July 8, 2013

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Regulation Systems Compliance and Integrity (RIN: 3235-AL43)

Ladies and Gentlemen:

Better Markets, Inc.[1] appreciates the opportunity to comment on matters identified in the above-captioned proposed rule ("Regulation SCI") of the Securities and Exchange Commission ("SEC"). The Release addresses important issues relating to technology systems at self-regulatory organizations, alternative trading systems, plan processors, and exempt clearing agencies.

INTRODUCTION

In an era of high speed, automated financial markets, it is essential that market participants have systems and protocols in place to reduce the risk of technological breakdowns and failures. The need for robust systems has been made abundantly clear by a series of recent events. For example, on May 6, 2010, the markets inexplicably and without warning experienced extreme fluctuations, where major indices plummeted almost $1 trillion in minutes before partially rebounding and over 20,000 trades were executed at prices more than 60 percent away from their market values. It was not until over four months later that these market events, now known euphemistically as the Flash Crash, were analyzed by the SEC and the Commodity Futures Trading Commission and asserted to be the result of one institutional investor's use of a flawed trading algorithm.[2]

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[1] Better Markets, Inc. is a nonprofit organization that promotes the public interest in the capital and commodity markets, including in particular the rulemaking process associated with the Dodd-Frank Act.

[2] *Findings Regarding the Market Events of May 6, 2010*, Report of the Staffs of the CFTC and SEC to Joint Advisory Committee on Emerging Regulatory Issues (Sept. 30, 2010).

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Similar systems-related disasters include:

- the computer breakdown at Knight Capital Group Inc. in August 2011, which caused losses of $440 million;[3]

- the excess trading at Direct Edge exchanges in October 2011, which caused a systems outage and losses of $2.1 million;[4]

- the systems breakdowns at NASDAQ, which stalled and delayed Facebook, Inc.'s initial public offering in May 2012,[5] causing substantial losses and prompting NASDAQ to offer investors $62 million in partial compensation;[6]

- the four-year systems fault preventing investors from receiving the best price at BATS Global Markets Inc. revealed in January 2013,[7] which has cost investors $420,360;[8] and

- the breakdown in surveillance systems that failed to prevent abusive short selling at the Chicago Board Options Exchange, resulting in a June 2013 agreement with the SEC to pay a $6 million penalty and implement major remedial measures.[9]

These systems breakdowns not only disrupt markets and destroy investor wealth, but also erode investor confidence in fair and honest capital markets. Thus, maintaining a stable and orderly national market system through robust regulation of technological systems is essential.

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3 Nina Mehta, *Knight $440 Million Loss Sealed by Rules on Canceling Trades*, BLOOMBERG, Aug. 14, 2012, *available at* http://www.bloomberg.com/news/2012-08-14/knight-440-million-loss-sealed-by-new-rules-on-canceling-trades.html.

4 SEC, Release 2011-208, *SEC Sanctions Direct Edge Electronic Exchanges and Orders Remedial Measures to Strengthen Systems and Controls*, Oct. 13, 2011, *available at* http://www.sec.gov/news/press/2011/2011-208.htm.

5 SEC, Release 2013-95, *SEC Charges NASDAQ for Failures During Facebook IPO*, May 29, 2013, *available at* http://www.sec.gov/news/press/2013/2013-95.htm.

6 In the Matter of The Nasdaq Stock Market, LLC, SEC Admin. Proceeding File No. 3-15339, 12 n.12 (May 29, 2013).

7 Nathaniel Popper, *Errors Mount at High-Speed Exchanges in New Year*, N.Y. TIMES, Jan. 10, 2013, *available at* http://www.nytimes.com/2013/01/11/business/in-new-year-errors-mount-at-high-speed-exchanges.html?ref=business&_r=0.

8 Nina Mehta & Eleni Himaras, *Bats Says System Errors Cause Pricing Problems*, BLOOMBERG, Jan. 10, 2013, *available at* http://www.bloomberg.com/news/2013-01-10/bats-says-system-errors-caused-pricing-problems-over-4-years-1-.html.

9 SEC, Release 2013-107, SEC Charges CBOE for Regulatory Failures, June 11, 2013, *available at* http://www.sec.gov/news/press/2013/2013-107.htm.

