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June 7, 2012

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: *NYSE Arca Fixed Incentive Program (File No. SR-NYSEArca-2012-37)*

Dear Ms. Murphy:

The Investment Company Institute¹ is writing to respond to NYSE Arca's proposal to create the Lead Market Maker ("LMM") Issuer Incentive Program ("Fixed Incentive Program"), a pilot program that would provide incentives to market makers to undertake LMM assignments in certain exchange-traded products ("ETPs") listed on the Exchange.²

The Fixed Incentive Program is the most recent in a number of market maker incentive programs offered by exchanges to issuers of ETPs. Last month, ICI provided comments on a proposal by The NASDAQ Stock Market to establish its Market Quality Program ("MQP").³ As we stated in our comment letter on the MQP, as issuers of exchange-traded funds ("ETFs"), ICI members have a strong interest in ensuring that the securities markets are highly competitive, transparent and efficient, and ICI has long advocated for regulatory changes that would result in more efficient markets for issuers of ETFs.

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$13.4 trillion and serve over 90 million shareholders.

² Securities Exchange Act Release No. 66966 (May 11, 2012), 77 FR 29419 (May 17, 2012) ("Release").

³ See Letter from Ari Burstein, Senior Counsel, Investment Company Institute, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated May 3, 2012. The letter can be found on ICI's website at <http://www.ici.org/pdf/26142.pdf>.

ICI therefore supports the overall goal of the Fixed Incentive Program, and market maker incentive programs in general - to incentivize market makers to make high-quality, liquid markets in ETPs. To the extent the Fixed Incentive Program results in narrower spreads and more liquid markets for ETPs, without any associated unintended consequences for these products or the markets as a whole, the Program could prove beneficial. At the same time, we recognize that market maker incentive programs, such as the Fixed Incentive Program, represent a departure from current rules precluding market makers from accepting payment from an issuer of a security for acting as a market maker and raise concerns whether payments under such programs create conflicts of interest between an issuer and the market maker for a security.

While there are various similarities with the recent NASDAQ proposal, the Fixed Incentive Program contains important differences in the manner in which the Program will operate. Most significantly: (1) the Fixed Income Program does not limit ETP participation based on liquidity levels or volume thresholds; (2) LMMs and issuers are permitted to negotiate the specific "Optional Incentive Fee" to be paid by the issuer to the LMM⁴ and related performance standards to obtain the fee (*i.e.*, there are no objective performance standards for LMMs); (3) there are no additional or higher performance standards that an LMM must meet to become eligible to obtain the Optional Incentive Fee (unless specifically negotiated between the issuer and LMM); and (4) there are limits to the number of existing ETPs a single issuer can place in the Program. We believe some of these differences could raise potential conflicts of interest between an LMM and an ETP issuer. Specifically, certain elements of the proposal could provide incentives or opportunities for LMMs to pressure ETP issuers to place each and every ETP listed on the Exchange in the Program, and therefore generate the maximum amount of Optional Incentive Fees, or face the threat of the withdrawal of the LMM from making a market in that issuer's ETPs.⁵

Our specific comments and recommendations on the Fixed Incentive Program follow below.⁶

⁴ Under the Program, an issuer of an ETP could elect to pay NYSE Arca an "Optional Incentive Fee," which would range from \$10,000 to \$40,000 per year, in addition to the currently applicable listing and annual fees.

⁵ There are certain other differences between the NYSE Arca and NASDAQ incentive programs that we believe are significant in examining the potential benefits of such programs to ETP issuers, and any potential conflicts of interest, specifically that only one market maker, the LMM, is involved in the NYSE Arca market while multiple, competing market makers are involved in the NASDAQ market. We recognize, however, that this element of the proposal is a product of the overall NYSE Arca market structure.

⁶ We recommend that as the SEC considers the issues raised by the NYSE Arca proposal, it also consider the implications raised by market maker incentive programs as a whole and, significantly, the impact of the various programs on ETP investors. While our comment letter focuses on the impact of the proposal on issuers of ETPs, it is unclear, at this time, whether market maker incentive programs will result in overall benefits to investors.

