Statement of Thomas Wittman
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1. Introductions and Background

Good afternoon Chair White, Commissioners, Committee Members and my fellow panelists. My name is Tom Wittman. My background is in exchange technology. Since joining the Philadelphia Stock Exchange in 1987, I have been engaged in every element of market infrastructure.

I've designed, coded, tested and operated technology for front ends, trading engines, routers, back-office, and clearance and settlement. I've migrated systems from open outcry, to electronic messaging, to automated matching. Today, I serve as Executive Vice President and Global Head of Equities at NASDAQ OMX. I am responsible for the management and strategy of NASDAQ's three U.S. equities markets; and three U.S. options markets, equities and equity derivatives trading in Copenhagen, Helsinki, Stockholm and Amsterdam. I also serve as CEO and President of The NASDAQ Stock Market, NASDAQ PHLX LLC and NASDAQ BX Inc.

NASDAQ spans the world and the lifecycle of trading. NASDAQ owns and operates the global infrastructure of public markets -- markets for securities that are publicly traded and available to all investors. Outside the U.S., we own 18 securities markets, 3 clearing houses, and 5 central securities depositories, spanning six continents. In addition to equities and options, we trade derivatives, fixed income products, freight, power and commodities. Seventy exchanges in 50 countries run on our trading technology, and markets in 26 countries rely on our surveillance technology to protect investors, driving growth in emerging and developed economies. We are the largest single liquidity pool for U.S. publicly traded equities and provide the technology behind 1 in 10 of the world's securities transactions.

Based on my 28-years in the industry, I can say without reservation that U.S. market structure continually evolves. It never stands still. Regulation must evolve with it. Markets are not self-correcting. They are complex and dynamic, and they grow and decay like any organic ecosystem. Without attentive and prudent steering, markets will spin further and further from their core purpose, creating wider and wider ranges of unexpected, unanticipated outcomes. As the speed of evolution increases, so too must the speed of regulation. If markets fragment, regulation must unify. If markets darken, regulation must shed more light. If markets move, and they always move, regulation must also move.

If we don't give our markets the attention and upkeep they demand, the U.S. markets will deteriorate in relation to their global competitors. NASDAQ operates markets all over the world, and I can say unequivocally that foreign markets do not accept the proposition that U.S. markets will always be the most liquid and efficient. For example, a number of markets in Asia and Europe have the economic dynamics, the foundational institutions, the resources, the skills, and the ambition to supplant the U.S. as the leading venue for capital raising. Quite simply, like in so many areas, the U.S. must continuously improve to stay on top.

2. NASDAQ Issuer Credibility and Focus

NASDAQ runs what we view as the world's largest public company listing operation. On our markets, we list over 3,500 companies in 9 countries, with a total market valuation of 9.5 trillion dollars. My colleague, Tom Farley, at the Intercontinental Exchange will no doubt agree that open-access, non-discriminatory listing venues that facilitate issuer capital raising on a daily basis offer the Committee a unique perspective on the evolution of the U.S. markets.

NASDAQ has been and is the birthplace and home of growing, innovative, job-creating companies. We like to say that supporting emerging, high-growth companies is in our DNA. The creation of NASDAQ introduced sound regulation to the over-the-counter trading. And around NASDAQ grew an ecosystem of analysts, brokers, investors and entrepreneurs allowing high growth companies to raise capital that was not previously available to them. Companies like Apple, Microsoft, Cisco, Google, and Intel, all of which made their initial public offerings on the NASDAQ Stock Market, use the capital they raised to make the cutting edge products that are now integral to our daily lives. NASDAQ supports these companies as they grow and they in turn bolster the U.S. economy by creating millions of jobs.

3. Wrong Question

NASDAQ's heritage drives our belief that market structure should serve all investors and in particular strengthen and nourish growth companies. In our view, the current U.S. market structure does not sufficiently emphasize serving investors and is definitely not well suited to help emerging growth companies. In fact, we believe that public skepticism regarding the public markets and their increasing complexity hurt efforts to get companies to go public here in the U.S. and to support them once they do go public. Through the JOBS Act and the Tick Pilot, Congress and the SEC have recognized that the markets need to evolve to support growth companies. By creating this Committee, the SEC is also recognizing that the markets need to evolve to serve investors and support both large and small companies.

You've asked us to focus on Rule 611 but, with all due respect, evaluating Rule 611 as a stand-alone rule is not the best way to evaluate its effectiveness. For example, the introduction of new order types, as well as increased fragmentation of lit and dark venues are the product of a variety of additional factors, including distortionary rebates , differential regulation for ATSs, single dealer systems, and exchanges, as well as many other forces. Evaluating Rule 611 based solely on its two primary objectives would overly simplify the issues we face.

