade-through rule. The results are clear.

Fact: Effective spreads in Nasdaq S&P 500 stocks are narrower than in NYSE S&P 500 stocks.

Fact: Contrary to the rhetoric, the SEC execution quality statistics show that investors sending an order to the NYSE are equally likely to receive a worse price relative to the NYSE quote than a better price.

Fact: When Instinet customers route orders in NYSE stocks the average execution time is 19.7 seconds as compared to 1.2 seconds in Nasdaq stocks.

Fact: Our customers have found that slippage on the NYSE is 2.5 times worse than in NASDAQ stocks.

Fact: When the trade through rule applied to the QQQ, the market's most actively traded security, the spread was 4 cents in the primary market. After a trade-through exemption was implemented, INET reduced the spread to THREE TENTHS OF A PENNY, a tenfold improvement for investors.

Fact: The SEC's mere consideration of allowing market participants to trade-through "slow" markets caused the NYSE to suddenly announce that it intends to make improvements to Direct Plus. We can only imagine what improvements would be made if trade-through were repealed.

I believe that these facts demonstrate the benefits that an effective opt-out will have on investors.

In closing, let me once more commend the Commission for its progressive regulatory reform on opt-out. But in order to deliver on the principles embodied in this reform, we must ensure a fair, efficient, and user-friendly opt-out. I look forward to working closely with the Commission on this issue.

REMARKS FOR ACCESS FEE PROPOSAL

I respectfully submit that the Commission should not be in the business of fixing prices. There is no statistical or other basis for fixing access fees at any level. The Proposal effectively caps access fees at 2 tenths of a penny while nearly the entire industry has arrived at 3 tenths of a penny through competitive forces.

We also should think about how we arrived at this point that we are considering fixing just this one particular fee called an "access fee." Clearly, there is a plethora of fees associated with accessing a market. For example, if an investor accesses the NYSE, the specialist charges a fee for limit orders that can be as much as 1 penny per share. It costs approximately $1.5 million to become a member of the NYSE to obtain full access to the NYSE's market. All these costs are significantly higher than the 3 tenths of a penny charged by electronic markets. Yet, there is no proposal to cap these fees.

The Proposed access fee cap will encourage marketplaces to raise fees for posting limit orders. This should be of concern to the Commission for at least three reasons. First, this approach discourages the entry of limit orders when one of the central purposes for proposing Regulation NMS is to encourage the entry of limit orders. In short, if market participants are charged to post limit orders, they will post fewer limit orders. It's that simple. Second, with fewer limit orders, spreads will increase and displayed size will decrease. Third, by fixing access fees, the Proposal directly benefits market makers that internalize customer orders, causing an increase in internalization. That's why market makers and market maker controlled industry groups have so strongly supported an access fee cap. Nothing is better for market makers than artificially wider spreads and reduced costs for accessing quotes on an agency basis. But the Commission has consistently stated that internalization harms investors because it reduces order interaction, harming price discovery. Investors will pay the price of an increase in internalization through the wider spreads and reduced quote competition.

Rather than engage in price fixing and risk all these unintended consequences, the Commission should instead allow market forces to continue to determine the appropriate price for services provided by a marketplace.

REMARKS FOR SUB-PENNY QUOTING PROPOSAL

I am opposed to the Commission fixing the minimum quoting increment. I believe that the market has already shown that it is responsive to investors when determining the appropriate minimum increment. Commission intervention will only cement the status quo and prevent marketplaces from making future changes to their quoted increments in response to investor needs.

I don't know whether the members of the Commission are aware of this or not, but the only major market permitting quoting in sub-pennies over $1.00 is BRUT ECN and even BRUT currently limits sub-penny quoting to stocks valued at $5.00 and under. Every other market center has, due to competitive forces, already eliminated sub-penny quoting. At the same time, the market needs the flexibility to introduce sub-pennies when they are appropriate. For example, INET currently trades every stock over a dollar in pennies with the exception of the QQQ. INET has found that the QQQ is a true sub-penny market where sub-penny usage is generally spread evenly along all price points. That is, sub-penny usage isn't grouped around $.001 and $.009, which would indicate that market participants are engaging in 'subpenny jumping.' In fact, the average spread in QQQ on INET is under $.003 (three tenths of a penny), well under the proposed penny increment. As a result, quoting in sub-pennies in QQQ is saving investors money. In fact, we estimate that if all markets traded just QQQ in sub-pennies the savings would be approximately $150 million per year.

Another example is Sirius Radio. INET recently began trading and quoting Sirius, a stock valued at approximately $4, in penny increments rather than sub-pennies. Immediately, INET lost market share to BRUT, the only market still trading Sirius in sub-penny increments. Clearly, investors prefer to quote and trade Sirius in sub-pennies. INET is now contemplating changing Sirius to sub-pennies. And there may be other stocks that may be ready for sub-pennies. Low priced, widely-held companies such as Sun Microsystems, Lucent, and Nortel all come to mind as stocks that may well be more efficiently quoted and traded in sub-pennies. But if the Commission adopts a prohibition on quoting in subpennies, the markets will lose the flexibility to respond to the needs of the marketplace. In the end, investors will pay because spreads in certain securities will be artificially fixed at a level that is higher than necessary. Sub-pennies save investors money. Given the fact that certain securities should be traded in sub-pennies, and the fact that the Commission cannot be as responsive as the marketplace in determining the appropriate increment for each security, I urge the Commission not to eliminate sub-penny quoting by rule but to leave that decision where it belongs, to the marketplace.