

January 23, 2023

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

Re: IntelligentCross ATS Proposal (File No. SR-FINRA-2022-032)

Dear Ms. Countryman:

Citadel Securities appreciates the opportunity to provide comments to the Securities and Exchange Commission (the “Commission”) on the proposal by the Financial Industry Regulatory Authority, Inc. (“FINRA”) to add the IntelligentCross ATS to the Alternative Display Facility (the “FINRA Filing”).¹

While we do not object to alternative trading systems utilizing the FINRA Alternative Display Facility (“ADF”), the FINRA Filing incorrectly asserts that the IntelligentCross displayed quotations would qualify as “protected quotations” under Commission regulations. As detailed below, the FINRA Filing’s reliance on staff guidance that purports to deem intentional access delays of less than a millisecond as automatically *de minimis* for purposes of accessing displayed quotations is misplaced and contrary to Commission action. In fact, the IntelligentCross matching process includes an intentional delay that contains a number of novel and untested features that operate to impair fair and efficient access to displayed quotations, none of which are adequately assessed in the FINRA Filing.² In light of the absence of the required analysis, the FINRA Filing should be disapproved.

More generally, we urge the Commission to reconsider its approach to assessing whether displayed quotations subject to intentional delays can be considered “protected quotations.” By attempting to re-define the term “immediate” through an interpretation that establishes an amorphous *de minimis* standard, the Commission continues to be faced with requests for exceptions, which in aggregate, risk considerable harm to the most liquid and efficient equities market in the world. Instead, to the extent modifications to the definition of a “protected quotation” are deemed necessary, the Commission should engage in that exercise through the regular rulemaking process.

¹ 87 FR 79401 (Dec. 27, 2022), available at: <https://www.finra.org/sites/default/files/2022-12/sr-finra-2022-032-federal-register-notice.pdf> (the “FINRA Filing”).

² As set forth in the FINRA Filing, IntelligentCross “establishes a matching schedule using an overnight optimization process that uses historical performance measurements from prior days’ matches across all three IntelligentCross ASPEN books. Match schedules are defined by minimum/ maximum time bands for each security, and these bands can have a minimum time of 150 microseconds and a maximum time of 900 microseconds [. . .] The time of the actual match event is randomized within the match event band throughout the course of the trading day.”

I. Intentional Delays Of Less Than 1 Millisecond Are Not Automatically *De Minimis*

In order to qualify as a “protected quotation” under Commission Regulation NMS, the IntelligentCross displayed quotations must meet the definition of an “automated quotation.”³ The “automated quotation” definition requires that these displayed quotations can be “immediately and automatically” executed against an incoming IOC order.⁴

Despite the Commission specifically recognizing in Regulation NMS that the term “immediate” means that “a trading center’s systems should provide the fastest response possible *without any programmed delay* (emphasis added),”⁵ the Commission nonetheless re-defined the term “immediate” in a 2016 Interpretation as “not precluding a *de minimis* intentional delay—*i.e.*, a delay so short as to not frustrate the purposes of Rule 611 by impairing fair and efficient access to an exchange’s quotations.”⁶ The Commission’s re-definition of “immediate” is inconsistent with the plain text of Regulation NMS and therefore invalid.⁷ We remain deeply concerned about the Commission employing an “Interpretation” instead of notice-and-comment rulemaking to materially change the definition of a key term in Regulation NMS.⁸ Nevertheless, the *de minimis* test continues to be used by the Commission to assess whether displayed quotations subject to intentional delays can qualify as “protected quotations.”

However, in the 2016 Interpretation, the Commission explicitly rejected setting a bright line threshold for evaluating whether an intentional delay is *de minimis*. Although the Commission initially proposed to include a bright line threshold that would automatically deem intentional delays of less than a millisecond *de minimis*,⁹ this was removed in the final 2016 Interpretation, with the Commission stating:

At this time, the Commission is not adopting the proposed guidance under this interpretation that delays of less than one millisecond are *de minimis*. The Commission believes that, in light of the evolving nature of technology and the markets, and the need to assess the impact of intentional access delays on the markets, establishing a bright line *de minimis* threshold is not appropriate at this time. Rather, the Commission believes that the interpretation is best focused on whether an intentional delay is so short as to not frustrate the purposes of Rule 611 by

³ 17 C.F.R. § 242.600(70)–(71).

⁴ *Id.* § 242.600(6).

