american securities association
America's Voice for Main Street's Investors

June 10, 2021

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: June 10th Meeting of the Investor Advisory Committee

Dear Ms. Countryman:

The American Securities Association[1] provides these comments for the discussion regarding equity market structure at the June 10th meeting of the Securities and Exchange Commission (SEC or Commission) Investor Advisory Committee (IAC).

While the SEC has made great strides in recent years to implement certain offering reforms, longstanding concerns over equity market structure have been largely unaddressed. The ASA has been a leading voice in finding ways to help more companies in the United States go and stay public. Research has shown that when more companies go public, more jobs are created, and Main Street investors have greater opportunities to invest in growing American businesses. In short, we believe that any laws and regulations addressing equity market structure must support small business capital formation and market stability.

General Discussion.

The big picture discussion in this area must recognize that different tiers of market structure exist; that the current one-size-fits-all regime has contributed to a decrease in IPOs; that the reliance on "time-price" priority exacerbates price moves in all securities; and that current law grants monopoly pricing power to for-profit entities whose interests are not aligned with those of mom-and-pop investors.

Market structure is a function of regulation, technology, and competition. Government sets the rules in a zero-sum game and market participants compete to obtain the best technology, so they can extract whatever profits they can before everyone else catches up. Today, we have a hyper-competitive market because everyone whose business model depends on it, has access to similar

[1] The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA's mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This mission advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership of almost one hundred members that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States.

technology and the rules haven't changed. As a result, both costs and margins have come down significantly as the market has reached a point of maximum efficiency. This should be a net positive for market participants but for one fact: certain players continue to *unfairly* extract government-approved monopoly rents from investors (i.e. how can the cost of technology continue to decrease while the price of market data or to access a market continues to rise?).

To that end, market participants are left with two options: (1) petition policymakers to change the rules in a way that will increase their profits at the expense of others or (2) ask for a total reset of how the game is played. We support the later.

The SEC can end today's one-size-fits-all market structure by changing the rules to recognize that: (1) different tiers of market structure exist within the current ecosystem; (2) the order handling, time-price priority, and best execution obligations must be changed to make sense for each tier of market structure; (3) payment for order flow drives market behavior; (4) government-licensed monopoly control over all manner of pricing must end; and (5) the profit motive of Wall Street's high frequency traders must take a back seat to Main Street's desire for market stability.

Concentration.

There is a disconcerting amount of concentration in our equity markets at many levels. This has allowed a small number of entities to collect monopoly rents, which are ultimately paid by America's mom-and-pop investors.

The decline in competition deserves a strong response from regulators who have an obligation to promote competition and protect investors. We believe that now is the right time to tackle fundamental problems inherent in today's equity market structure and we appreciate the IAC taking up the issue during the June 10th meeting.

Areas of Focus.

I. Promoting Competition in Equity Markets: Recent research demonstrates the alarming level of concentration in our equity markets. This has led to increased costs for brokers and investors. As the level of exchange members has dramatically decreased, exchanges have driven up prices for market data products and connectivity.

One analysis estimates the drop in membership since 2012 at the largest exchanges – NYSE (down 26%); Arca (down 69%); and Nasdaq (down 44%).[2]

[2] John Ramsay, *The Rising Tide of Broker Costs, and the Shrinking Pool of Competitors*, June 8, 2021, *available at* https://medium.com/boxes-and-lines/the-rising-tide-of-broker-costs-and-the-shrinking-pool-of-competitors-40d4d389e59a

Another analysis estimates that the fees for proprietary market data products increased by 1,100% from 2010 to 2018.[3]

We are also concerned that pricing tiers for brokers based on volume serve as a facially discriminatory way to limit the access of smaller brokers to exchange products, especially when the fees a smaller broker pays are compared to those of the largest brokers executing transactions on the same market (more detail below).

In other words, one is left to conclude that exchanges are driving up prices to make up for a drastic reduction in membership and membership fees. While the SEC has taken some incremental steps to address this problem – such as new rules to increase competition for market data[4] – we believe the Commission must promote more competition within the equity markets. We hope that the IAC meeting will ultimately lead to recommendations for the SEC to consider in this regard.

II. Payment for Order Flow (PFOF): We have one question: does an order executed with PFOF obtain better execution than order executed without PFOF? Some will claim that because such an order gets price improvement, the answer is yes. However, we think the SEC needs to dig a little deeper because while an order may receive price improvement, we think that the price improvement could have been better if the order was not part of a firm's PFOF decision. The Chairman seems to agree. In a recent speech, he noted a firm that "explicitly offered to accept less price improvement for its customers in exchange for receiving higher payment for order flow for itself. As a result, many [of the firm's] customers shouldered the costs of inferior executions."[5]

As the IAC and policymakers examine this issue, we believe that both wholesale PFOF and exchange PFOF must be taken into consideration. You cannot change or end one type of PFOF without also ending the other, especially when many believe that the heart of the problem lies with exchange PFOF. The exchanges assert their power in this area through maker-taker rebate programs, which are nothing more than monopoly rent seeking.[6] Many firms, who are acting rationally, have sought a way to avoid paying this rent by executing trades off-exchange (i.e. dark pool execution, internalization, etc.).

