June 30, 2004

Mr. Jonathan G. Katz
Secretary
United States Securities and Exchange Commission
450 Fifth Street NW
Washington, DC 20549

Via e-mail and Fedex

Re: File Number S7-10-04 (Regulation NMS)

Dear Secretary Katz:

American Century Investment Management Inc. ("ACIM")[1] welcomes the opportunity to comment on the Security and Exchange Commission's proposed Regulation NMS[2] and the Commission's supplemental request for comment on the proposed rules.[3]

While Regulation NMS consists of four separate initiatives, we will focus primarily on the most controversial of the four proposals, the trade-through rule. I testified on behalf of the Investment Company Institute[4] at the Commission's recent Regulation NMS hearing[5] and we continue to support the Institute's stance on all facets of Regulation NMS. Like the ICI, we have followed the debate surrounding Regulation NMS and feel compelled to comment in light of some innovative ideas that have surfaced. We also remain

[1] American Century was established in 1958 and focused its business on developing direct contact with investors through no load mutual funds. Today, American Century Investment Management Inc. manages over $90 Billion for over 1.5 million retail and institutional investors.

[2] Securities Exchange Act Release No. 49325 (February 26, 2004), 69 FR 11126 (March 9, 2004) ("Release").

[3] Securities Exchange Act Release No. 49749 (May 20, 2004), 69 FR 30142 (May 26, 2004) ("Supplemental Release").

[4] The Investment Company Institute is the national association of the American investment company industry. Its membership includes 8,595 open-end investment companies ("mutual funds"), 612 closed-end investment companies, 124 exchange-traded funds and 5 sponsors of unit investment trusts. Its mutual fund members have assets of about $7.554 trillion. These assets account for more than 95% of assets of all U.S. mutual funds. Individual owners represented by ICI member firms number 86.6 million as of mid 2003, representing 50.6 million households.

[5] SEC Regulation NMS Hearing, April 21, 2004, New York, New York.

concerned about the short-sighted and economically self-interested participants who continue to support an "opt-out" exemption to the trade-through proposal.

Sub-penny Quoting Proposal

ACIM see no issues with continuing to allow passive crossing networks or algorithmic trading systems to report trades in sub-penny increments so long as those reports represent mid-point trades or similar pricing algorithms. For example if a stock is quoted \$20.01 – \$20.06 with a 5 cent spread, trade reports of \$20.035 would be acceptable as would a \$20.015 trade report in a stock with a quoted spread of \$20.01 – \$20.02. **However, the negotiation of that trade between buyer and seller, if a negotiation occurs, should be limited to whole penny increments.**

Given the near unanimous disdain for sub-penny trading and quoting within our industry we will frame our trade-through comments around the premise that the Commission will act, as proposed, and ban sub-penny quoting and trading for all stocks above \$1/share. **In fact, we would urge the Commission to separate the sub-penny proposal from Regulation NMS and act on it immediately.**

Trade-Through Proposal

We, at ACIM, do not believe that the intent of Regulation NMS is to dictate structure over market centers but rather to promote healthy competition between market centers while providing protection for all participants in the price discovery process. We need to do this right the first time. And, we need to ignore those who put their proprietary or misguided interests before the collective interests of investors who are so critical to the capital formation process in this country. In that vein, we support the establishment of a uniform trade-through rule for all securities across all market centers within the National Market System.

As I testified in April, we view Regulation NMS as a unique opportunity to put the "outdated" practices of antiquated market structures behind us and move forward with a single fundamental principal – limit order protection. **We believe that adequate technology currently exists which can guarantee protection for any displayed limit order anywhere within the National Market System against being traded through by another participant within the National Market System.**

The Commission should recognize that market centers currently have the ability to identify their quotes and/or limit orders as being available for automatic execution (auto-ex). That said, the Commission should remove itself from the exercise of attempting to classify entire market centers as “fast” or “slow.” We believe that a more appropriate response would be for the Commission to shift the onus to the various market centers and require them to identify whether or not the quotes they are disseminating are auto-ex. The Commission should define auto-ex as a quote that is immediately available for execution on a first come/first served basis without human intervention. Market centers would then be charged with the responsibility of taking whatever reasonable steps they can to ensure that a quote that is disseminated as auto-ex cannot be touched by human hands and is one which requires an immediate response. The quest to identify appropriate time parameters for acceptable quote turnaround or “refresh” times has potential for abuse. History has shown us repeatedly that once a line is drawn in the sand, participants will line up just one grain away.

If we are going to move forward, we need to recognize that only auto-ex displayed prices, whether they represent customer limit orders or proprietary interests, deserve the protection of a trade-through rule. In other words, quotes which do not represent firm, executable orders are meaningless and need to be treated as such by not having any standing within the NMS. **We should not consider an auto-ex trade at a price inferior to a nominal “quote” to be a trade-through.** To do so implies that the two are of equal importance to the price discovery process and they clearly are not.