⁵ 70 FR 37496 (June 29, 2005) at 37519, available at: <https://www.sec.gov/rules/final/34-51808fr.pdf>.

⁶ 81 FR 40785 (June 23, 2016) at 40786, available at: <https://www.gpo.gov/fdsys/pkg/FR-2016-06-23/pdf/2016-14876.pdf> (the “2016 Interpretation”).

⁷ *See, e.g., Am. Fed’n of Gov’t Emps., AFL-CIO, Local 3090 v. Fed. Labor Relations Bd.*, 777 F.2d 751, 758 (D.C. Cir. 1985) (agency action that is inconsistent with existing regulations cannot be sustained).

⁸ *See* Citadel Letter to the Commission (April 14, 2016), available at: <https://www.sec.gov/comments/s7-03-16/s70316-11.pdf>.

⁹ 81 FR 15660 (March 24, 2016) at 15665, available at: <https://www.govinfo.gov/content/pkg/FR-2016-03-24/pdf/2016-06633.pdf>.

impairing fair and efficient access to an exchange’s quotations. As it makes findings as to whether particular access delays are *de minimis* in the context of individual exchange proposals, the Commission recognizes that such findings create common standards that must be applied fairly and consistently to all market participants.¹⁰

The FINRA Filing does not evaluate or make any such findings regarding whether the IntelligentCross displayed quotations are subject to an intentional delay that frustrates the purposes of Rule 611 by impairing fair and efficient access, such as (i) the rationale for the delay, and (ii) whether it has specific features that impair fair and efficient access to displayed quotations. Instead, the FINRA Filing simply points to subsequent guidance issued by SEC staff that purports to re-establish the bright line threshold of one millisecond that was explicitly rejected by the Commission.¹¹

Importantly, the FINRA Filing’s reliance on Commission staff’s “guidance” is inappropriate. As the guidance document candidly acknowledges, staff statements “are not rules, regulations, or statements of the Securities and Exchange Commission,” nor have they been “approved” by the Commission.¹² Moreover, the staff’s guidance document concededly “does not address whether any particular access delay would be approved by the Commission as consistent with the Commission’s [2016] [I]nterpretation.”¹³

Those disclaimers are necessary because Commission staff has no authority to depart from the Commission’s 2016 Interpretation. Even assuming the 2016 Interpretation is an interpretative, rather than a legislative rule, interpretative rules bind agency employees—including Commission staff.¹⁴ Commission staff was accordingly bound by the Commission’s determination that “establishing a bright line *de minimis* threshold is not appropriate at this time.”¹⁵ Rather than adhere to that determination, however, Commission staff issued guidance that purports to take a policy step the Commission expressly declined to take for itself. It lacked any authority to do so.¹⁶ The Commission should direct the staff to formally withdraw its unauthorized guidance, which only sows confusion about the Commission’s current regulatory framework regarding intentional delays.

¹⁰ 2016 Interpretation at 40792-93.

¹¹ FINRA Filing at 79403 and Staff Guidance on Automated Quotations under Regulation NMS (June 17, 2016), available at: <https://www.sec.gov/divisions/marketreg/automated-quotations-under-regulation-nms.htm>.

¹² See Staff Guidance on Automated Quotations under Regulation NMS (June 17, 2016)

¹³ See *id.*

¹⁴ See *Yale-New Haven Hosp. v. Leavitt*, 470 F.3d 71, 80–81 (2d Cir. 2006); *Splane v. West*, 216 F.3d 1058, 1064 (Fed. Cir. 2000) (“interpretive rule . . . was certainly binding on agency officials insofar as any directive by an agency head must be followed by agency employees”); *Warder v. Shalala*, 149 F.3d 73, 82 (1st Cir. 1998) (“[A]n interpretative rule binds an agency’s employees . . .”) (quoting Kenneth C. Davis & Richard J. Pierce, Jr., *Administrative Law Treatise* § 6.3 (3d ed. 1996 & Supp. 1997)), *abrogated on other grounds by Azar v. Allina Health Servs.*, 139 S. Ct. 1804 (2019).

¹⁵ 2016 Interpretation at 40792-93.

¹⁶ See *supra* note 14.