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DISCUSSION OF PROPOSED RULE PROVISIONS

Regulation SCI is intended to help prevent and mitigate systems-related disasters by amending the current voluntary program and **requiring** self-regulatory organizations, alternative trading systems, plan processors, and exempt clearing agencies to adopt comprehensive policies and procedures governing their technological systems. Under Regulation SCI, these market participants would be held to a set of long-overdue, minimum policies and procedures and would have to employ "objective personnel" to annually review system risks and assess internal controls. Additionally, the regulation would enhance SEC supervision through certain notification and reporting requirements.

However, Regulation SCI is lacking in several major respects. Specifically, it:

- Fails to ensure that each firm has minimally adequate policies and procedures in place so that technology systems have appropriate levels of capacity, integrity, resiliency, availability, and security;

- Fails to ensure reliable and robust compliance review by permitting internal review by "objective personnel," rather than requiring review by an independent third party;

- Creates an unnecessary safe harbor from liability for firms and individuals, which unnecessarily binds the Commission in its enforcement of Regulation SCI; and

- Does not require that senior officers certify the adequacy of their systems compliance measures, thus failing to ensure that senior officers are accountable for their systems compliance.

To address these material weaknesses in the proposal, the following changes must be made.

Meaningful minimum policies and procedures.

First, the SEC must ensure that each firm has adopted **meaningful** policies and procedures designed to ensure that systems have appropriate levels of capacity, integrity, resiliency, availability, and security. To accomplish this, the Commission must do two things: (1) ensure that the required minimum elements of the policies and procedures are more robust, and (2) set forth clear, concrete, mandatory standards defining the minimum scope of the required policies and procedures.

In general, the six required elements for policies and procedures, labeled A-F, are so vague that they will fail to provide any meaningful improvement in technological systems. For example, item (F) requires the adoption of "standards that result in such systems being designed, developed, tested, maintained, operated, and surveilled in a

manner that facilitates the successful collection, processing, and dissemination of market data." This requirement is overly general. At a minimum, "successful collection, processing, and dissemination of market data" should be modified to include a condition requiring SCI entities to provide impartial access and assess non-prohibitive fees for real-time data.

This latter step is necessary to promote market efficiency and strengthen investor confidence. As noted in the proposing release, "many trading algorithms make trading decisions based primarily on market data and rely on that data being **current** and **accurate** [and] [a]n SCI event in connection with market data could significantly disrupt markets."[10] But preferential treatment virtually ensures that the data, when it is finally disseminated to the public, is stale and no longer reflects market realities.

Moreover, mandating impartial access and non-prohibitive fees for real-time data is critically important for managing the stresses that high-frequency trading ("HFT") can place on a market and on technology systems. Because HFT strategies typically involve massive trading volume, at exceedingly high speeds, pursuant to automated algorithms, they pose significant challenges to technology systems. Therefore, all SCI entities must, at a minimum, have the capacity to deal with those stresses. But these challenges and stresses are magnified tremendously whenever HFT firms have **preferential access to market data.** This privileged access not only enables HFT firms to in effect foresee the future, but also to trigger and intensify dramatic market moves. The resulting market turmoil can in turn cause systems to fail.

Indeed, according to the office of the CFTC's Chief Economist, the May 6, 2010 Flash Crash was precipitated and exacerbated by HFT traders acting as so-called "market makers" who suddenly and *en masse* pulled liquidity out of the market when a poorly-designed algorithmic trade was executed and triggered a series of stops.[11] The HFT "market making" model,[12] which was in place on May 6 (and continues to this day), relied heavily on privileged access to data feeds. Removing this privileged access would encourage high-frequency traders to adopt far safer and more effective true market-making methodologies, to promote market efficiency and ensure liquidity in times of market stress, and to reduce the risk of system failures on trading platforms.

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10 78 Fed. Reg. 18,161 (emphasis added).

11 Andrei Kirilenko, The Flash Crash: The Impact of High Frequency Trading on an Electronic Market, May 26, 2011, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1686004.

