March 31, 2023

<u>Via E-Mail (rule-comments@sec.gov)</u>

Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Disclosure of Order Execution Information (Release No. 34-96493; File No. S7-29-22)
Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders (Release No. 34-96494; File No. S7-30-22)
Order Competition Rule (Release No. 34-96495; File No. S7-31-22)
Regulation Best Execution (Release No. 34-96496; File No. S7-32-22)

Dear Secretary:

Citigroup Global Markets Inc. ("CGMI")[1] appreciates the opportunity to comment on the above-referenced proposals: (i) Disclosure of Order Execution Information (the "Rule 605 Proposal");[2] (ii) Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders (the "Tick Size Proposal");[3] (iii) Order Competition Rule (the "OCR Proposal");[4] and (iv) Regulation Best Execution (the "Best Ex Proposal"[5] and, together with the Rule 605 Proposal, Tick Size Proposal and OCR Proposal, collectively the "Proposals"), issued by the U.S. Securities and Exchange Commission (the "SEC" or "Commission") on December 14, 2022.

CGMI generally supports the SEC's goals of enhancing transparency, promoting competition and reducing costs of trading. We actively participated in the drafting of

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[1] Citigroup Inc. ("Citi") is a diversified global financial services holding company whose businesses provide a broad range of financial services to consumer and corporate clients as well as governments and other institutions. Citi has some 200 million client accounts and does business in more than 100 countries. Citi's primary U.S. broker-dealer subsidiary, Citigroup Global Markets Inc. ("CGMI"), is registered as a broker-dealer in all 50 states, the District of Columbia, Puerto Rico, Taiwan and Guam, and is also a primary dealer in U.S. Treasury securities and a member of the principal United States futures exchanges. CGMI's affiliate, Citigroup Derivatives Markets Inc., is actively engaged in U.S. options market making. Additional information may be found at www.citigroup.com or www.citi.com.

[2] https://www.sec.gov/rules/proposed/2022/34-96493.pdf

[3] https://www.sec.gov/rules/proposed/2022/34-96494.pdf

[4] https://www.sec.gov/rules/proposed/2022/34-96495.pdf

[5] https://www.sec.gov/rules/proposed/2022/34-96496.pdf

SIFMA's comment letters on the Proposals and generally agree with many of the substantive points made in those letters.[6] However, we are submitting this separate comment letter to add some specific thoughts and recommendations of our own. In particular, while we agree with SIFMA that the Commission should not move forward with the OCR Proposal or Best Ex Proposal, we do think it is helpful to offer up constructive recommendations should the SEC decide to move forward despite this opposition.

Process: Taken together, the Proposals represent the most significant changes to Equity Market Structure since Regulation NMS was adopted in 2005. In the years since then, before undertaking ambitious changes to the regulatory landscape for equity trading, the Commission has typically chosen to issue concept releases (including the SEC's January 2010 Concept Release on Equity Market Structure[7]) or host public roundtables on such topics as Market Data / Access to Markets, Thinly Traded Securities and Retail Investor Fraud.[8] The purpose of those concept releases and public roundtables was to solicit feedback and input from the industry and the broader public to facilitate a more informed rulemaking process for the Commission. That was noticeably absent here. Given the clear inter-relationship among these four proposed rules and the sheer scale of proposed reforms, there was a compelling need for early and active engagement with stakeholders prior to the publication of the Proposals. We raise this point in the hope that any finalization of new rules will carefully consider input from the industry, and any subsequent implementation will be done equally as carefully, in stages, and only after thoroughly analyzing the impact of singular changes one-by-one.

Costs: Given the breadth of these proposed changes, implementation costs will be extremely burdensome on impacted firms and ultimately borne by investors. For example, changes to the minimum quoting increments under the Tick Size Proposal would require significant systems work to receive and analyze data from primary listing venues on a quarterly basis and then apply across all of a broker's systems. In addition, significant routing changes would be required under the OCR Proposal to send orders to auctions ahead of wholesalers, in addition to the myriad of vendor changes under the Rule 605 Proposal. The impact of implementing the proposed changes by smaller broker-dealers may be existential to existing firms and cost-prohibitive to new entrants, which seems counter to the SEC's stated goal of promoting competition. We, therefore, encourage the Commission at all stages of this rulemaking process to consider whether there are more cost-efficient ways to accomplish its stated goals.

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[6] "SIFMA's Omnibus Comment Letter" and "SIFMA's Fixed Income Best Ex Letter" are both being filed with the Commission concurrent herewith.