Improper staff guidance notwithstanding, the Commission has never identified any facts or changed circumstances that would justify a departure from its 2016 conclusion that a “bright line *de minimis* threshold is not appropriate.”¹⁷ Under that interpretation, the key inquiry is “whether an intentional delay is so short as to not frustrate the purposes of Rule 611 by impairing fair and efficient access to an exchange’s quotations.”¹⁸ Rather than provide a basis for such a finding—such as evidence that the IntelligentCross intentional delay lacks specific features that would impair fair and efficient access—the FINRA Filing simply assumes that any sub-millisecond intentional delay is *de minimis*. Accordingly, the Commission should reject the FINRA Filing as inconsistent with the 2016 Interpretation.

II. The IntelligentCross Intentional Delay Is Not *De Minimis*

The IntelligentCross intentional delay contains a number of novel features that have never been applied by a market center to protected quotations. These features clearly operate to frustrate the purposes of Rule 611 by impairing fair and efficient access to displayed quotations. These features are not assessed in the FINRA Filing nor have they been assessed previously by the Commission in the context of other intentional delays.

A. Displayed Quotes Can Be Canceled After An Incoming Order Reaches the IntelligentCross Matching Engine

According to the FINRA Filing, an incoming order may not execute against a resting order on IntelligentCross if the resting order is canceled prior to the next match event.¹⁹ Specifically, a resting order can be canceled “at any time prior to the match.”²⁰ This means that the following scenario can occur: (1) a market participant displays a bid (offer) at the NBB (NBO) on IntelligentCross, (2) an incoming order is routed to execute against that displayed quote, (3) the incoming order is received by IntelligentCross, (4) a liquidity provider cancels the displayed quote after the incoming order is received by IntelligentCross, and (5) no execution occurs. This scenario is precisely what the definition of a “protected quotation” in Regulation NMS was intended to prevent.

We note the scenario above is not hypothetical. According to the FINRA Filing, over 4% of potential matches were not executed due to the liquidity provider canceling its displayed quote

¹⁷ 2016 Interpretation at 40792-93; *see, e.g., Saget v. Trump*, 345 F. Supp. 3d 287, 300 (E.D.N.Y. 2018) (“Even if the new policy is interpretive, Defendants would be required to provide a reasoned explanation of the change in position.”); *Centro Presente v. United States Dep’t of Homeland Sec.*, 332 F. Supp. 3d 393, 417 (D. Mass. 2018) (“[E]ven interpretive changes ‘must be addressed expressly, at least by the agency’s articulate recognition that it is departing from precedent.’”) (quoting *Nat’l Labor Rel. Bd. v. Lily Transp. Corp.*, 853 F.3d 31, 36 (1st Cir. 2017)).

¹⁸ 2016 Interpretation at 40792-93.

¹⁹ FINRA Filing at 79402, FN 22.

²⁰ *Id.* at 79402, FN 23.

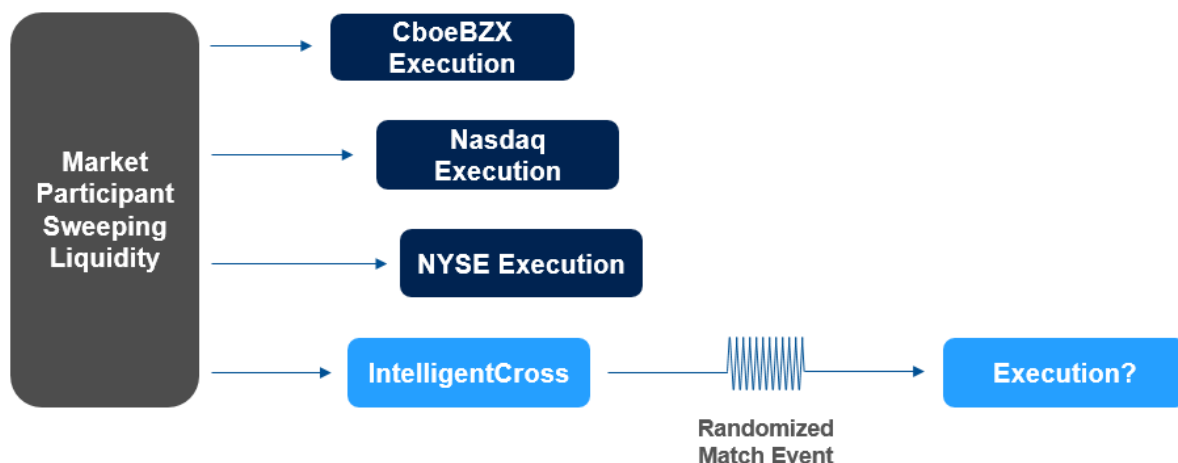
after an incoming order reached the IntelligentCross matching engine (but during the period in which the matching engine delays the match for up to 900 microseconds).²¹

