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*Via E-Mail: rule-comments@sec.gov*

Ms. Vanessa Countryman  
Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1091

Re: Supplemental Information and Re-opening of Comment Period for Amendments to Exchange Act Rule 3b-16 Regarding the Definition of "Exchange"; File No. S7-02-22

Dear Ms. Countryman,

Fidelity Investments<sup>1</sup> ("Fidelity") appreciates the opportunity to provide additional comments on the Securities and Exchange Commission's ("SEC" or "Commission") proposed amendments to Rule 3b-16 under the Securities Exchange Act of 1934 ("Exchange Act") and Regulation Alternative Trading Systems ("Regulation ATS").<sup>2</sup> The Reopening Release does not alter the SEC's 2022 Proposed Rules on this topic, which would, among other items: (1) significantly expand the current definition of "exchange" under the Exchange Act; (2) eliminate certain existing exemptions under Regulation ATS for systems that exclusively trade government (Treasury and agency) securities; and (3) impose new obligations on filing and operational requirements for ATS. Instead, the Reopening Release requests further information and public comment on certain aspects of the Proposed Rules as applicable to all securities and the compliance dates and other alternatives for the Proposed Rules. Fidelity provides comments on

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<sup>1</sup> Fidelity and its affiliates are one of the world's leading providers of financial services, including investment management, retirement planning, portfolio guidance, brokerage, benefits outsourcing and other financial products and services to more than 40 million individuals and institutions, as well as through 3,600 financial intermediaries. Fidelity's carrying broker-dealer, National Financial Services LLC, currently operates the CrossStream ATS, an NMS Stock ATS. Fidelity generally agrees with the views expressed by the Securities Industry and Financial Markets Association and Investment Company Institute in their comment letters and Fidelity submits this letter to supplement their views on specific issues.

<sup>2</sup> Securities Exchange Act Release No. 94062 (Apr. 14, 2023), 88 FR 29448 (May 5, 2023) ("Reopening Release"). See also *Amendments Regarding the Definition of "Exchange" and Alternative Trading Systems (ATSs) That Trade U.S. Treasury and Agency Securities, National Market System (NMS) Stocks, and Other Securities*, Securities Exchange Act Release No. 94062 (Jan. 26, 2022), 87 FR 15496 (March 18, 2022) ("Proposed Rules", "Proposal", or "Proposing Release"). Fidelity's comments on the Proposing Release available at:

<https://www.sec.gov/comments/s7-02-22/s70222-20124034-280156.pdf> ("Fidelity's 2022 Comment Letter").

Capitalized terms not otherwise defined herein have the meaning ascribed to them in the Proposing Release and Reopening Release.

the Reopening Release to emphasize certain points made in Fidelity's 2022 Comment Letter and to respond to new, additional SEC requests for comment.

As outlined in Fidelity's 2022 Comment Letter, the Commission's proposed changes to Rule 3b-16 would fundamentally change the current definition of "exchange" which has provided investor protection and clear guidance to the marketplace for more than twenty years. In the Reopening Release, like the Proposing Release, the Commission has failed to provide evidence of issues that warrant this significant change and to adequately explain key terms in its proposed, revised definition of "exchange." If finalized in its current form, we continue to anticipate that the proposed, revised definition of "exchange" will impact many more systems than the Commission has identified and will cause confusion, impact liquidity, and stifle innovation in the marketplace. Our comments that follow address the following points.

- The Commission has failed to adequately justify its reasoning for this rulemaking;
- The Commission has failed to provide needed clarity and guidance on key terms. The proposed, revised definition of "exchange" under Rule 3b-16 remains broad and ambiguous;
- The Commission should finalize proposed rulemaking eliminating the Regulation ATS exemption for Government Security ATS, prior to finalizing any proposed revisions to the definition of "exchange"; and
- If, alternatively, the Commission determines to proceed with the proposed, revised definition of "exchange," which we recommend it does not, it should provide market participants substantial time to evaluate whether certain of their systems rise to the level of New Rule 3b-16(a) Systems and to complete significant operational and administrative requirements to register as a national securities exchange or ATS.

Each of these points is discussed further below.