[7] https://www.sec.gov/rules/concept/2010/34-61358.pdf

[8] https://www.sec.gov/spotlight/equity-market-structure-roundtables

Substantive Areas of Agreement: Though we have a number of comments and criticisms on the specific proposed rules that are detailed below, we can initially identify several areas where we are broadly supportive of the Commission's Proposals:

- ***Rule 605 enhancements (Rule 605 Proposal)* –** CGMI and most of the industry has for some time supported updates to the disclosure of order execution information required by Rule 605 of Reg NMS. As far back as 2010 and 2014, CGMI has in previous comment letters made recommendations for how to enhance Rule 605 reporting.[9] We reiterate our support now for enhanced disclosure of order execution information, subject to certain recommendations made in SIFMA's Omnibus Comment Letter.

- ***Reducing access fees (Tick Size Proposal)* –** CGMI and SIFMA have previously supported a reduction in the access fee cap established under Rule 610 of Reg NMS.[10] We reiterate our support here for that aspect of the Tick Size Proposal, though we make some specific recommendations below for how best to do this in conjunction with a corresponding reduction in the minimum quoting increment.

- ***Accelerating implementation new round lot definitions (Tick Size Proposal)* –** CGMI supports the Tick Size Proposal's call to accelerate the SEC's previously-adopted changes to round lot definitions under the Market Data Infrastructure Rule, adopted by the SEC in December 2020.[11]

- ***Requiring fees and rebates to be known at the time of trade (Tick Size Proposal)*** – CGMI also supports the Tick Size's Proposal's requirement that exchange fees and rebates be made known at the time of trade, rather than the end of month, and further question the benefit of exchange tiers more broadly.

- ***Promoting competition for retail order flow (OCR Proposal)* –** Many of CGMI's institutional investor clients (who represent retail as well) view much of off-exchange (TRF) volume as "inaccessible liquidity" and we support the notion of

[9] See (i) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (May 5, 2010), available at https://www.sec.gov/comments/s7-02-10/s70210-174.pdf (our "May 2010 Letter"); and (ii) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (August 7, 2014), available at https://www.sec.gov/comments/s7-02-10/s70210-416.pdf (our "August 2014 Letter").

[10] See (i) our August 2014 Letter; and (ii) Letter from Tim Gately, Managing Director, Citigroup Global Markets Inc. (May 25, 2018), available at https://www.sec.gov/comments/s7-05-18/s70518-3712928-162399.pdf (our "May 2018 Letter"). See also Letter from Theodore R. Lazo, Managing Director, SIFMA (May 24, 2018), available at https://www.sec.gov/comments/s7-05-18/s70518-3706424-162467.pdf.

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

trying to increase interaction among retail and institutional order flow. However, CGMI does not support the OCR Proposal's overly prescriptive approach of requiring retail price improvement auctions; we believe the Commission should allow exchanges and alternative trading systems ("ATS's") more room for innovative solutions to achieve this goal.

Comments on Specific Proposed Rules

Tick Size Proposal

Tick Sizes: In our August 2014 Letter,[12] CGMI made five specific recommendations to improve Equity Market Structure, including an explicit acknowledgment that "any market structure changes need to be tailored to specific segments of the market, whether varied by capitalization (large/mid/small cap) or by share price," and further that "a 'one size fits all approach' is not appropriate in today's market." We maintain that view today and support the Commission's proposal to tier the minimum quoting increment based on spread.

That said, we respectfully suggest that the SEC's proposed \$0.0010 and \$0.0020 increments are too granular and should be eliminated. Several of our institutional clients oppose this level of granularity, as it would lead to excessive quoting and "noise" in the market, encourage "penny-jumping" of orders by an economically immaterial amount and result in significant information leakage to the market (making it much more difficult to trade in large sizes).[13] As proposed, this overly granular tick regime would also lead to an explosion of market data message traffic, thereby increasing reliance on the exchanges' proprietary market data feeds. This result seems to be in direct contravention of the Commission's intent as seen in the SEC's actions to bolster the SIP through unanimous adoption of the Market Data Infrastructure Rule in December 2020.

A broad industry consensus seems to have formed around the idea of changing the current penny-wide (\$0.01) minimum quoting increment to half-penny (\$0.0050) for a small subset of securities. In line with this sentiment, we propose different tiers for the minimum quoting increment:

- adopting a new \$0.0050 quoting increment for the most liquid, "tick-constrained" securities;

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[12] See Footnote 9 above.

[13] These concerns are not new – in fact, we made very similar arguments in our May 2010 Letter.

- retaining the current $0.01 quoting increment for the majority of symbols (maintaining the status quo would lead to fewer unintended consequences and lower implementation costs); and

- implementing a wider $0.05 quoting increment for the most illiquid and/or high-priced securities, consistent with a recommendation we made in our May 2010 Letter.

