CITADEL | Securities

August 3, 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 further comments to the Securities and Exchange Commission (the "Commission") on the proposal by FINRA to add the IntelligentCross ATS to the Alternative Display Facility and classify their displayed quotations as "protected quotations" under Regulation NMS (the "FINRA Filing").[1]

More than two months after firms submitted comments in response to the Commission's order instituting proceedings to determine whether to approve or disapprove the FINRA Filing,[2] IntelligentCross elected to provide new information on July 14th, a mere 41 days before the Commission must make a final decision.[3] Combined with the nearly universal opposition to this filing, the IntelligentCross July Response confirms that the FINRA Filing should be rejected.

1. FINRA Has Not Demonstrated That Displayed Quotations on IntelligentCross Are "Protected Quotations"

A central question raised by this filing is whether displayed quotations on IntelligentCross qualify as "protected quotations" under Commission regulations given that the matching process includes an intentional delay before orders are executed against resting quotations.[4] The answer to that question is no.[5] But the Commission need not reach that conclusion, as FINRA has failed to "demonstrate that [the] proposed rule change is consistent with the Exchange Act."[6] Under Commission rules, FINRA must, among other things, provide "a legal analysis of [the proposal's]

[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"). The FINRA Filing covers the "ASPEN Fee/Fee" order book. IntelligentCross has two other limit order books which are not covered by this filing.

[2] *See* https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032.htm.

[3] *See* Letter from Imperative Execution (July 14, 2023), available at: https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-224439-469862.pdf ("IntelligentCross July Response").

[4] Under the rules that govern our national market system, "protected quotations" are quotations that are "immediately and automatically" executable. *See* 17 C.F.R. § 242.600(b)(71), (b)(70), (b)(6).

[5] *See* Letter from Citadel Securities at 2-7 (May 4, 2023), available at: https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-189919-374262.pdf ("Citadel Securities May 2023 Letter").

[6] 17 C.F.R. § 201.700(b)(3).

consistency with applicable requirements" that is "sufficiently detailed and specific to support an affirmative Commission finding" that the proposal is "consistent with the Exchange Act."[7] "A mere assertion that the proposed rule change is consistent with [the Exchange Act] … is not sufficient," as it does not allow "the public to provide meaningful comment on the proposed rule change" or the Commission to determine for itself "whether the proposed rule change is consistent with the requirements of the Exchange Act."[8] FINRA's proposal falters at this preliminary step. FINRA has not performed[9] the necessary analysis to conclude that the IntelligentCross displayed quotations are "protected quotations" – i.e. that they are "immediately and automatically" executable, as required by Commission regulations.

First, and even putting aside the proposal's contradiction of the plain text of Regulation NMS,[10] FINRA must determine that the IntelligentCross intentional delay is *de minimis* (i.e. that the delay is so short as to not frustrate the purposes of Rule 611 (*the Order Protection Rule*) by impairing fair and efficient access to an exchange's quotations) in order to assert that IntelligentCross displayed quotations are "protected quotations."[11] FINRA has not even attempted to do this. It is undisputed that the Commission has not established a bright-line test to determine whether a particular intentional delay is *de minimis* (and, in fact, explicitly rejected setting one).[12] Even the latest letter from IntelligentCross acknowledges that "the Commission did not establish a bright line de minimis threshold."[13] Instead, the Commission requires a facts-and-circumstances analysis to determine whether the intentional delay frustrates the purposes of Rule 611 by impairing fair and efficient access to displayed quotations.

However, the FINRA Filing wrongly asserts that the IntelligentCross intentional delay is *de minimis* simply because it is less than one millisecond in length.[14] That "mere assertion" is "not sufficient" under Commission rules,[15] and is plainly inaccurate. Since FINRA's explanation is not a legally valid interpretation of the *de minimis* standard, the FINRA Filing does not demonstrate that the IntelligentCross intentional delay is consistent with the Exchange Act and the rules and regulations thereunder. The Commission should reject the proposal for this reason alone and

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[7] *Id.*

[8] *Id.*

[9] *See* Citadel Securities May 2023 Letter at 2-3.

[10] *See id.*

[11] 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"). For purposes of this letter, we leave aside that this reinterpretation of the term "immediate" is flatly inconsistent with the plain text of Regulation NMS (as detailed in our prior letters).

[12] 2016 Interpretation at 40792. The Commission stated it "is **not adopting** the proposed guidance under this interpretation that delays of less than one millisecond are de minimis. (emphasis added)."

[13] IntelligentCross July Response at 4.

[14] FINRA Filing at 79403.

[15] 17 C.F.R. § 201.700(b)(3).

remand the matter to FINRA to, at the very least, conduct the required facts-and-circumstances analysis.

