# Statement at Open Meeting on Regulation SCI

## Commissioner Daniel M. Gallagher

**Nov. 19, 2014**

Thank you, Chair White. I'd like to begin by thanking the Trading and Markets staff, in particular Dave Shillman, David Liu, Heidi Pilpel, and Yue Ding, for all of their hard work on this rulemaking. I'd especially like to note their thoughtful and comprehensive treatment of the comments we received on the proposing release. I would also like to thank the staff in DERA and the Office of General Counsel for all of their hard work on this matter.

Like so many of our rulemakings these days, Reg SCI has taken a long, winding, and bumpy road to adoption. It is important to remember that the rule was originally conceived — and internally marketed — as a simple codification of the Commission's voluntary Automation Review Policy program. In light of the numerous market outages over the last several years, and given a certain unfortunate other voluntary program administered by the Commission, I was predisposed to look favorably on a codification of ARP that would both add transparency through the notice and comment process and convert it into a mandatory program.

The original version of the Reg SCI proposing release, however, was a classic example of regulatory overreach. It is an unfortunate sign of the times that the simple project of codifying the ARP program morphed into something so unwieldy and overly burdensome. The proposing release that was ultimately approved by the Commission in March 2013 represented a compromise between the ARP codification originally envisioned and the overreaching first draft of the proposal.

We received a number of detailed, thoughtful comments on the proposing release and again, the staff did a particularly good job addressing these comments. The resulting final rule, while certainly more prescriptive than I would have preferred, makes mandatory the most important aspects of the ARP program while minimizing the accompanying burdens to the extent possible.

It is vital for the Commission to recognize that the entities that will be covered by Reg SCI have more skin in the game than we do. No exchange wants to mishandle an IPO or have their SIP malfunction. If we could write a rule prohibiting all systems malfunctions with the confidence that the rule would actually work, than that is what we would do. But we can't, of course, and so we need to design a system of oversight that harnesses the natural incentives of the market participants it covers — that is, their enlightened self-interest in getting things right. I hope that is what we have done with today's rule.

I'm particularly pleased that the rule features a safe harbor provision for individuals employed by SCI entities. Since the beginning of my tenure as Commissioner, I have stressed the need for our rules to incentivize regulated entity personnel to take a proactive role in addressing problems. Although my comments have focused primarily on failure to supervise liability for lawyers and compliance personnel, they are equally applicable in the context of personnel at SCI entities. We must be cautious as we increasingly regulate the operations and information technology of our registrants — we do not want fear of personal liability in the securities industry to leave us with the B- and C-team technologists and operations professionals. We are already treading on that slippery slope and I hope the Commission will monitor this issue carefully. I certainly will.

Our system of regulation works best when we encourage personnel at regulated entities to proactively serve as the proverbial first line of defense, and I believe that the safe harbor will serve as such encouragement.

I have no questions.

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