It is also important to note that this scenario is clearly distinguishable from delays that arise due to geographic latency. With respect to geographic latency, the cancel message from the liquidity provider (step 4 above) would be subject to the same latency as the incoming order routed to execute against the displayed quote (step 2 above). Therefore, as long as the cancel message was sent after the incoming order reached the IntelligentCross matching engine, an execution would still occur before the cancel message was received.²²

While it is already material that over 4% of potential matches were not completed because a displayed order was canceled, this figure likely understates expected cancellation rates in the event IntelligentCross was granted “protected quotation” status and market participants were required to route order flow to the venue. To provide one example why, consider the execution of a larger order across multiple venues once market participants must attempt to access the displayed quote on IntelligentCross (see diagram below). Assuming the routing broker-dealer attempts to sweep displayed liquidity from each venue as quickly as possible, executions would occur on venues other than IntelligentCross (and be visible in market data feeds) before the next match occurs on IntelligentCross due to the operation of the intentional delay. A liquidity provider posting a resting order on IntelligentCross would be able to view this execution activity in the market data feeds, and anticipate that an incoming order was also sent to IntelligentCross, and then determine whether or not to cancel its resting quote before the incoming order is executed. This free option for liquidity providers means that incoming orders are likely to be filled only when the market is moving in the opposite direction (i.e. when commercially beneficial for the liquidity provider).

²¹ *Id.* at 79403.

²² This scenario also raises questions as to whether the IntelligentCross displayed quotes should be considered “automatically” executable as required by Commission regulations since the party providing the displayed quote has complete discretion to cancel its quote, even after the incoming order has been received by IntelligentCross. This feature is novel compared to all other market centers, and Commission regulations specify that “a quotation will not qualify as ‘automated’ if any human intervention after the time an order is received is allowed to determine the action taken with respect to the quotation.”



Importantly, the length of the intentional delay on IntelligentCross (up to 900 microseconds) would provide ample time for a liquidity provider to cancel its resting quote if advantageous to do so. While the FINRA Filing suggests the intentional delay may be as short as 150 microseconds, an analysis of our trading activity on IntelligentCross over the past three months shows that the intentional delay was almost never less than 500 microseconds, and was 800 to 900 microseconds in length for approximately 75% of IOC executions in the relevant ASPEN Fee/Fee order book.²³ As noted above, this type of intentional delay is fundamentally different than any geographic latency applicable to all market participants, evidenced by the fact that resting orders can be canceled after an incoming order has navigated any geographic latency and has been received by IntelligentCross.

Notably, the FINRA Filing provides no detail or analysis of how the IntelligentCross intentional delay is set in practice, and whether it impairs fair and efficient access to displayed quotations by allowing resting orders to be canceled after an incoming order is received.

B. The Randomized Nature of the Intentional Delay Increases the Harm

According to the FINRA Filing, each symbol on IntelligentCross has a specific matching schedule that is computed each day, and the actual match event time (or length of the intentional delay) is “randomized within the match event band throughout the course of the trading day.”²⁴ This means that market participants will not know the actual length of the intentional delay for any given symbol.

In evaluating other intentional delays, the Commission has accorded considerable weight to the theoretical possibility that market participants could adopt routing strategies to account for the intentional delay by staggering order routing such that orders arrive (and are executed) at different

²³ IntelligentCross has two other limit order books which are not covered by this filing.

²⁴ *Id.* at 79402.

venues at the same time.²⁵ This purported solution to navigating intentional access delays is even more unworkable when market participants do not know the actual length of the intentional delay at any given time (and when the length of the delay can frequently change).

Again, the FINRA Filing does not assess whether this aspect of the IntelligentCross intentional delay impairs fair and efficient access to displayed quotations.

C. The Intentional Delay Prevents Executions Even When Both Parties Wish To Transact

According to the FINRA Filing, an incoming order may not execute against a resting order on IntelligentCross if the NBBO moves between the time an order is received and the next match event.²⁶ Based on the example in the FINRA Filing,²⁷ the following situation can and does occur: (1) a market participant displays a bid (offer) at the NBB (NBO) on IntelligentCross, (2) an incoming sell (buy) order is routed to execute against that displayed quote, (3) the incoming order is received by IntelligentCross (and can be executed against the displayed quote), (4) during the IntelligentCross delay, the NBBO has moved in way that would result in a trade-through if the orders are now matched, and (5) the execution does not occur.