Limiting Eligibility of Fixed Incentive Program to Certain ETPs

The Fixed Incentive Program, as proposed, does not limit which ETPs can be included within the Program based on trading volume, and does not provide for the removal or withdrawal of an ETP from the Program if the ETP reaches a certain liquidity level or volume threshold. ICI recommends that NYSE Arca limit the type of ETPs permitted in the Program based on trading volume. We also believe that it would be appropriate for an ETP to be removed from the Program once it reaches a certain liquidity level or volume threshold. Such requirements would limit the Program to ETPs that truly need LMM participation and assistance, and could help prevent the potential conflicts of interest discussed above.⁷

LMM Selection Process and Performance Standards

Under the proposal, NYSE Arca would communicate the ETPs proposed for inclusion in the Fixed Incentive Program on a written solicitation that would be sent to all qualified LMM firms along with the Optional Incentive Fee the issuer proposes to pay NYSE Arca for each ETP. The issuer and the LMM would then agree on the final Optional Incentive Fee for each ETP and, if more than one qualified LMM proposed to serve as the ETP LMM, the issuer would choose the LMM.⁸

The Release requests comment on a number of issues relating to how LMMs will be chosen by issuers, the standards LMMs will be subject to, and the negotiation of the Optional Incentive Fee by issuers and LMMs. ICI believes that it is appropriate to provide flexibility to issuers to choose the LMM they desire for their ETP; given that the NYSE Arca market structure does not allow for competing market makers, the choice of a specific LMM for an issuer may be more significant than that on other markets where multiple market makers exist. We also believe that it is appropriate to allow issuers and LMMs to negotiate the specific Optional Incentive Fee.

However, to address concerns regarding potential conflicts of interest, we recommend that NYSE Arca establish objective performance standards for LMMs participating in the Program, and require that these standards be higher than the current LMM performance standards. We believe that requiring heightened performance standards to receive the Optional Incentive Fee also may provide a greater incentive for LMMs to make better markets in ETPs. In addition, objective performance standards will make the overall standards more transparent to issuers and investors.

⁷ NASDAQ would limit the type of ETPs that could participate in the MQP in this manner.

⁸ It is unclear from the proposal whether the entity paying the Optional Incentive Fee is the ETP sponsor or the fund. We understand from discussions with NYSE Arca staff that it will be up to the ETP sponsor to determine whether the sponsor or the fund pays the Optional Incentive Fee. We request that NYSE Arca clarify this element of the proposal.

Ms. Elizabeth M. Murphy

June 7, 2012

Page 4 of 5

Number of ETPs Permitted in Pilot Program

Under the proposal, an individual issuer is limited in the amount of ETPs permitted in the pilot program, *i.e.*, to not more than five existing ETPs. We agree with NYSE Arca that limiting the Program to only a certain number of ETPs during the pilot is reasonable to permit the SEC, the Exchange and others to assess the impact of the Fixed Incentive Program before making it available to all ETPs.

More importantly, however, we believe that limiting the number of ETPs from a single issuer in the Program would, as discussed above, prevent any incentive for LMMs to pressure ETP issuers to place each and every ETP listed on the Exchange into the Program.

Importance of Implementing the Fixed Incentive Program Through a Pilot Program

NYSE Arca has proposed to implement the Fixed Incentive Program on a pilot basis beginning no later than 90 days after the effective date of the proposal, until December 31, 2013. ICI strongly supports the establishment of the Fixed Incentive Program through a pilot program. We believe it is critical that NYSE Arca and the SEC have an opportunity to evaluate the impact of the Program on the quality of markets in ETPs prior to considering its permanent approval, both with respect to ETPs participating in the Program and those ETPs that choose not to participate.

During the pilot program, NYSE Arca would provide the SEC with certain market quality data on a confidential basis each month. The Release requests comment whether the Exchange should be required to publicly (and anonymously) disclose statistics on the performance of LMMs. ICI supports the public disclosure of statistics on the performance of LMMs. We believe this information could provide meaningful information to investors and would facilitate assessing how much liquidity is being provided by LMMs in the Fixed Incentive Program.

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If you have any questions on our comment letter, please feel free to contact me directly at (202) 371-5408.

Sincerely,

/s/ Ari Burstein

Ari Burstein
Senior Counsel

Ms. Elizabeth M. Murphy

June 7, 2012

Page 5 of 5

cc: The Honorable Mary L. Schapiro
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes
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