By electronic mail to rule-comments@sec.gov

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Re: Further Definition of "As a Part of a Regular Business" in the Definition of Dealer and Government Securities Dealer  (Release No. 34-94524; File No: S7-12-22)

Dear Ms. Countryman:

Modern Markets Initiative ("MMI"), the education and advocacy organization devoted to the role of technological innovation in creating the world’s best markets, appreciates the opportunity to provide written comments to the U.S. Securities and Exchange Commission (the "SEC" or "Commission") in connection with the “Further Definition of "As a Part of a Regular Business" in the Definition of Dealer and Government Securities Dealer” (File No: S7-12-22)(the “Proposal”). MMI stands in broad support of global regulatory efforts to establish holistic, data-driven policies to best ensure the stability of the markets for all participants, and to offer tools for the advancement of secure savings and investment through innovation.

By way of background, MMI members collectively employ more than 2000 people in over 50 markets globally, and account for approximately 20 percent of daily trading volume in the US equity markets. MMI’s members deploy automated trading technology systems to enhance efficiency of trading for retail and institutional investors.

Benefits of Market Automation

The Proposal is motivated by the stated belief that an increase in electronic trading and the emergence of unregulated significant market participants could be a contributing factor to more frequent market disruptions, and that these market participants are directly affecting the provision of liquidity in the markets. However, over the past decades, the US equities markets,
and increasingly the US Treasury markets, have seen the benefits of market automation for retail investors, with benefits including:

- Narrowed bid-ask spreads and investor savings
- Enhanced transparency for market participants and regulators,
- More competition in price discovery
- Dependable liquidity in periods of volatility.

Automated trading technology has reduced the cost of trading for the average investor, both in direct trading costs and savings through tighter bid ask spreads. Investors saving for college, retirement, and institutional investors such as pension funds and university endowments have benefited from narrowed bid-ask spread, low cost trading and dependable liquidity. Specifically, over a decade, automation of the electronic intermediaries has brought down trading costs by 50 percent, and yielded 30 percent more in lifetime savings for investors.

**Importance of Transparency, Market Integrity, and Regulatory Oversight**

MMI appreciates the SEC’s intent in the Proposal to further support transparency, market integrity, and resiliency across the U.S. Treasury market and other securities markets, as it relates to ensuring that proprietary (or principal) trading firms and other market participants who are acting as dealers be, in fact, registered as “dealers.” MMI agrees it is important that dealers or those who engage in buying and selling of government securities as registered dealers should become members of a self-regulatory organization, and receive the benefits and obligations under the existing framework of federal securities laws.

**Concern About Arbitrary Thresholds, Potential for Market Distortion**

However, MMI expresses concern that some of the provisions in the Proposal appear arbitrary and could pose a risk of distorting the efficiency of the US securities markets and could adversely affect competition in liquidity provision.

MMI disagrees with the fundamental characterization of the activity in which traders engage. Principal traders are not dealers, as they do not have customers. They transact primarily on anonymous electronic trading venues or as counterparties to entities that are registered as dealers – in other words, they are the clients of dealers, rather than being dealers themselves. Traders do not provide “dealer services,” such as investment advice, extending credit, or lending securities, to any “clients.” They do not handle money or securities for any customer or third party. The Proposal appears to deem active traders “dealers” solely based on
the volume of securities they trade, which ignores long-standing judicial and SEC settled precedent on the distinction between a dealer and a trader.

We do not believe this reclassification of firms will “level the playing field,” rather, it threatens to reduce liquidity in markets. The costs of dealer registration, including capital requirements, SRO fees and compliance and reporting requirements among others, are significant and could limit trading activity and liquidity provision. New trading firms could face insurmountable barriers to entry, and smaller participants could exit the market, leading to fewer market participants, which would lead to a reduction in market liquidity.

Beyond the conflation of traders with dealers, we believe the thresholds to classify participants are also arbitrary: the $50 million threshold in total assets to be excluded from applicability of regulation; the $25 billion of Treasury securities traded monthly covering 4 of the past 6 calendar months. Further, MMI notes the potential for lack of clarity in instances in which an entity that is registered as a broker dealer in one market or instance, but may not be registered as a dealer in other markets.

Conclusion

MMI supports the overall objectives of increasing transparency and protecting investors, however we doubt the Proposal is the best way to achieve them. We strongly believe in transparency, but transparency and reporting can – and are – being achieved in other ways, including existing frameworks such as TRACE reporting for U.S. Treasury Securities and FINRA registered broker-dealers and CAT Reporting for options and equities trades. All trades conducted by a principal trading firm through registered broker-dealers are already reported and available to regulators for review and oversight. We note TRACE reporting will be expanded to cover banks as of September 2022. We believe it would be prudent to wait for existing requirements to go into effect and judge transparency once this data is being collected before promulgating a sweeping registration requirement that has the potential to create market disruption. With respect to customer protection, we question what benefit the registration of active (proprietary) traders will have in this regard, as these traders do not have customers or hold any customer assets.

Principal trading firms are also subject to risk limits, margin requirements, financial controls and market access control imposed by their prime brokers and executing broker-dealers. Therefore, the rule proposal is not needed to enhance market integrity or curb excessive risk taking. In addition, as the Commission notes, principal traders are already subject to anti-fraud and anti-manipulation provisions of the Exchange Act without being registered as a broker-dealer, and broker-dealers who have principal trading firms as customers are required to and do monitor the trading of the principal trading firms. Moreover, regulators can and do
receive information regarding principal trading firms through inquiry to the broker-dealers that they effect transactions through, subpoenas to the firm and regulatory reporting of transactions. Accordingly, the rule proposal does not seem necessary to enhance the oversight of principal trading firms activity or market integrity.

We respectfully submit that the SEC should engage in an additional study on the Proposal’s potential economic or adverse impacts on the markets and give further review to a holistic, principles-based regulation to avoid drawing an arbitrary line on what constitutes a “dealer,” which could have unintended consequences.

Thank you for your consideration.


Very truly yours,


Kirsten Wegner
Chief Executive Officer
Modern Markets Initiative