*The Commission has failed to adequately justify its reasoning for this rulemaking.*

We agree that fair competition requires entities performing similar functions to be regulated similarly. Currently, Regulation ATS includes an exemption for trading venues that only trade government securities as defined under Section 3(a)(42) of the Exchange Act or repurchase and reverse repurchase agreements on government securities ("Government Security ATS"). These ATS are currently both exempt from exchange registration and are not required to comply with Regulation ATS.

In recognition of the important role ATS play in the government securities market, in 2020 the Commission proposed rules to, among other items, eliminate the Regulation ATS exemption

for Government Security ATS.<sup>3</sup> Eliminating this exemption would require these trading venues to: (1) register as broker-dealers; (2) become members of FINRA; and (3) comply with the investor protection and Commission oversight provisions of Regulation ATS. The Commission also proposed that Government Securities ATS file a new form, Form ATS-G, which would be subject to Commission review and made publicly available on the SEC website after becoming effective. In the 2020 Proposal, the Commission provided evidence that Government Security ATS were significant trading venues requiring Commission oversight and outlined the Commission's reasoning for removing the Regulation ATS exclusion for such ATS. Comment letters submitted were largely supportive of proposed Commission action.

However, rather than advance proposed rules on Government Security ATS, the SEC's Proposing Release sought to include Government Securities ATS under the Regulation ATS regime *and* to fundamentally change the current definition of "exchange" under which market participants evaluate which systems, across all asset classes, rise to the level of an "exchange," and relatedly, require compliance with Regulation ATS.

Our comments on the Proposing Release urged the SEC to clarify why a wholesale change to the definition of "exchange" was necessary, particularly when the change would impact all asset classes, not simply fixed income securities.<sup>4</sup> In response, the Reopening Release solicited comment largely regarding the impact of the proposed, revised definition of exchange in the context of "trading systems for crypto asset securities and trading systems that use distributed ledger or blockchain technology (DLT), including decentralized finance." That is, in the Reopening Release, the SEC again failed to identify existing marketplace issues that require a wholesale change to the definition of "exchange." This omission is particularly troublesome because the SEC has, and actively uses, enforcement tools to address systems that meet the current definition of "exchange" but fail to register as one.<sup>5</sup> Given its current authorities, the SEC should clearly explain why such a significant change to the definition of "exchange" is necessary, prior to any rulemaking on this topic.

*The Commission has failed to provide needed clarity and guidance on key terms. The proposed, revised definition of "exchange" under Rule 3b-16 remains broad and ambiguous.*

Current Rule 3(b)-16(a) under the Exchange Act defines an "exchange" as "An organization, association, or group of persons" that "(1) Brings together the orders for securities of multiple buyers and sellers; and (2) Uses established, non-discretionary methods (whether by

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<sup>3</sup> See *Regulation ATS for ATSS that Trade U.S. Government Securities, NMS Stock, and Other Securities; Regulation SCI for ATSS that Trade U.S. Treasury Securities and Agency Securities; and Electronic Corporate Bond and Municipal Securities Markets*, Exchange Act Release No. 90019 (Sept. 28, 2020) available at <https://www.sec.gov/rules/proposed/2020/34-90019.pdf> (hereinafter "2020 Proposal").

<sup>4</sup> Proposing Release at 15503. As the SEC notes, Rule 3b-16 applies to all securities, including government securities, corporate bonds, municipal securities, NMS Stocks, OTC equity securities, private restricted securities, repurchase agreements and reverse repurchase agreements, foreign sovereign, options, and, as the SEC notes in the Reopening Release, digital asset securities.

<sup>5</sup> For example, Press Release. Securities and Exchange Commission, "*SEC Charges Crypto Asset Trading Platform Bittrex and its Former CEO for Operating an Unregistered Exchange, Broker, and Clearing Agency*" April 17, 2023.

providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade.”<sup>6</sup>

The Proposing Release’s changes to the definition of “exchange” included, among other items: removing references to “orders” and “multiple” buyers and sellers; replacing “orders” with “trading interest”; changing “uses” to “makes available”; and referencing interactions of “buyers and sellers” instead of interactions of “orders.” The Commission also proposed to add “communication protocols” to Rule 3b-16(a) as an example of a non-discretionary method, provided by organization, association, or group of persons, to allow buyers and sellers to interact and agree to the terms of a trade. While the Commission provided examples of “communication protocol systems” in the Proposing Release, the Commission did not define the term. Fidelity’s 2022 Comment Letter urged the SEC to provide further clarity around certain key terms in the Proposing Release, including “communication protocols.” We observed that given the many different types of electronic communications systems used in trading, lack of a clear definition of “communication protocols” could bring a significant number of systems under the revised definition of “exchange” and create uncertainty as to what was/was not included in its scope.