We agree with the Commission that the minimum trading increment should be uniform regardless of the trading center, to foster a more level playing field among exchanges and wholesale market makers. However, we do not believe that the minimum quoting and minimum trading increment need to be the same, and in fact should not be the same; doing so would likely eliminate some of the very significant price improvement afforded to retail order executions. We support a minimum trading increment of $0.0010; this would level the playing field while still allowing meaningful price improvement for retail orders to continue.[14]

Access fees: CGMI has previously supported a reduction from the current 30-mil access fee cap (30 cents per 100 shares) under Rule 610 of Reg NMS to less than 10 mils, as spreads have narrowed and commissions have decreased considerably since Reg NMS was adopted in 2005.[15] To coincide with the changes to the minimum quoting increment we proposed above, and reiterating prior comments that a "one size fits all approach" is not appropriate in today's market, we propose a tiered approach to access fee caps:

- we believe the access fee cap should be reduced to 5 mils for the most liquid, "tick-constrained" securities that would now be subject to a $0.0050 minimum quoting increment;

- further, the cap should be reduced to 10 mils for the majority of names still covered by the $0.01 minimum quoting increment.

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[14] What level of price improvement is "meaningful" vs. "de minimis" has been debated for many years; for our previous thoughts on this issue, please see (i) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (October 22, 2013), available at https://www.sec.gov/comments/4-657/4657-24.pdf (our "October 2013 Letter"); and (ii) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (December 22, 2014), available at https://www.sec.gov/comments/4-657/4657-73.pdf (our "December 2014 Letter").

[15] See our August 2014 Letter and our May 2018 Letter. The Commission also unanimously approved a Transaction Fee Pilot in December 2018 to reduce the access fee cap, available at https://www.sec.gov/rules/final/2018/34-84875.pdf.

- Recognizing that a lower access fee cap will necessitate lower exchange rebates – which could have a negative impact on liquidity, especially in illiquid securities – we would support leaving the access fee cap at 30 mils for illiquid securities subject to the new $0.05 minimum quoting increment. This would allow exchanges to continue to provide meaningful rebates to incentivize liquidity provisioning in symbols that need it most.[16]

Exchange tiers: As mentioned above, CGMI supports the Tick Size's Proposal's requirement that exchange fees and rebates be made known at the time of trade, rather than the end of month, and we further question the benefit of exchange tiers more broadly. Many of CGMI's institutional clients are increasingly measuring their execution costs all-in, inclusive of exchange fees. We view exchange tiers as anti-competitive in that they require significant scale to effectively offer the most competitive cost. Tiers can discourage innovation by not rewarding superior routing strategies and techniques, and can make it more difficult for smaller brokers and new entrants to the market who might lack scale. This can discourage market-making activity from smaller brokers who will have higher costs than larger wholesale market makers, and as such may be unable to provide the level of price improvement to retail orders that larger wholesale market makers can. All of this leads to a less competitive market, in our view.

Finally, the SEC should establish a transparent structured process to evaluate whether proposed changes to minimum quoting and trading increments and access fees are actually improving the execution experience. Ideally we would like to see more liquidity and depth, and a more stable quote with less quote flickering (possibly measured by quote-to-trade ratios). If these proposed changes are not having the desired effect, then there needs to be a clearly articulated off-ramp / kill-switch to unwind these changes and return to current quoting increments and access fee caps.

<u>Best Ex Proposal</u>

It is our view that the current FINRA and MSRB guidance on best execution is more than sufficient for brokers, and we do not see an immediate need for an additional set of best execution parameters from the SEC. We respectfully suggest that the Commission's Best Ex Proposal is redundant and would be extremely costly to implement, and its applicability to fixed income markets is highly problematic.

However, if the Commission is intent on issuing its own Best Execution Rule, we make the following recommendations to ensure it is workable and not overly prescriptive:

[16] It is worth reiterating our previously expressed view in our May 2018 Letter that this entire issue could be mitigated more simply by a move to basis point pricing in the U.S. (as in Europe and much of the rest of the world).

- The Commission should make very clear that its Best Execution Rule would take priority over and supersede FINRA's and MSRB's guidance, rather than simply add to them. If the Commission opts instead to allow three distinct best execution rules to remain in effect, then the rules need to be harmonized to the maximum extent possible. Otherwise brokers will not know which set of guidance they are obligated to follow, and areas of conflict among the rules resulting from multiple regulatory standards could lead to a worse execution experience for investors.

- Consistent with the recommendation in SIFMA's Fixed Income Best Ex Letter, CGMI strongly supports an exemption for institutional investor transactions in fixed income markets. The Best Ex Proposal attempts to apply a predominantly equities-centric set of principles to fixed income markets, ignoring the differences between those markets – most notably, the equities market is predominantly an agency market, while fixed income is predominantly a principal market. Most institutional customers are sophisticated and conduct their own best execution analyses, and should not be treated the same as retail customers.