12 In fact, the HFT "market making" model often bears little resemblance to actual market making. *See, e.g.,* Better Markets' comment letter to the CFTC on anti-disruptive trading practices (dated January 3, 2011, *available at* http://www.bettermarkets.com/sites/default/files/CFTC-%20Comment%20Letter-%20Antidisruptive%20Practices%20%201-3-11.pdf, incorporated here as if fully set forth). The key issue is that genuine market makers are obligated to offer liquidity consistently, while HFTs generally have no such obligation. In addition, traditional market makers capture spreads but do not widen them. On the other hand, privileged access to data and low-latency API access allows HFTs to artificially widen spreads by flashing orders and then cancelling them. This fools other market participants by making apparent spreads look narrower than the spreads that can actually be executed on, a destabilizing and disruptive practice.

In addition to strengthening these overly-generalized requirements for policies and procedures, the SEC must ensure that the mandatory minimum standards which define the adequacy of these policies and procedures are robust and concrete. As set forth in the Release, Regulation SCI provides only one suggested standard: current SCI industry standards. These in turn are defined as those that are (1) comprised of free, widely available information technology practices and (2) issued by an authoritative government body or a widely recognized organization. Thus, rather than defining appropriate standards, the SEC, the primary regulator of SCI entities, would defer to unspecified practices and standards set by other regulators or "widely recognized" organizations. Exacerbating the problem is the proposal's assurance that this is not the exclusive means of compliance: Rather, an SCI entity may use any policies and procedures that are **reasonably designed** to comply with Regulation SCI.

Regulation SCI's lack of robust and concrete standards for policies and procedures not only fails to provide the necessary clarity and transparency to market participants and the public, it also fails to protect investors and the public by allowing the same type of systems-related malfunctions, disruptions, and failures described above to recur. Moreover, without a specific, mandatory set of standards, compliance with Regulation SCI will be much more difficult for the SEC to monitor and enforce. Rather than assessing SCI firms' compliance with a set of specific, fully-vetted compliance standards, SEC examiners will be forced to rely on vague minimum requirements and industry assurances.

Independent compliance reviews

Second, the SEC must require that an annual SCI compliance review be conducted by an **independent third party**. Regulation SCI would allow a compliance review to be conducted by "objective personnel," an undefined term that the SEC believes encompasses persons "who have not been involved in the development, testing, or implementation of the systems being reviewed."[13] It is true that persons involved in the development, testing, or implementation process lack a fresh perspective and have a conflict of interest in reviewing their own work. However, simply removing them from the review process and replacing them with "objective personnel" is not sufficient. Anyone within the entity has a presumptive conflict with respect to evaluating compliance. Therefore, the SEC must go further and require independent **third party** review. A mandatory third party review would not only reduce conflicts of interest, but also provide the necessary degree of independence to ensure reliable and comprehensive review.

Eliminating the safe harbor

Third, the SEC must **eliminate the safe harbor from liability** in Regulation SCI. The safe harbor is available to individuals as well as SCI entities, and it is framed in such

[13] 78 Fed. Reg. 18,123.

general terms that it would be easy to invoke. By including this unprecedented safe harbor provision for compliance standards, the SEC unnecessarily and severely limits its ability to deter violations through meaningful enforcement actions. Moreover, the proposing release contains no compelling justification for such a safe harbor.

Senior officer certifications

Fourth, the SEC must ensure compliance and accountability by requiring **senior officer certifications**. Such certifications are an important regulatory tool, recognized specifically in Section 302 of the Sarbanes-Oxley Act of 2002, which promotes corporate accountability through certain certifications by CEOs and CFOs in issuers' periodic financial reports. As proposed, Regulation SCI would only require that the annual report of the SCI review be submitted for review to **senior management** and then for the report and **any** response by senior management to be submitted to the SEC.[14]

This is insufficient. It is not enough to leave the annual report on the desk of some unnamed senior-level manager. Rather, senior officials must be encouraged to read the report, appropriately react and respond internally, and finally vouch for the report through certifications that, at a minimum, set forth the official's name and position and attest to the accuracy and reliability of the report.[15] This requirement would promote individual responsibility and accountability, thus improving systems compliance and integrity and facilitating appropriate SEC enforcement.

All of the foregoing changes are necessary to help ensure that market participants are sufficiently diligent in preventing, detecting, and responding to defects and breakdowns in the technology systems that are so critical to the day-to-day functioning of our financial markets.

