CITADEL | Securities

May 26, 2020

Ms. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549–1090

Re: Market Data Infrastructure (File No. S7-03-20)

Dear Ms. Countryman:

Citadel Securities appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "Commission") on the proposal to update the national market system ("NMS") for the collection, consolidation, and dissemination of information with respect to NMS stocks (the "Proposal").[1]

The Proposal expands the information relating to NMS stocks that is required to be collected, consolidated, and disseminated by the securities information processors ("SIPs") by (a) revising the definition of a round lot to be tiered based on the price of a stock,[2] thereby more closely tracking the total value of an order compared to the current definition of 100 shares, and (b) adding information relating to depth-of-book and auctions.

We generally support this proposed expansion in the core data that will be disseminated by the SIPs, provided that it does not materially increase overall latency. We also support a round lot definition that addresses the significant increase in the number of high-priced stocks, and propose a slightly simplified approach below. However, we strongly disagree with the Commission's proposal not to apply the new round lot definition to the order protection rule and the prohibitions on locked and crossed markets. Instead, the Commission proposes to amend Regulation NMS such that Rules 610 and 611 only apply to orders of at least 100 shares. As detailed below, this establishes a much narrower order protection rule than was originally intended, introduces unnecessary complexity and confusion, and raises a number of questions that require further clarification.

[1] 85 Fed. Reg. 16726 (Mar. 24, 2020), available at: https://www.govinfo.gov/content/pkg/FR-2020-03-24/pdf/2020-03760.pdf.

[2] The proposed definition is tiered as follows:

Stock Price Group	**Round Lot**
$0.00 - $50.00	100 shares
$50.01 - $100.00	20 shares
$100.01 - $500.00	10 shares
$500.01 - $1,000.00	2 shares
$1,000.01 or more	1 share

The Proposal also introduces a decentralized consolidation model where competing consolidators would replace the exclusive SIP for each equities tape. Given the central role of a market data consolidator in U.S. equities market structure, we detail below the significant costs and complexities associated with this proposed change that, in aggregate, likely outweigh any potential benefits.

For both of these aspects of the Proposal, we recommend that the Commission engage in further outreach and solicit additional feedback from market participants prior to finalizing such fundamental changes to the Regulation NMS framework.

I. The New Round Lot Definition Should Be Universally Applied

The Proposal establishes a new round lot definition that is tiered based on the price of a stock, thereby more closely tracking the total value of an order compared to the current definition of 100 shares. While we support a tiered round lot definition based on the total value of an order, we suggest simplifying the Proposal by reducing the number of tiers and using a higher order value threshold than the $1,000 threshold referenced in the Proposal.[3]

More importantly, regardless of the round lot definition that is used, it should continue to universally apply under Regulation NMS, including for purposes of the order protection rule and the prohibitions on locked and crossed markets. Under the Proposal, the Commission proposes to amend Regulation NMS such that Rules 610 and 611 only apply to orders of at least 100 shares. This will result in the creation of two distinct NBBOs: (i) the NBBO containing quotes that qualify under the new round lot definition and (ii) a "protected NBBO" only containing quotes that are of at least 100 shares. In many cases, the "protected NBBO" will be wider than the NBBO, meaning that market participants may often trade-through the NBBO disseminated by the SIPs.

Creating a framework where market participants may regularly trade-through the NBBO disseminated by the SIPs represents a fundamental change to Regulation NMS that materially undermines the order protection rule and introduces significant complexity and confusion. At the moment, the dissemination and protection provisions of Regulation NMS are aligned, with the order protection rule applying to all round lot orders, which are orders considered to be economically material in size to merit dissemination by the SIPs, As a result, the displayed NBBO provides a transparent and objective standard against which investors can measure execution quality and economically material orders that improve the displayed NBBO are automatically protected from trade-throughs.

In contrast, under the Proposal, the order protection rule is materially narrowed such that it no longer provides protection to all economically material orders that are disseminated by the SIPs. In the Proposal, the Commission details the extent to which the current round lot definition no longer adequately captures orders that are economically material in size, given the increase in the number of high-priced stocks. The Proposal addresses this problem for much of Regulation NMS

[3] Proposal at 16742.

by creating a tiered round lot definition but then separately amends the scope of the order protection rule such that it no longer covers all orders that are considered to be round lots. As a result, orders of fewer than 100 shares that the Commission acknowledges are economically material will not be included in the "protected NBBO," undermining its use as an objective market-wide standard to measure execution quality.

In addition, market participants posting economically material orders of fewer than 100 shares that improve the displayed NBBO may not be protected from trade-throughs, potentially disincentivizing the posting of displayed limit orders, contrary to the objectives of Regulation NMS and leading to concerns regarding market fairness and investor confidence. In explaining the rationale for revising the round lot definition, the Proposal clearly focuses on enhancing protections for liquidity takers by ensuring they are able to access economically material orders of fewer than 100 shares in high-priced stocks. However, there is insufficient focus on the protections afforded to resting orders, and the consequences of permitting an economically material order of fewer than 100 shares that improves the NBBO and is disseminated by the SIPs to be traded-through if the order protection rule does not apply.[4]

A review of executed retail non-marketable limit orders handled by Citadel Securities during the month of April 2020 shows the significance of this issue:

- Apple (with a new round lot definition of 10 shares): 37% of orders would newly qualify as a round lot, but would not receive order protection;

- Tesla (with a new round lot definition of 2 shares): 64% of orders would newly qualify as a round lot, but would not receive order protection; and

- Amazon (with a new round lot definition of 1 share): 92.5% of orders would newly qualify as a round lot, but would not receive order protection.