- The Commission should move away from the idea of a heightened best execution standard for "conflicted transactions", instead relying upon the enhanced transparency and disclosures offered by the Rule 605 Proposal's changes. If the "conflicted transactions" standard is retained, the standard needs to be clarified to avoid the likelihood of *post hoc* regulation by enforcement. In particular, the SEC should make clear that simply obtaining a rebate from a public exchange should not subject a broker to a heightened best execution standard for "conflicted transactions."

OCR Proposal

While CGMI supports the SEC's goal of promoting greater competition for retail order flow, we do not support the OCR Proposal and respectfully urge the Commission not to adopt it as a final rule. The OCR Proposal fails to identify a problem that needs to be solved in a market where retail investors currently have access to ample liquidity in most securities, receive quick and efficient executions at or better than the price they see on their computer screens at time of order entry, all with zero commissions and virtually limitless investing resources at their fingertips. This investing experience is the result of intense free market competition for the privilege of executing these orders. In our opinion, the OCR Proposal's economic analysis fails to justify why a wholesale and very costly overhaul of the current ecosystem is warranted.

Adopting the OCR Proposal as a final rule will likely do more harm than good for the market for retail orders, particularly for illiquid securities. When the Commission adopted Reg NMS in 2005, the issue of order-by-order vs. venue-by-venue competition was intensely debated. Adopting a venue-by-venue approach ensured that wholesale market makers would be commercially obligated to make markets in all securities, not just the most liquid. By proposing to move from venue-by-venue competition to order-by-order competition, we believe the likely outcome for less liquid securities is a considerably worse execution experience, as market makers who are currently incentivized to provide liquidity across all liquidity profiles may pull back due to lack of cross-subsidization. This seems to be in direct contravention of the Commission's previous efforts to encourage more liquidity for thinly traded securities.[17] And as with the Tick Size Proposal, this very prescriptive auction mechanism would similarly lead to an explosion of market data message traffic and increase reliance on the exchanges' proprietary market data feeds, in direct contravention of the Commission's Market Data Infrastructure Rule in December 2020.

Further, forcing retail orders into price improvement auctions at exchanges would leave a very significant issue unresolved – who would be responsible to make retail customers whole in the event of any issues with the operation of these auctions? As various technology failures at exchanges have demonstrated over the past decade – from Nasdaq's mishandling of the Facebook IPO in May 2012, to NYSE's recent issues with its opening auction on January 24, 2023 – the for-profit exchanges are insulated from liability under their exchange rules as well as the judicial construct of SRO regulatory immunity. Fortunately for retail investors, the wholesale market makers typically make their retail customers whole, even when the problems were outside of their control and in most cases caused directly by the exchanges themselves. This safeguard would disappear under the OCR Proposal, and retail investors would have no such recourse against the for-profit exchanges.[18]

The OCR Proposal is overly prescriptive and forgoes the possibility of innovation by market participants. To help facilitate greater interaction among retail and

[17] https://www.sec.gov/rules/policy/2019/34-87327.pdf

[18] The need to overturn the judicial construct of regulatory immunity for commercial activities of exchanges and to right-size the exchanges' absurdly low rules-based liability limits is a topic on which CGMI has written for many years. See (i) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (August 22, 2012), available at https://www.sec.gov/comments/sr-nasdaq-2012-090/nasdaq2012090-5.pdf; (ii) our August 2014 Letter; (iii) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (March 2, 2020), available at https://www.sec.gov/comments/4-757/4757-6904770-211156.pdf; and (iv) Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (February 25, 2021), available at https://www.sec.gov/comments/4-698/4698-8419819-229522.pdf.

institutional order flow, we encourage the SEC to foster an environment of free market competition and encourage more innovation among exchanges and ATS's. We believe this can be achieved by reinvigorating the exchanges' retail liquidity programs and other innovative ideas, such as the Members Exchange's (MEMX) Retail Midpoint Liquidity Program proposal.[19]

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[19] https://www.sec.gov/rules/sro/memx/2021/34-92844.pdf

We sincerely appreciate the opportunity to comment on the Proposals and all equity market structure issues, and we welcome feedback from all market participants on our above recommendations. CGMI looks forward to continuing its dialogue on these matters with the Commission and its Staff. If you have any comments or questions, please do not hesitate to contact me.

Sincerely,

/s/ Tim Gately

Tim Gately
Managing Director
Head of Equities Sales, Americas

cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
The Honorable Mark T. Uyeda, Commissioner
The Honorable Jaime Lizárraga, Commissioner
Haoxiang Zhu, Director, Division of Trading and Markets
Jessica Wachter, Director, Division of Economic and Risk Analysis