(demonstrating that between 2012 and 2021, then number of exchange members decreased at NYSE by 26%, Arca by 69%, and Nasdaq by 44%).

[3] https://www.sec.gov/comments/4-729/4729-4559181-176197.pdf

[4] https://www.sec.gov/rules/final/2020/34-90610.pdf

[5] SEC.gov | Prepared Remarks at the Global Exchange and FinTech Conference

[6] *See* Robert Battalio, Shane Corwin & Robert Jennings, *Can Brokers Have it All? On the Relation Between Make-Take Fees & Limit Order Execution Quality* 10 (Dec. 13, 2013), *available at* https://www3 nd.edu/~scorwin/documents/BattalioCorwinJennings_20131213_SSRN.pdf

We ask that whatever market structure changes the SEC undertakes, the outcome of such changes do not serve to benefit *for-profit* monopolies who have a long history of abusing their statutorily created position in our market structure to price gauge market participants.

III. Pricing Tiers: As noted above, exchange pricing tiers impacts competition among brokers by favoring those who trade large volumes over those who do not. To access today's regulated exchanges, our members must sift through numerous pricing tiers based on order type, volume, and securities traded, among other things. This limits their access to trading and other proprietary exchange products. As a result, we agree with those who believe exchange pricing has directly impacted exchange membership and broker routing decisions.[7]

The SEC should evaluate whether *for-profit* exchange pricing complies with the language and the intent of the Securities and Exchange Act.[8]

IV. Suspending Unlisted Trading Privileges (UTP) for Small Issuers with Distressed Liquidity. UTP enables securities listed on an exchange to be traded on other national securities exchanges and, as the Statement notes, is automatically extended to securities prior to their listing on an exchange. While UTP makes sense for larger companies with adequate liquidity and significant trading volume, it simultaneously fragments liquidity and increases trading costs for thinly traded stocks, which overwhelmingly tend to be smaller issuers. Low trading volume also tends be highly correlated with a lack of analyst research coverage. We think one solution to incent research and generate more interest in smaller market cap companies would be to allow those companies to have the option to suspend their UTP.

V. Permit Certain Issuers to Determine their Own Intelligent Tick Sizes. We also think issuers should be eligible to determine their own "tick-size" to improve the liquidity of their stocks if those stocks are thinly traded. The SEC's 2000 decimalization order transitioned the trading of stocks – regardless of stock price or market capitalization – to penny increments. While decimalization may make sense for large capitalization, highly traded stocks, narrow spreads can serve as a disincentive for market makers to trade the shares of EGCs or other small issuers. We believe the SEC should consider issuer choice of tick sizes to solve for this problem.

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[7] Commissioner Robert Jackson, *Unfair Exchange: The State of America's Stock Markets,* September 19, 2018. https://www.sec.gov/news/speech/jackson-unfair-exchange-state-americas-stock-markets#_ftn38 Adding to my concern, rebate payments have historically been structured in a way that only exacerbates the conflict of interest issues I've described. Different market participants receive different rebates depending on how much business they do with the exchange. *See, e.g.*, NASDAQ Price List—Trading Connectivity, *available at* https://www nasdaqtrader.com/Trader.aspx?id=PriceListTrading2; *see also* New York Stock Exchange Fees, *available at* https://www nyse.com/markets/nyse/trading-info/fees; Laura Cardella, Jia Hao, and Ivalina Kalcheva, *Liquidity-Based Trading Fees and Exchange Volume* (working paper) (Aug. 1, 2017).
Exchanges divide brokers into tiers based on their trading volume at the exchange, and the broker's prices for the past month are determined by the tier the broker falls into. If a broker trades more at a particular exchange, then, it might enter a higher "tier" and pay lower prices for all of its trades during the relevant period. Thus, a broker near the threshold for entering a better tier on a certain exchange is incentivized to route all of its orders to that exchange to get a significant rebate windfall.
[8] 15 U.S. Code § 78f(b)(4), (b)(5), and (b)(8).

Conclusion.

The ASA appreciates the opportunity to provide these comments and looks forward to working with the IAC and the Commission on these critical issues.

Sincerely,

Christopher A. Iacovella

Christopher A. Iacovella
Chief Executive Officer
American Securities Association