This scenario results in nearly 5% of potential matches not being completed, further underscoring the material nature of this intentional delay.²⁸ Again, this is precisely a scenario that the definition of a “protected quotation” in Regulation NMS was intended to avoid, yet the FINRA Filing does not assess whether this aspect of the IntelligentCross intentional delay impairs fair and efficient access to displayed quotations.

D. The Matching Process Appears Generally Incompatible With Protected Quotations

The Commission has never before granted “protected quotation” status to a matching process that uses discrete match events. This would treat the IntelligentCross displayed quote as equivalent to those on other market centers even though the matching of counterparties and the execution of transactions only occurs after the match event is conducted. This timing disconnect leads to many

²⁵ We note there are many reasons why a market participant may not elect to do this practice, as conforming to the lowest denominator (i.e. the longest time to execution) may risk missing out on liquidity available on other venues that could otherwise be accessed more quickly.

²⁶ FINRA Filing at 79403.

²⁷ *See id.* (“As another example, assume the NBBO in XYZ stock is \$10.00 × \$10.01 at 9:30:00.000000 and ASPEN Fee/Fee is displaying a limit order to buy at \$10.00. At 9:30:00.000010, ASPEN Fee/Fee receives a sell order to sell at \$10.00. At 9:30:00.000040—the time of the next scheduled match event in XYZ stock—the NBBO has changed and is now 10.01 × 10.02. A match will not occur because ASPEN Fee/Fee will not execute a match outside of the NBBO (i.e., the resting order is now nonmarketable) except that, as set forth in IntelligentCross’ summary, if the sell order were an ISO, an execution would occur at \$10.00 at the scheduled match event time.”).

²⁸ FINRA Filing at 79403.

of the concerns detailed above and the Commission should fully consider the associated implications through notice-and-comment rulemaking.

Based on the above, it is clear that the FINRA Filing does not provide the Commission with sufficient basis to make an affirmative finding that the filing is consistent with the Exchange Act. The required assessment of whether or not an intentional delay is *de minimis* must consider the impact of the intentional delay on fill rates and execution quality and whether it operates to frustrate the purposes of Rule 611 by impairing fair and efficient access to displayed quotations. Based on the data in the FINRA Filing, nearly 9% of executable transactions do not occur because of the reasons discussed above, which is certainly not *de minimis*. In addition, as detailed above, we would expect these figures to further increase if market participants are required to route order flow to the venue.

III. The Commission Should Reconsider the 2016 Interpretation

This filing is the latest example of a trading venue attempting to design an intentional delay that is considered *de minimis* under the 2016 Interpretation and that yet promises to increase its market share by giving certain market participants a competitive advantage that is not permitted on our largest and most important exchanges (i.e. expressly not *de minimis*).

Each time a new variation of an intentional delay is approved as *de minimis* under the 2016 Interpretation, the fabric of our equities markets frays. As intentional delays proliferate, with varying lengths, displayed quotes become an increasingly inaccessible mirage, harming investor confidence and execution quality. Liquidity providers on these special venues can free-ride on the pricing heuristics and risk-taking capabilities of others by price-matching, with a free option to cancel later. Compelling market participants to access this fleeting liquidity limits their ability to act in their own economic interest and impairs overall market competition to the detriment of total welfare, as rents are directed to a small subset of market participants. Market volatility is likely to become more pronounced, as quote fading increases and fill rates decline.

The Commission has recently demonstrated that it has the capability to propose modifications to any aspect of equity market structure through the notice-and-comment process. To the extent modifications to the definition of a “protected quotation” are deemed necessary, then the Commission should engage in that exercise through the regular rulemaking process. By contrast, the Commission should not attempt to re-define the term “immediate” through an interpretation that establishes an amorphous *de minimis* standard, which has only resulted in the Commission continually being faced with requests for exceptions, which in aggregate risk considerable harm to the most liquid and efficient equities market in the world.

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We urge the Commission to disapprove this FINRA Filing.

Please feel free to call the undersigned with any questions regarding these comments.

Respectfully,

/s/ Stephen John Berger

Managing Director

Global Head of Government & Regulatory Policy