



IEX Group, Inc.

3 World Trade Center
58th Floor
New York, NY 10007

t. 1 646 343 2000
f. 1 646 365 6862
iextrading.com

November 18, 2019

Via Email (oddlotcomments@forefrontcomms.com)

Nasdaq Unlisted Trading Privileges Plan Participants
Consolidated Quotation Plan Participants

Re: **Odd Lots Proposal and Round Lot Proposal**

Dear Operating Committees:

Investors Exchange LLC (“IEX”) is writing in response to the request for comment on the “Odd Lots Proposal” from the Participants of the Nasdaq Unlisted Trading Privileges (UTP) Plan and the Consolidated Quotation (CQ) Plan (collectively, the “Plans”).¹

As a member of the Plans’ Operating Committees, IEX supports and endorses the Odd Lots Proposal, and looks forward to comments from market participants. IEX supports adding more quotation information to the SIPs in general, including information on price levels beyond the “top of book” best bid and offer quotes from each exchange. Adding odd lot top-of-book data to the SIP would be one useful step to increase transparency. Among other benefits, it will improve the ability of many market participants to monitor and evaluate execution quality by providing a complete best-price audit trail.

IEX is primarily writing this letter to voice strong support for reducing the round lot size for higher-priced securities in order to improve market structure for all participants. Reducing the round lot size would serve a number of objectives. First, it would help to support the objectives of Rule 611 of Regulation NMS by limiting the occurrence of “trade-throughs” in the substantial volume of transactions that presently occur in sizes of less than 100 shares, thereby benefiting displayed limit orders as well as market orders.² Second, it would be a natural way to help the regulatory framework keep pace with recent market developments, including inflation in security

¹ See Securities Information Processor Operating Committees, Odd Lots Proposal, *available at* http://www.utpplan.com/DOC/Odd_Lots_Proposal.pdf.

² In keeping with the original intent of Rule 611 of Regulation NMS, “strengthened protection of displayed limit orders would help reward market participants for displaying their trading interest and thereby promote fairer and more vigorous competition among orders seeking to supply liquidity” and “strong intermarket price protection offers greater assurance, on an order-by-order basis, that investors who submit market orders will receive the best readily available prices for their trades.” SEC, Regulation NMS Adopting Release, No. 34-51808 at 22, *available at* <https://www.sec.gov/rules/final/34-51808.pdf>.



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prices and the impact of algorithmic trading in lowering average trade size. Finally, reducing the round lot size would also increase transparency, improve price discovery, and diminish the existing information asymmetry between traders who obtain market data feeds that include odd lots, and traders who obtain market data through the SIP or other more affordable market data feeds that do not include odd lots. Accordingly, IEX encourages the participants in the Plans to pursue coordinated action on an updated common definition of round lot size, in parallel with consideration of the Odd Lots Proposal.

Round Lot Proposal

IEX strongly supports reducing the round lot size for higher-priced securities. Reducing the round lot size to 50 shares for any security priced \$25 or higher would strengthen public markets by benefiting displayed limit orders, achieving better prices for a large number of liquidity-taking orders, and reducing information asymmetry between market participants who can see displayed odd lots and those who cannot.

Background

The distinction between odd lot orders and round lot orders has a long history in U.S. equity markets.³ In 2005, Regulation NMS reaffirmed this distinction by reserving the benefits of the Order Protection Rule to round lot orders (orders larger than one round lot). The size of a round lot is another strong historical tradition. Although the application of the round lot definition to each stock is determined by the listing exchange,⁴ in practice, virtually all NMS securities today have a round lot size of 100 shares.⁵

In 2005 when Regulation NMS was passed, odd lot volume was relatively small—around 2% to 4% of the total share volume.⁶ Since then, odd lot volume has increased steadily to around 7% to 8% of total volume today.⁷ (Measured in number of trades rather than volume,

³ See O'Hara, Yao and Ye, What's Not There: The Odd-Lot Bias in TAQ Data, 2014, Journal of Finance.

⁴ See, e.g., NYSE Rule 55.