In the Reopening Release, the Commission has not provided clarity and guidance on key terms and as a result, the proposed, revised definition of “exchange” remains broad and ambiguous. Moreover, Commission commentary in the Reopening Release regarding terms such as “makes available” and “established, non-discretionary” is confusing. We remain concerned that the proposed, revised definition of “exchange” will impact many more systems than anticipated.

For example, in the Reopening Release, the Commission states that the term “makes available” was intended to make clear that, in the event a party, *other than* the entity or persons which constitutes, maintains, or provides a marketplace designated as an “exchange,” performs a function of the exchange, the function performed by that third party would still be captured for purposes of determining the scope of the “exchange” under Exchange Act Rule 3b-16. We do not understand why the SEC has selected this broad definition of the term “makes available,” which could encompass a myriad of entities outside of an “exchange,” given a lack of evidence that such a broad definition is warranted. In its place, we recommend the Commission consider a more limited term, such as the original term “uses” or “establishes” that acknowledges the active role performed by an entity, or person, in developing an “exchange.”

Similarly, in the Reopening Release, the Commission has not provided a definition of “communication protocol” and instead solicits comment on how it should address non-discretionary methods under which buyers and sellers interact and agree to the terms of a trade. If the Commission wishes to regulate certain technology protocols as an “exchange,” it should clearly articulate the protocols it wishes to regulate based on investor protection, competitive or other regulatory considerations. If the Commission is not able to articulate the specific types of “communication protocols” it seeks to regulate, it should exclude this term as an example of a non-discretionary method under which buyers and sellers can interact and agree to the terms of a trade.

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<sup>6</sup> See 17 CFR 240.3b-16(a).

Likewise, the Commission provides confusing commentary regarding whether an investment adviser's order and execution management system ("OEMS"), as used by the investment adviser to manage their portfolio investments on behalf of regulated funds and other clients, may, or may not, meet the definition of "exchange." An investment adviser uses an OEMS to connect to trading venues. The OEMS itself does not establish protocols for trading on or through a trading venue – any such protocols typically are established by the trading venue to which the investment adviser's OEMS connects. From a policy standpoint, we do not believe that the Commission intended to require institutional asset managers to register as broker-dealers to operate systems for their own use, or to outsource this activity to broker-dealers. We recommend that the SEC explicitly exclude investment adviser's OEMS from the definition of "exchange," and treat these asset management systems as analogous to the SEC's proposed exemption in Rule 3(b)-16 for systems used by issuers to sell their own securities.

The SEC's lack of clarity on certain key terms in the definition of "exchange" presents a double disadvantage to the industry. Without the SEC's justification as to why the SEC believes revisions to the long-standing definition of "exchange" are necessary, the industry lacks understanding of the SEC's goals. Similarly, without understanding what the SEC hopes to achieve in the proposed, revised definition of "exchange," it is difficult to determine whether certain terms should be used over others.

As we wrote in Fidelity's 2022 Comment Letter, the importance of clear definitions in rulemaking is not simply an academic exercise. Industry participants face significant regulatory repercussions if they engage in activities that fall under the definition of "exchange" but fail to register as either a national securities exchange or as a broker-dealer and comply with Regulation ATS. As a matter of good rulemaking, market participants should be able to clearly understand whether they are, or are not, subject to a rule. Lack of regulatory clarity creates confusion and uncertainty and stifles innovation, competition, and liquidity as market participants become hesitant to offer services without a clear understanding of the regulatory status of their offering. Moreover, lack of clear definition regarding what is, and what is not, an exchange allows regulators to alter, and potentially expand, their interpretation of this term over time through inspections, examinations, and guidance all of which are outside the established rulemaking process and not reflected in cost benefit analysis.

*The Commission should finalize proposed rulemaking eliminating the Regulation ATS exemption for Government Security ATS, prior to finalizing any proposed revisions to the definition of "exchange."*

Several commenters to the Proposing Release, including Fidelity, expressed concern that trading systems that meet the criteria of Exchange Act Rule 3b-16(a), as proposed to be amended, ("New Rule 3b-16(a) Systems") would not be provided enough time to comply with their new regulatory obligation. To facilitate trading system operator's compliance with the Proposed Rules, the SEC requested further public comment on compliance dates for the Proposed Rules.