The Commission asserts that leaving the scope of the order protection rule unmodified would result in a significant expansion, given the revised round lot definition.[5] However, this is not supported by data; instead, data shows that the scope of the order protection rule has significantly narrowed over time and applying the new round lot definition would simply serve to reverse this trend and appropriately cover orders that are economically material in size. Below, we analyze stocks in the Russell 3000 that were included in the index both in 2005 when Rule 611 was first

[4] We note that it has been argued that protected quote status is not required since best execution requirements would lead broker-dealers to access the better-priced order of fewer than 100 shares. If this is true, then there is no reason to fundamentally revise the scope of the order protection rule, as the outcome should be the same. If, however, revising the scope of the order protection rule does have a practical impact, and could lead to trade-throughs, then presumably the Commission has considered how often this should be expected to occur and the potential impacts on market functioning. We urge the Commission to further consider the costs of revising the scope of the order protection rule prior to finalizing the Proposal.

[5] Proposal at 16747.

adopted and in 2019 (approximately 1500 symbols in total). The table shows, for a given order size, the number of symbols for which that order size would receive order protection.

Order Size	Number of Symbols (2005)	Number of Symbols (2019)	% Change
$3,000	818	536	-34%
$4,000	1,078	712	-34%
$5,000	1,251	845	-32%
$6,000	1,357	944	-30%

This analysis clearly shows the erosion of the order protection rule over time: for a given order size and population of symbols, *the scope of the order protection rule has decreased by approximately one-third between 2005 and 2019*. As stock prices have increased (and stock splits have become less common), many fewer orders now receive order protection under Rule 611 than when it was first implemented. Therefore, applying the new tiered definition of a round lot would simply serve to reverse this trend and appropriately cover orders that are economically material in size. In contrast, affirmatively amending the scope of the order protection rule to only cover orders of at least 100 shares establishes a much narrower order protection rule than was originally intended, excluding many round lot orders that the Commission acknowledges are economically material.

Finally, we note that there are a number of practical questions that require further clarification, including:

- How are best execution obligations interpreted when the SIP contains both protected and unprotected quotes?

- What is the impact on the pricing of pegged orders, such as midpoint orders, due to setting a best-bid or best-offer with an unprotected quote?

- How is the routing of certain orders, such as ISOs, affected? Will market participants be required to make technological changes as a result?

- What will be the impacts of significantly increasing the number of locked/crossed markets between protected and unprotected quotes?

We also note that using quotations of less than 100 shares to form the NBBO for some symbols will increase existing limitations with certain Rule 605 execution quality statistics, given that these statistics benchmark executions to the NBBO without regard to the size of the quote. As a result, we recommend the Commission propose and adopt recommendations put forward by the Financial Information Forum to modernize Rule 605, including (a) creating a "marketable benchmark" statistic that reflects the size of the quote at the NBBO, (b) adding notional buckets as an additional method of categorization, and (c) incorporating all customer orders regardless of size.[6] This would

[6] https://www.sec.gov/comments/s7-02-10/s70210-5002077-182848.pdf.

increase the quality of disclosure provided to investors in the U.S. equities market, facilitating more accurate comparisons of broker-dealer execution quality

In light of the above, and the overall significance of fundamentally changing the scope of the order protection rule, we recommend the Commission further consider the associated costs and benefits and narrow the Proposal to focus specifically on market data infrastructure topics.

II. The Costs of Competing SIPs Outweigh the Benefits

The Proposal introduces a decentralized consolidation model where multiple "competing" consolidators replace the exclusive SIP for each equities tape. However, it is unclear how introducing multiple consolidators per tape addresses the market data fees imposed by exchanges, which is the purported purpose. Introducing multiple consolidators per tape can only be expected to have an impact on the incremental costs associated with aggregation and dissemination, not on underlying market data fees.

In addition, given the central role of a market data consolidator in U.S. equities market structure, there are significant costs and complexities associated with the Proposal, including:

- Each consolidator will provide its own version of the NBBO, introducing significant confusion to the critically important transparent and objective standard against which investors can measure execution quality;

- To the extent multiple consolidators per tape offer truly differentiated levels of service, how comfortable will market participants be not using the best offering and how should various relevant criteria be weighed, such as reliability, average latency, and peak latency?

- Will there be differences in the regulatory immunity granted to consolidator offerings from SRO and non-SRO entities?

In our view, these costs and complexities likely outweigh the potential benefits of multiple consolidators per tape. As noted above, multiple consolidators per tape should not be expected to decrease underlying exchange market data fees. In addition, the existence of multiple consolidators per tape will not eliminate geographic latency, and is not a unique solution compared to an exclusive SIP distributing consolidated data from multiple locations. In any case, as with the proposed change to the scope of the order protection rule, we believe this aspect of the Proposal would benefit from further consideration by both the Commission and market participants prior to being finalized, and should be the subject of a separate rulemaking.

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We appreciate the opportunity to provide comments on the Proposal. Please feel free to call the undersigned at [redacted] with any questions regarding these comments.

Respectfully,

/s/ Stephen John Berger

Managing Director

Global Head of Government & Regulatory Policy