⁵ Out of more than 8,000 symbols traded on IEX, only 12 have a round lot size different from 100 shares.

⁶ Odd lots were 2.25% of total volume in early 2008 and 4% in late 2009 according to O'Hara, et al., Odd-Lot Bias (for Nasdaq volume only). Odd lots made up 4% of total volume in 2010 according to <https://www.sec.gov/rules/concept/2010/34-61358.pdf>.

⁷ See data on SEC MIDAS, available at <https://www.sec.gov/marketstructure/midas.html>.



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around 41% of trades today are odd lot.) Frequently cited factors include the rise of algorithmic trading and the inflation in typical security prices.⁸

Round lot sizes have not kept up with this trend. Virtually all NMS securities had a round lot size of 100 shares 14 years ago, and virtually all still do today. As a result, more and more trading occurs in odd lots and thus falls outside of the scope of Rule 611, which is intended to limit the incidence of “trade-throughs” in NMS securities for the benefit of all market participants.

Proposal to Reduce Round Lot Size

IEX proposes reducing the round lot size to 50 shares for any security priced \$25 or higher. Today, securities priced \$25 or higher account for approximately 50% of volume.⁹ Table 1 breaks down the average daily traded volume across three price buckets and three trade size buckets. Currently (left side of Table 1), odd lots are approximately 7.3% of the volume. Under this proposal (right side of Table 1), odd lots would be approximately 4.0% of the volume—close to the 2010 level.¹⁰

| CURRENT REGIME | | | | PROPOSED REGIME | | | | |
|--------------------|------|-------|-------|--------------------|------|-------|-------|-------------|
| Shares | 1-49 | 50-99 | 100+ | Shares | 1-49 | 50-99 | 100+ | |
| price ≤ \$1 | 0.0% | 0.0% | 2.7% | price ≤ \$1 | 0.0% | 0.0% | 2.7% | unprotected |
| \$1 < price ≤ \$25 | 0.6% | 1.2% | 47.8% | \$1 < price ≤ \$25 | 0.6% | 1.2% | 47.8% | protected |
| \$25 < price | 2.1% | 3.3% | 42.2% | \$25 < price | 2.1% | 3.3% | 42.2% | |

% of volume, week of 2019.10.28

Table 1: share of traded volume by trade price and trade size categories (Source: IEX).

Benefits of Reducing Round Lot Size

Reducing the round lot size would benefit the market by expanding trade through-protection to different types of orders, including liquidity-providing and liquidity-taking orders, by increasing transparency and price discovery, and by helping equalize the view of the market across participants consuming different tiers of data feeds.

⁸ See Alexander Osipovich, Tiny ‘Odd Lot’ Trades Reach Record Share of U.S. Stock Market, Oct. 23, 2019, Wall Street Journal, available at <https://www.wsj.com/articles/tiny-odd-lot-trades-reach-record-share-of-u-s-stock-market-11571745600>.

⁹ IEX data.

¹⁰ Measured in number of trades rather than shares traded, around 41% of the trades are odd lot today. Under this proposal, that number would fall to around 33%.



First, under this proposal, certain displayed liquidity-providing orders would benefit by gaining protection under Rule 611. This would include some displayed orders entered in sizes smaller than 100 shares, but also some displayed orders entered in sizes *larger* than 100 shares, whose remaining size on the book is less than 100 shares because of a partial fill. The best priced odd lot limit orders are frequently better priced than the protected NBBO. Table 2 shows that this happens between 30% to 50% of the trading day for a selection of high-volume stocks.¹¹ Furthermore, those odd lot orders are frequently traded through. Column 2 in Table 2 shows the percentage of trades that trade through an odd lot order, out of all trades that occur when the odd lot BBO is better than the protected NBBO. Column 3 shows the percentage of all trades that trade through an odd lot order.¹²

| | Time where odd lot BBO is better than protected NBBO | Trade-through rate when odd lot BBO is better | Overall trade-through rate |
|------|--|---|----------------------------|
| AAPL | 2% | 27% | 0.1% |
| AMZN | 32% | 41% | 5.2% |
| BIIB | 35% | 37% | 5.6% |
| GOOG | 35% | 37% | 6.3% |
| ICE | 29% | 36% | 1.0% |
| NFLX | 40% | 43% | 6.3% |
| PCLN | 84% | 38% | 7.0% |
| PXD | 20% | 14% | 2.0% |
| TSLA | 50% | 35% | 5.8% |
| WYNN | 43% | 29% | 1.3% |