The Commission seems to be struggling with traditional exchanges which want to adopt a “hybrid” market where some posted quotes are auto-ex at times, but not at others, or where a market center needs some time to refresh an auto-ex quote once it has been depleted. These considerations would be rendered pointless once we adopt the principal that auto-ex quotes are the only prices that deserve standing in the NMS. Once a market center’s auto-ex quote is depleted, the next best auto-ex quote would have standing. The initial market center would be free to refresh its auto-ex quote at any time – whether that delay is 20 milliseconds, 20 seconds or 20 minutes. If its new auto-ex quote is at a better price than the current price, it would re-gain standing within the NMS.

In reality, one facet of this proposed solution is already in place as the NYSE allows its specialists to “turn off” the auto-ex feature of Direct+ ™[6] by simply posting a 100 share market. The facet that we **are** burdened with currently is the ITS requirement of forcing us to continue to expose our orders to the NYSE even when no facility or "condition" exists to provide us with an automatic execution. Again, any "quote" that is not auto-ex represents nothing more than an advertisement of an interest to trade and therefore should not have standing over auto-ex quotes within the NMS. Once we adopt the principle that only auto-ex quotes are worthy of standing and they are protected, without exception, with a trade-through rule much of the wailing and gnashing of teeth over various exemptions to the trade-through simply have no philosophical justification.

- "Opt-Out" Exemption – We should focus more on the investors who have "opted-in" to the NMS. **Investors take considerable risk by displaying their trading intentions, via limit orders, to the investment community and deserve every ounce of protection our regulatory bodies can provide.** We believe that an opt-out exemption would hurt retail investors while benefiting institutional investors and intermediaries. Oddly, we also believe that a strict trade-through rule will actually benefit the very people who are arguing for an opt-out by promoting and protecting the display of large limit orders. While we want to believe that the "opt-out camp" is merely adopting a short-sighted position to meet their best execution responsibilities, we are concerned about possible questionable practices which might flourish if the Commission endorses a provision which allows participants to bypass legitimate, auto-ex limit orders.

- "Block Trading" Exemption – While the proposed opt-out provision would be available for all investors, block trading exemptions would allow institutions to trade large blocks of stock at prices "away" or inferior to the current market. We strongly oppose a block trading exemption as it would violate limit order protection. Like the opt-out provision, the block trading exemption would benefit large institutional investors and intermediaries at the expense of retail investors. Again, if a strict trade-through rule were adopted, and enforced, we

[6] Direct+ was introduced by the NYSE to allow Member Firms to enter limit orders of 1,099 shares or less and qualify for automatic execution at the bid/offer. The auto-ex feature is disabled when the bid/offer is for exactly 100 shares. Member Firms cannot access Direct+ more frequently than every 30 seconds.

> believe that large institutional investors (ourselves included) will see significantly more displayed limit orders. More importantly, as we interact with those orders, we will not be pitting retail against institutional interests. All investors will be treated equitably.

In our view there is no reason <u>ever</u> to trade-through an auto-ex quote. Those who are arguing for exemptions are doing so for proprietary purposes and therefore they should take a back seat to the overriding principal of limit order protection.

In summary, the marketplace has long realized that “quotes” which are not auto-ex are nothing more than meaningless advertisements used to attract customer order flow – with little assurance of an actual execution. The Commission now has the opportunity to acknowledge that fact by adopting regulation that would provide investors the opportunity to post their auto-ex limit orders within the National Market System with the full protection of a trade-through rule. If a market center wants to adopt a hybrid model with some manual trading and some auto-ex trading they should be free to do so – providing they do not trade-through auto-ex limit orders posted by a competing market center. Once the Commission levels the playing field by adopting a trade-through rule that protects only auto-ex quotes, investors will find comfort in posting their limit orders. Competition will increase as investors will vote with their keystrokes and competing market centers will respond rapidly to meet the needs/demands of the investing public. Investors, large and small, deserve to have complete confidence that if the posting of their auto-ex limit order within our National Market System does not result in an execution, at least no other participant within the National Market System received a better price.

Sincerely,

John J. Wheeler
VP, Director of U.S. Equity Trading
American Century Investment Management Inc.

cc:

The Honorable William H. Donaldson, Chairman

The Honorable Paul S. Atkins, Commissioner

The Honorable Roel C. Campos, Commissioner

The Honorable Cynthia A. Glassman, Commissioner

The Honorable Harvey J. Goldschmid, Commissioner

Annette L. Nazareth, Director

Robert L. D. Colby, Deputy Director
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