It remains unclear to us why the Commission determined to issue a proposed rulemaking seeking a wholesale change to the definition of "exchange," rather than proceed incrementally with

rulemaking designed to eliminate the Regulation ATS exemption for Government Security ATS.<sup>7</sup> We recommend the Commission take an incremental approach to rulemaking and first eliminate the Regulation ATS exemption for Government Security ATS, prior to finalizing any proposed revisions to the definition of “exchange.” This approach would focus market participant implementation efforts and provide increased investor protection and Commission oversight for a new type of ATS. This work could be performed simultaneously with further discussions on proposed revisions to the definition of “exchange.”

*If, alternatively, the Commission determines to proceed with the proposed, revised definition of “exchange,” which we recommend it does not, it should provide market participants substantial time to evaluate whether certain of their systems rise to the level of New Rule 3b-16(a) Systems and to complete significant operational and administrative requirements to register as a national securities exchange or ATS.*

If, alternatively, the Commission determines to proceed with the proposed, revised definition of “exchange,” which we recommend it does not, it should first provide justification as to why this change is needed. The Commission should also provide guidance on the revised definition of “exchange” in the form of clear definitions, examples of systems that fall within scope, frequently asked questions, and/or roundtable discussions to help inform understanding as to the Commission’s intended scope of the revised language.

The Commission should also provide market participants substantial time to evaluate whether certain of their systems rise to the level of New Rule 3b-16(a) Systems and complete significant operational and administrative requirements to register as a national securities exchange or ATS. Even for market participants who are currently broker-dealers and have experience with Regulation ATS, this evaluation and implementation process will be time consuming and potentially disruptive. For this reason, we suggest the Commission adopt a two-stage compliance date with the first compliance stage requiring the identification of New Rule 3b-16(a) Systems and the second compliance stage requiring completion of required registrations and forms.

For example, Fidelity broker-dealers have current systems that, while already subject to extensive FINRA and SEC regulation and oversight, including disclosure and recordkeeping obligations, may be subject to heightened Regulation ATS requirements under a proposed, revised definition of “exchange.” Given the significant operational and administrative costs of Regulation ATS compliance, we will need time to identify these systems as well as evaluate whether we wish to continue to offer them. We anticipate that other firms will undertake similar evaluations, resulting in an evolving, and potentially different, market landscape post rule-implementation.

If our broker-dealers determine to continue to offer systems identified as New Rule 3b-16(a) Systems, we will need time to potentially open new broker-dealers, develop initial ATS disclosure documents, as well as hire additional staff to help establish new disclosure processes. Simultaneously, we will need to update existing ATS disclosure documents to comply with new,

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<sup>7</sup> *Supra* note 3.

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concurrently issued, SEC proposed changes to Regulation ATS.<sup>8</sup> Any final SEC rulemakings issued concurrent with a final rule on this topic will further impact implementation efforts.<sup>9</sup> The amount of time ultimately needed for implementation will depend on the clarity of the SEC's final rulemaking, as well as the timeliness of SEC review of initial disclosure documents.

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Fidelity would be pleased to provide further information, participate in any direct outreach efforts the Commission undertakes, or respond to questions the Commission may have about our comments.

Sincerely,



Thomas Tesauro

cc:

The Honorable Gary Gensler, Chair  
The Honorable Hester M. Pierce, Commissioner  
The Honorable Caroline A. Crenshaw, Commissioner  
The Honorable Mark T. Uyeda, Commissioner  
The Honorable Jaime Lizárraga, Commissioner

Mr. Haoxiang Zhu, Director of the Division of Trading and Markets  
Mr. David Saltiel, Assistant Director, Division of Trading and Markets  
Mr. Tyler Raimo, Assistant Director, Division of Trading and Markets

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<sup>8</sup> *Supra* note 2.

<sup>9</sup> The breadth and depth of the current SEC administration's rulemaking agenda is notable, particularly during a time of market resiliency. The Commission has identified a number of rules that it may finalize in the up-coming twenty-four months pursuant to the SEC's Fall 2022 Regulatory Flexibility Agenda. If the SEC issues multiple final rules with overlapping compliance dates, available legal and compliance resources will be constrained at impacted firms.