Table 2: Odd lot BBO and odd lot trade-throughs, April 20-24, 2015. (Source: Battalio, et al., Unrecognized Odd Lot Liquidity Supply)

Rule 611 also protects orders on the other side of a trade—the liquidity-taking orders. Whenever a trade-through happens, a liquidity-taking order could have received a better price on a different venue, and the order providing liquidity at this better price was displayed. But only some traders were able to see the order because they purchased premium data feeds that carry

¹¹ Data from Battalio, Corwin and Jennings, Unrecognized Odd Lot Liquidity Supply: A Hidden Trading Cost for High Priced Stocks, 2017, *Journal of Trading* (using data from April 20-24, 2015).

¹² Before the adoption of Rule 611, the overall trade-through rate for round lot orders was 2.5%. See SEC Office of Economic Analysis, Analysis of Trade-throughs in Nasdaq and NYSE Issues, 2004, available at <https://www.sec.gov/spotlight/regnms/analysis121504.pdf>.



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odd lot information. All traders could have seen those orders if they had purchased those premium data feeds. Under this proposal, formerly odd lot orders with better prices would now be round lot orders, and thus would be more generally available.

The minimum notional size of an order that would gain trade-through protection under this proposal is large compared to orders that currently receive this protection. The smallest notional value of an order that would gain protection under this proposal is \$1,250. Today, 77.9% of volume with a notional value below \$1,250 is already round lot. For volume with a notional value between \$1,250 and \$2,500, 84.5% is already round lot; our proposal would increase this number to 88.9%. Given how much volume around and even below \$1,250 notional is already protected, there can be no reasonable concern that orders of such notional size are too small for protection.

A further benefit of reducing the round lot size would be to improve transparency and price discovery. More limit orders would be eligible to contribute to the protected National Best Bid and Offer. More trades would be last sale eligible, thereby providing more frequent reference price updates and strengthening the market in a broad spectrum of areas including Limit Up-Limit Down bands, buyback trading rules, venue collar reference prices, and the computation of financial indices.

Finally, this proposal would reduce the disparity between different views of the market, depending on the data feed subscribed to. Premium proprietary feeds from exchanges typically carry displayed odd lot order information while SIPs and other more affordable data feeds do not. Even under the Odd Lots Proposal put forward by the Plans, the odd lot top-of-book information would only be indicative and may be disregarded by traders.¹³ Rule 611 provides much stronger guarantees.

Potential Variations

Reducing the round lot size to 50 shares for any security priced \$25 or higher is not the only reasonable way to reduce round lot sizes. The SEC and the Plans may also want to consider, for example, an additional 10 share round lot tier for the small number of high-priced securities—e.g., \$100 or higher. The general points outlined in this letter stand with alternative proposals.

¹³ Furthermore, under the Odd Lots Proposal, a 50-share order still would not be reflected in the SIPs data feeds if a single share order was in front of it.



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Conclusion

It is time to update the round lot regime to reflect the realities of modern trading. The update should be significant enough to bring back a significant proportion of volume under the scope and protection of Rule 611. Any action should be broad enough to impact trading in a large number of securities and not just a handful of outliers. Doing so would strengthen public markets, increase transparency, and promote the goal of providing effective access to all market participants to the best available prices.

Very truly yours,

A handwritten signature in blue ink, appearing to read "Benjamin Connault", written over a horizontal line.

Benjamin Connault
Economist
benjamin.connault@iextrading.com

A handwritten signature in blue ink, appearing to read "Lucy Malcolm", written in a cursive style.

Lucy Malcolm
Associate General Counsel
lucy.malcolm@iextrading.com