Yes, Rule 611 must be evaluated, as well as other market dynamics to determine a course of action. Clearly, market reforms in their decade-old forms have created competition among market centers, which has brought down trading costs. They have at the same time caused a proliferation of venues, which leads to fragmentation, technology challenges, reduced order interaction, and increased order isolation.

Rule 611 alone has magnified the role of access fees, creating more and more momentary monopolies, as Bob Greifeld predicted in an editorial in the Wall Street Journal many years ago. NASDAQ is about to complete a four-month pilot to test whether a reduction in access fees and rebates leads to measurable, meaningful behavioral changes. What we have found so far is that a reduction in access fees does not attract volume to NASDAQ, reduce fragmentation, or reduce the level of dark trading. But, a reduction in rebates does lead to a reduction in displayed liquidity.

A related point about the need for evolution is the need to clarify the Best Execution principle. For investor protection and protection of true Main Street investors, there is no principle more important than Best Execution. And yet, Best Execution analysis based on the displayed NBBO has changed little since Reg NMS took effect almost a decade ago in spite of the explosion in dark liquidity, often available at the midpoint of the NBBO. Best Execution remains a principles-based regulation even as Rule 611 and numerous other rules governing exchange conduct are becoming more and more prescriptive and detailed. It is difficult to reconcile the broad treatment of Best Execution with the narrow treatment of Reg NMS. Wouldn't you expect a well-defined Best Execution obligation to prompt a more vigorous search for midpoint liquidity? I think there is no doubt that the market would benefit from a more nuanced SEC view regarding Best Execution

We know that the U.S. markets can work better. Today's U.S. markets are increasingly fragmented, volatile, and a source of systemic risk. Liquidity in U.S. stocks is dispersed across 11 exchanges, over 50 other registered equity execution venues, and uncounted other trading facilities. The declining cost of launching and operating electronic order crossing systems has led to a proliferation of decentralized pools of liquidity that compete by offering their owners and customers reductions in fees, obligations, transparency and order interaction. Markets also compete on speed and on their cleverness in meeting regulatory obligations.

Foreign markets have used the evidence provided by the U.S. markets as the basis to reform their own market structures while avoiding the dysfunction of the U.S. markets. We have wrung our hands over this dysfunction, but done little to fix it in over a decade.

4. One Size Does Not Fit All

Our exchange system and its rules are based on a one-size-fits-all approach. One approach to access; one approach to display; one approach to order protection; one approach to order interaction. Just last week, the Commission approved a two-year experiment with multiple quoting and trading increments. We applaud that pilot, but it was triggered by Dodd-Frank almost five years ago, and it will not yield definitive benefits for another three to four years. We must find a better, faster way to implement rules and structures that differ depending on issuer size and trading patterns.

Market simulations using agent-based modeling, for example, offer substantial benefits in reducing the time and resources expended by the Commission staff on essentially routine matters. As simulation technology evolves it may also be able to tackle the more complex questions of market structure and design.

For example, given the intense price competition we question the time and resources spent analyzing whether exchanges have fully justified proposals reducing their fees. (Of course, nearly 40 percent of executions occur on venues that lack not only pre-trade price discovery but operational and fee transparency.) NASDAQ has two pending Petitions for Review for fee reductions that appear to be in limbo, one for over four years and another for over two years. In the most recent example, NASDAQ proposed to reduce fees for members that transact the most volume across all three of its options exchanges. NASDAQ filed this proposal in November of 2013 and it remains unable to implement this pro-competitive fee reduction. In what other industry would a company be prohibited from lowering prices for its most valued and value-contributing customers?

Exchanges should be free to evolve and experiment as the market evolves. As mentioned previously, NASDAQ is about to complete a four-month experiment to generate data on the impact of lower access fees paired with lower rebates in a range stocks from the most active mega caps to active growth companies. We didn't know what the data would show. We didn't know whether it would increase or decrease market share or profit. We did know it would generate valuable data and advance the debate over maker-taker pricing.

The SEC must give us more leeway to experiments like that. The right to experiment through lighter regulation should not only be granted to ATSs. BATS has proposed another initiative to reduce fragmentation in trading smaller stocks. NASDAQ supports its right to experiment and to cooperate with other markets in doing so. While such experiments by a single exchange may vary from a universally applicable rule, there is still value in experimentation and flexibility and little to be gained from stifling them.

There has been a great deal of focus since the JOBS Act on whether our market structure supports growth companies. While I agree with the attention given growth stocks, I question whether our market structure serves investors in more active issues as well. Proponents of the status quo point to the fact that trading costs in active stocks are as low as they have ever been as evidence that there are few issues to be addressed in these stocks. From my perspective, this Committee's charge to consider the profusion of complex order types is precisely about these most active stocks.