DISCUSSION OF ECONOMIC ANALYSIS

The persistent and unfounded criticisms from industry regarding economic analysis

Even when the SEC has clearly fulfilled its duty to consider the economic impact of its rules, representatives from industry have challenged proposed rules claiming – without merit – that the SEC failed to appropriately conduct what the industry calls "cost-benefit analysis."

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[14] Proposed Rule 1000(b)(7)-(8).

[15] The precise wording of the certification could mirror Section 302 of Sarbanes-Oxley, substituting language referring to "internal controls" with the phrase "systems compliance and integrity." Other certification language would also be effective and appropriate. *See, e.g.*, Speech of Commissioner Luis Aguilar, "Developing Solutions to Ensure that the Automated Systems of Our Marketplace are Secure, Robust, and Reliable," Mar. 7, 2013, *available at* https://www.sec.gov/news/speech/2013/spch030713laa.htm (recommending that an entity's senior officers be required to "certify, in writing, that (i) the entity has processes in place to establish, document, maintain, review, test, and modify controls reasonably designed to achieve compliance with Regulation SCI; and (ii) that the annual budget and staffing levels are adequate for the entity to comply with its obligations under Regulation SCI").

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These attacks rest on a series of fundamentally flawed claims. For example, in challenging rules promulgated by the SEC, the industry has:

(1) greatly exaggerated the actual duty imposed on the SEC by its governing statutes, Sections 3(f) and 23(a)(2) of the Exchange Act, in effect seeking to transform that limited duty into what they call "cost-benefit analysis, but which is in fact really an "industry cost-only analysis;"

(2) entirely disregarded the paramount statutorily required role of the public interest in the rulemaking process; and

(3) indefensibly ignored the enormous cost of the financial crisis and the larger collective benefit of all rules designed to help prevent a recurrence of that crisis or something far worse.[16]

Accordingly, it is important that the SEC adhere to a series of core principles governing the actual contours of its duty to consider the economic impact of its rule.

Core principles that must apply to the SEC's consideration of the protection of investors and the public and efficiency, competition, and capital formation.

1. *Under the securities laws, the SEC has no statutory duty to conduct cost-benefit analysis; in fact, its far more narrow obligation is simply to consider certain enumerated factors.*

Sections 3(f) and 23(a)(2) of the Exchange Act set forth the SEC's statutory requirement to "consider" a rule's impact on several specifically listed economic factors.[17] In particular, Section 3(f) requires the SEC, after considering "the public interest" and the "protection of investors," "to consider . . . whether the action will promote efficiency, competition, and capital formation." Section 23(a)(2) requires the SEC to "consider among other matters the impact any such rule or regulation would have on competition," and to refrain from adopting the rule if it "would impose a burden on competition not necessary or appropriate in furtherance of the purposes of [the statute]."

[16] *See* BETTER MARKETS, THE COST OF THE WALL STREET-CAUSED FINANCIAL COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION (Sept. 15, 2012), *available at* http://bettermarkets.com/sites/default/files/Cost%20Of%20The%20Crisis.pdf; *see also* U.S. GOVERNMENT ACCOUNTABILITY OFFICE, FINANCIAL REGULATORY REFORM: FINANCIAL CRISIS LOSSES AND POTENTIAL IMPACTS OF THE DODD-FRANK ACT, GAO-13-180, at 17 (Jan. 2013), *available at* http://gao.gov/assets/660/651322.pdf.

[17] 15 U.S.C. §§ 78c(f), 78w(a)(2).

The Exchange Act contains no language requiring a cost-benefit analysis and there is no basis for imposing any such requirement (and certainly none for an industry cost-only analysis, which is what the industry is really seeking). [18]

When Congress intends cost-benefit analysis to apply, it explicitly refers to "costs" and "benefits" and specifies the nature of the analysis.[19] And, when Congress wants agencies to be free from those constraints, it imposes a less burdensome requirement, thus giving overriding importance to particular statutory objectives.[20] Indeed, the Court of Appeals for the District of Columbia has recently assessed the CFTC's economic analysis duty under Section 15(a) of the Commodity Exchange Act, which actually refers to "costs" and "benefits," and confirmed that "[w]here Congress has required 'rigorous, quantitative economic analysis,' it has made that requirement clear in the agency's statute, but it imposed no such requirement here." *Inv. Co. Inst. v. CFTC*, No. 1:12-cv-00612, at 15 (D.C. Cir. June 25, 2013) (citing *American Financial Services Ass'n v. FTC*, 767 F.2d 957, 986 (D.C. Cir. 1985)); *cf., e.g.*, 2 U.S.C. § 1532(a).

