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New Stock Exchange Could Use "Speed Bump" to Combat High-Frequency Trading

By Ziqun Guo, J.D. Candidate 2018 | November 23, 2015

Recently, an investment company known as Investor Exchange, or IEX, proposed a new solution to the problems created by increasingly complex and high-speed stock markets. The firm plans to create a new American stock exchange that use a 350 microsecond "speed bump" as a limit for traders to place and cancel orders. IEX has proposed to create such a tool within the next five years to fight against high-frequency trading.

This proposal has already drawn some criticisms. Notably, other large stock exchange companies and high-speed trading firms have argued that this "speed bump" will make the stock market more complicated. The extra complexity might therefore benefit one side of the market over the other. Moreover, ordinary investors might enjoy trading immediately at the market price.

The new proposal and ongoing debate over high-speed trading raise larger policy questions about how to regulate stock markets that are becoming more and more complex. Some critics argue that the complexity arises from the regulatory rules known as the Regulation National Market System. The chief executive from IEX stated that the answer to those questions should come from market participants.

However, some policy-makers have a different opinion. Over the years, high-frequency trading has become a problem that many politicians and lawmakers have expressed concern about. Democratic presidential candidates Hillary Clinton, Bernie Sanders, and Martin O'Malley all proposed to raise taxes for traders who use their high-speed computers and expensive data lines to gain an advantage over ordinary investors. For example, Hillary Clinton pointed out in her campaign that banks and other financial institutions have been using high-frequency trading to abuse ordinary investors. Her campaign aide said, "The growth of high-frequency trading has unnecessarily burdened our markets and enabled unfair and abusive trading strategies." Hillary Clinton has also proposed to increase transparency and minimize conflicts of interest by changing the stock market rules.

Some proponents of these practices respond to these accusations by pointing out that high-frequency trading is actually not the most costly problem that ordinary investors are facing. They argue that statistics suggest that high-frequency trading only accounts for a small part of the stock market. They also argue that the stock market is a small part of the total securities market, and rather than worrying about the stock market, regulators should spend more time policing the bond market, which is twice as large.