Complex order types exist, in large part, to capture liquidity rebates and avoid paying access fees. I see this both in equities and options trading. As the executive in charge of NASDAQ's global trading business, I believe our fee experiment shows that access fees and rebates in the most active stocks serve solely as one means for exchanges and dealer systems to compete with each other. These charges are largely unnecessary as incentives to provide liquidity in these stocks. A tiered structure in the U.S. where pricing (both fees and rebates), tick sizes, fragmentation, and other aspects of market structure are based on the liquidity profile of particular stock makes far more sense to me than does a one-size-fits-all approach.

5. One Size Does Not Fit All for Listings

Evolution and experimentation should not be constrained to securities trading. We believe now is the time to allow smaller companies to have a voice in how their securities trade. We urge you to move forward with a model that would allow issuers the choice to concentrate liquidity on a single trading venue. The purpose of the regulatory changes in U.S. equity markets over the past several decades was to encourage multiple markets to compete with each other. This revolutionized trading in many liquid securities, in particular by enabling innovative new technologies, dramatically increasing the speed and throughput of exchange systems, and by encouraging price competition. Unfortunately, this revolution has not provided meaningful benefits to small, illiquid companies. The extent of any benefits for the most liquid companies is also called into question, as this Committee's existence shows. Affording these small companies the option to suspend unlisted trading privileges in their securities would deepen liquidity and re-ignite competition among orders by focusing all trading onto a single platform. To the extent that this competition results in improved spreads and deeper liquidity, smaller companies electing this option could enjoy many benefits, including reduced capital costs.

We also believe that issuers should have the choice to compensate market makers that support their securities, with the goal of better spreads for their investors and enhanced liquidity. Market quality incentive programs of this kind have successfully enhanced liquidity and market quality for investors in Europe for several decades. We believe that they could also be useful to smaller, less liquid companies, where it is currently not profitable for market making firms to provide liquidity and support.

The current one-size fits all approach also extends to listing standards, but exchanges should be free to experiment with their listing standards. In particular, in 2004, the SEC adopted a definition of a "penny stock" in Rule 3a51-1 that essentially froze exchange listing standards as they then existed. This has inhibited innovation in listing requirements over the last decade. As markets have evolved, however, and liquidity sources and metrics used to measure companies have changed, listing standards that were appropriate in 2004 may no longer reflect market reality, especially for smaller growth companies. Similarly, alternatives to the price requirement that recognize that substantial companies can also trade at low prices are prohibited under this regime. We believe that the SEC should reconsider this definition to allow exchanges greater flexibility to adopt novel listing standards for growth companies. Moreover, if we hope to attract new growth companies to our markets, beyond those already on exchange tiers for smaller companies, we will need to adjust the listing standards so they can qualify without being subject to burdensome penny stock and blue sky requirements. The SEC would need to approve any rules, but the Penny Stock Rule should not be allowed to act as a barrier to innovation.

6. Recommendations

Once the Committee's valuable work is complete, I believe that the Committee will share my belief that the U.S. equity markets are overly complex and at risk of failing in their mission to investors and listed companies. Rule 611 plays a role in market complexity but it is merely one of many factors at work. While one approach to addressing the need for reform in the regulation of the U.S. equity markets would be a Regulation NMS 2.0 with detailed, prescriptive, one-size-fits-all requirements, based on my experience I cannot endorse such an approach. Instead, I encourage the Committee to recommend the Commission channel the energy and creativity shown by this industry in responding to Reg NMS by encouraging innovation and experimentation through adopting a principles-based approach to regulation that emphasizes serving the investor and supporting capital formation.

Specifically, the Tick Pilot is a positive development for its recognition that a one-size-fits –all approach does not work. In addition, the Commission could delegate the authority to define tick sizes to the listing exchange. The tick size is a surprisingly important – and extremely sensitive – variable in trading quality. Too wide and trading costs become burdensome to investors; too small and volatility becomes rampant. It is our view that the listing exchange with the oversight of the SEC is in the best position to optimize tick size policy, and to do so in a way that is responsive to the ever-changing needs of listed companies.

Just as not all issuers are the same, not all investors are the same. The Commission and the exchanges can do more to protect Main Street investors. The Commission has long differentiated among investors based on investable assets. It has also considered differentiating between investors based on their holding periods or other indicators of buy-and-hold strategies. The display and protection of customer limit orders are consistent with this approach, and have been an overwhelming positive force in U.S. markets for both equities and options customers. Exchanges should be free to experiment with other ways to protect true investors. Equity exchanges have attempted limited programs to support retail investor orders, options exchanges have "customer priority" but more can and should be done. NASDAQ encourages the Commission give exchanges space to explore other ways to support true Main Street investors.

7. Conclusion

I thank the Chair, the Commissioners and the Committee for their time and attention. We welcome the opportunity to work with the Commission and the Committee as we consider the important changes which can benefit investors and listed companies. I look forward to your questions.