The SEC's statutory duty stands in sharp contrast to the statutory provisions in which Congress explicitly mandates a netting or specific balancing of costs and benefits, let alone mentions "costs" and "benefits."

Moreover, Congress's careful choice of words in Sections 3(f) and 23(a)(2) and the case law construing similar provisions, make clear that the SEC has broad discretion in discharging its duty. The Supreme Court has long recognized that when statutorily mandated **considerations** are not "mechanical or self-defining standards," they "imply wide areas of judgment and therefore of discretion" as an agency fulfills its statutory duty.[21]

The plain fact is that the SEC has no statutory or other obligation[22] to quantify costs or benefits,[23] weigh them against each other,[24] or find that a rule will confer a net

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18 Better Markets has set forth a comprehensive analysis regarding the scope of the SEC's duties under the securities laws in BETTER MARKETS, SETTING THE RECORD STRAIGHT ON COST-BENEFIT ANALYSIS AND FINANCIAL REFORM AT THE SEC, at 39-44 (July 30, 2012), *available at* http://bettermarkets.com/sites/default/files/CBA%20Report.pdf. In addition, Better Markets has recently filed an *amicus curiae* brief in support of the SEC on the agency's statutory duties in *American Petroleum Inst. v. SEC*, No. 12-1398 (D.C. Cir. Oct. 10, 2012). Both the report and *amicus* brief are incorporated by reference as if fully set forth herein.

19 *See American Textile Mfrs. Inst., Inc. v. Donovan*, 452 U.S. 490, 510-512 & n. 30 (1981) (stating that "Congress uses specific language when intending that an agency engage in cost-benefit analysis" and citing numerous statutory examples).

20 *See Whitman v. American Trucking Ass'ns., Inc.*, 531 U.S. 457, 471 (2001) (holding that a statute "unambiguously bars cost considerations"); *see also Nat'l Ass'n of Home Builders v. EPA*, 682 F.3d 1032, 1039 (D.C. Cir. 2012) (statutes in which agencies must "consider" the "economic" impact or "costs" do not require cost-benefit analysis); *Cent. Ariz. Water Conservation Dist. v. EPA*, 990 F.2d 1531, 1542 n.10 (9th Cir. 1993) (language in 42 U.S.C. § 7491(g)(1) requiring "consideration" does not require a cost-benefit analysis).

21 *Sec'y of Agric. v. Cent. Roig Ref. Co.*, 338 U.S. 604, 611 (1950).

22 Indeed, there is no other law which would subject the SEC to a cost-benefit duty. The APA does not require such an analysis, *Vill. of Barrington v. Surface Transp. Bd.*, 636 F.3d 650, 670-671 (D.C. Cir.

benefit before promulgating it. The rationale for this flexible obligation in the law is clear: requiring the SEC to conduct a resource intensive, time consuming, and inevitably imprecise cost-benefit analysis as a precondition to rulemaking would significantly impair the agency's ability to implement Congress's regulatory objectives. The industry's desire to have its costs prioritized over all other costs (what they falsely refer to as "cost-benefit analysis") does not change the law, the reasoned basis for the law, or the underlying policy.

2. *The SEC must be guided by the public interest and the protection of investors as it considers the economic impact of its rules, not by concerns over the costs of regulation imposed on industry.*

The SEC's preeminent duty when promulgating rules is to protect investors and the public interest. The agency was established for the purpose of implementing the securities laws, and therefore its primary duty is to achieve the legislative objectives of those laws, which are first and foremost to protect investors and the public interest from fraud, abuse, and manipulation in the securities markets. As is evident from the securities laws themselves, their legislative history, and the specific delegations of rulemaking authority, the public interest and protection of investors is a key consideration in the SEC's rulemaking process. Indeed, Section 3(f) of the Exchange Act explicitly refers to "the protection of investors" and "the public interest," but does not mention any industry-focused concerns, such as compliance costs or the feasibility of conforming to rule requirements.[25]

2011), and the Executive Orders on cost-benefit analysis exclude the SEC and other independent agencies. Executive Order 13,579, 76 Fed. Reg. 41,587 (July 14, 2011); Executive Order No. 13,563, 76 Fed. Reg. 3,821, § 7 (Jan. 21, 2011); Executive Order 12,866, 58 Fed. Reg. 51,735, § 3(b) (Oct. 4, 1993).

[23] *Cf.* 42 U.S.C. § 300g-1(b)(3) (imposing a duty on the Environmental Protection Agency to use analysis of specific factors including the "[q]uantifiable and nonquantifiable health risk reduction benefits," the "[q]uantifiable and nonquantifiable costs," and "[t]he incremental costs and benefits associated with each alternative."). Courts have repeatedly held that an agency need not quantify the costs and benefits of a rule when a statute does not require it. *See, e.g., FMC Corp. v. Train*, 539 F.2d 973, 978-979 (4th Cir. 1976) (finding that 33 U.S.C. §§ 1314(b)(1)(B), (b)(2)(B) and § 1316 do not require quantification of the benefits in monetary terms). In fact, the D.C. Circuit has explicitly recognized that even in a cost-benefit analysis an agency's "predictions or conclusions" do not necessarily need to be "based on a rigorous, quantitative economic analysis." *Am. Fin. Services Ass'n. v. FTC*, 767 F.2d 957, 986 (D.C. Cir. 1985); *see also Pennsylvania Funeral Directors Ass'n v. FTC*, 41 F.3d 81, 91 (3d Cir. 1994) (recognizing that "much of a cost-benefit analysis requires predictions and speculation, in any context," and holding that the "absence of quantitative data is not fatal").

[24] Even when a statute refers to "costs" and "benefits," Courts refuse to impose a duty to conduct cost-benefit analysis absent language of comparison in the statute. *See Weyerhaeuser Co. v. Costle,* 590 F.2d 1011, 1045 (D.C. Cir. 1978); *see also Am. Petroleum Inst. v. EPA,* 858 F.2d 261, 265 & n.5 (5th Cir. 1988); *Reynolds Metal Co. v. EPA*, 760 F.2d 549, 565 (4th Cir. 1985).

[25] *Cf.* 42 U.S.C. § 300g-1(b)(3)(C) (requiring analysis of certain costs of safe drinking water regulations including costs that "are likely to occur solely as a result of compliance with the maximum contaminant level, including monitoring, treatment, and other costs"); 42 U.S.C. § 6295(d) (1976 ed., Supp. II) (requiring a weighing of the economic impact on manufacturers and the savings in operating

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Moreover, the SEC's duty to protect investors and the public interest has renewed importance in light of the 2008 financial crisis. The financial crisis is a powerful reminder of the need to remain focused on the core purposes of securities regulation and the SEC's overriding duty to protect the public, investors, and the integrity of the markets. The Supreme Court's admonition about the importance of raising standards of conduct to the highest possible level following the Great Depression applies with equal force today:

> "It requires but little appreciation . . . of what happened in this country during the 1920's and 1930's to realize how essential it is that the highest ethical standards prevail" in every facet of the securities industry.[26]

If these goals are subordinated to industry concerns over the costs of regulation in the rulemaking process, then any financial reform will have little chance of protecting our markets and our economy from the ravages of another financial crisis. Thus, in promulgating rules, the SEC must be guided by the preeminent concerns of the public interest and the protection of investors, not the burdens of regulation on industry.

3. *For any rule promulgated in accordance with, or in furtherance of, the Dodd-Frank Act, the ultimate public interest and investor protection consideration is implementing the reforms that Congress passed to provide for a safer and sounder financial system and to prevent another financial crisis.*

The SEC must always consider and give proper weight to the overriding goal that Congress intended to achieve when it passed the comprehensive, interrelated law, and the enormous benefit that the rules collectively will provide to the public. That goal is to prevent another financial collapse and economic crisis, and that benefit is to avoid the economic costs, hardships, and human suffering that would inevitably accompany such disastrous events.

The dollar cost alone of the financial collapse and still-unfolding economic crisis is conservatively estimated to be in the trillions. A study by Better Markets estimates that those costs will exceed $12.8 trillion.[27] In addition, the Government Accountability Office issued the results of a study on the costs of the crisis earlier this year, observing that "the present value of cumulative output losses [from the crisis] **could exceed $13**

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costs as "compared to any increase in the price of, or in the initial charges for, or maintenance expenses of, the covered products which are likely to result").

26 *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186-87 (1963) (quoted authorities omitted).

27 *See* BETTER MARKETS, THE COST OF THE WALL STREET-CAUSED FINANCIAL COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION (Sept. 15, 2012), *available at* http://bettermarkets.com/sites/default/files/Cost%20Of%20The%20Crisis_0.pdf, incorporated by reference as if fully set forth herein.

trillion."[28] Therefore, as the SEC considers the public interest and the protection of investors under Sections 3(f) and 23(a)(2), it must continue to consider, above all, the benefits of the entire collection of reforms embodied in the Dodd-Frank Act, of which any specific rule is but a single, integral part.

The Application of Sections 3(f) and 23(a)(2) in the Release.

The Release shows that the SEC has considered the economic impact of Regulation SCI under Sections 3(f) and 23(a)(2). However, the SEC should more closely adhere to the statutory requirement, namely the duty simply to consider the specified factors, rather than attempting to review costs and benefits on a more comprehensive basis.

1. *The SEC complied with Sections 3(f) and 23(a)(2).*

The SEC appropriately identified both of the statutory provisions applicable to its economic considerations[29] and explained how various aspects of the rule would affect the specifically enumerated factors in those provisions.[30] This is what the Exchange Act requires, and by considering the specified factors, the SEC has fulfilled its duty with respect to economic analysis.

2. *The SEC must ensure that its economic consideration is limited to its narrow duty under Sections 3(f) and 23(a)(2).*

The SEC should carefully avoid undertaking a cost-benefit analysis, or any similar approach in which agencies determine and quantify costs and benefits, net them against one another, and adopt the least costly rule. This type of analysis is not required by Sections 3(f) and 23(a)(2), it poses a threat to the implementation of Congress's policy goals, and it wastes agencies' resources without producing accurate or useful results. In fact, consideration of costs and benefits beyond those specifically tied to the Exchange Act provisions tends to mislead the public and the Commission by overemphasizing easily quantifiable costs to the detriment of important, albeit unquantifiable, benefits.

At a minimum, the SEC should, in explaining its statutory duty under Sections 3(f) and 23(a)(2), explicitly assert that it is not required to perform a cost-benefit analysis, quantify or compare costs and benefits, or perform any analysis that exceeds the Section

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[28] U.S. GOVERNMENT ACCOUNTABILITY OFFICE, FINANCIAL REGULATORY REFORM: FINANCIAL CRISIS LOSSES AND POTENTIAL IMPACTS OF THE DODD-FRANK ACT, GAO-13-180, at 17 (Jan. 2013) (released Feb. 14, 2013), *available at* http://gao.gov/assets/660/651322.pdf (emphasis added).

[29] 78 Fed. Reg. 18,164.

[30] *See, e.g.*, 78 Fed. Reg. 18,168 ("The Commission preliminarily believes that proposed Rules 1000(b)(1)– (8), taken together, should result in actual systems improvements as well as enhanced availability of relevant information regarding SCI events to the Commission and members or participants of SCI entities. This, in turn, could facilitate better decisions by market participants, which could promote allocative efficiency of capital and capital formation, potentially providing an overall benefit to the securities markets and promoting the protection of investors and the public interest.").

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3(f) and 23(a)(2) requirements. In addition, as mentioned above, there is no need for the agency to quantify or "determine" Regulation SCI's costs and benefits.

Moreover, in the Economic Analysis section of the Release, the SEC discusses specific costs and benefits associated with the proposed rule. Assuming that particular costs and benefits are at all relevant to the SEC's required economic analysis, the agency should more clearly set forth how those costs and benefits are directly related to protecting investors or the public or to efficiency, competition, or capital formation.

CONCLUSION

We hope these comments are helpful.

Sincerely,

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