Notably, under Commission rules, along with basic principles of administrative law, the Commission cannot fix the deficiency in FINRA's filing on its own in an order approving the proposed rule change. As Commission rules explain, *FINRA* must provide all necessary information and analysis in its own proposal, so that the "public [can] provide meaningful comment" on FINRA's analysis.[16] FINRA's failure to provide that analysis, and expose it to public comment, is a fatal deficiency in the current proposal.

Second, FINRA has not adequately analyzed the "price-sliding" employed by IntelligentCross in order to avoid locking its own market.[17] While exchanges with actual "protected quotations" implement controls to avoid locking prices on *other markets*, the intentional delay on IntelligentCross can cause the venue to lock its *own market* by actively preventing a match between a willing buyer and seller. That makes no sense and is unheard-of elsewhere in the securities markets, further indication that the quotations on IntelligentCross are unlike "protected quotations" on other venues. The IntelligentCross July Response confirms that the proposed "price-sliding" mechanism to avoid locking its own market can result in the displayed bid and offer on IntelligentCross (which could also be the market-wide NBBO if this Proposal were approved) being completely inaccessible to incoming orders since the bid and offer will end-up matched together at the end of the next match event.[18] This means that, if market participants are compelled to route orders to the venue, they may be forced to attempt to access a displayed quote that only IntelligentCross knows is impossible to access. That is clearly inconsistent with Regulation NMS requirements for "protected quotations," which requires the quotations to be "immediately and automatically" executable, not completely inaccessible.

IntelligentCross's attempt to minimize the significance of this inconsistency with Regulation NMS is unavailing. IntelligentCross argues that this scenario is "extremely unlikely" based on *current* trading activity on the venue,[19] but the proposal, if adopted, would significantly change trading activity on the venue, as market participants would be forced to route orders to IntelligentCross. In this scenario, we would expect price sliding and inaccessible quotes to occur far more often. Fundamentally, the "price-sliding" proposed by IntelligentCross can result in (i)

[16] 17 C.F.R. § 201.700(b)(3).

[17] For example, the NBBO is $9.95 by $10.00, and IntelligentCross is at the NBBO posting an offer at $10.00. IntelligentCross then receives a Displayed Day limit buy order 100 @ $10.00. This order would trigger a match event. During the up to 900 microseconds of the match event, IntelligentCross would display the buy order at $9.99 on the SIP (the order is "price slid" and displayed one minimum price variation below the best offer in order to not create a locked market), creating an NBBO of $9.99 by $10.00.

[18] *See* IntelligentCross July Response at 7 ("The example the commenter illustrates, while possible to occur…").

[19] *Id.*

significant information leakage[20] and (ii) displayed quotes that are impossible to interact with, both of which are inconsistent with Commission regulations. Critically, these issues have not been considered at all by FINRA in the filing.

2. FINRA Has Not Demonstrated That IntelligentCross's Intentional Delay Is Not Unfairly Discriminatory

In our prior letter, we noted that, by giving liquidity providers the ability to cancel displayed quotations on an order-by-order basis, the IntelligentCross intentional delay operates as an asymmetric delay that favors liquidity providers, unfairly discriminating against others in violation of the Exchange Act. FINRA has not shown otherwise, even if one were to (improperly) consider IntelligentCross's belated attempt to bolster FINRA's missing analysis.

IntelligentCross has attempted to argue that a liquidity taker could also elect to cancel its order during the intentional delay, and thus that the delay is symmetric in nature. However, this assertion is simply inaccurate. Consider a liquidity taker sending an intermarket sweep order ("ISO") to IntelligentCross. If IntelligentCross believes an ISO order can be immediately cancelled by the sender before execution, it would appear to be a novel approach to complying with the intermarket sweep order exception under Rule 611. The IntelligentCross July Response confirms that IntelligentCross does not in fact believe that an ISO order can be instantaneously cancelled by the liquidity taker before execution.[21] Therefore, the intentional delay is clearly asymmetric in this scenario, as *only* the liquidity provider can cancel its quotation. Once again, this issue is not considered at all by FINRA in the filing, and no analysis has been conducted to determine whether the IntelligentCross intentional delay is consistent with (i) Exchange Act Section 15A(b)(6), which prohibits FINRA rules from permitting unfair discrimination, and (ii) Commission Rule 610(b)(2), which prohibits an ADF participant from imposing unfairly discriminatory terms that inhibit efficient access to displayed quotations.

3. IntelligentCross Displayed Quotations Are Not Immediately And Automatically Executable

In any event, in our prior letters, we explained that the IntelligentCross intentional delay is contrary to Regulation NMS and the Commission's 2016 interpretation.[22] As we explained, the delay frustrates the purposes of Rule 611 by enabling a liquidity provider to cancel its displayed quote after an incoming order reaches the IntelligentCross matching engine – the exact scenario

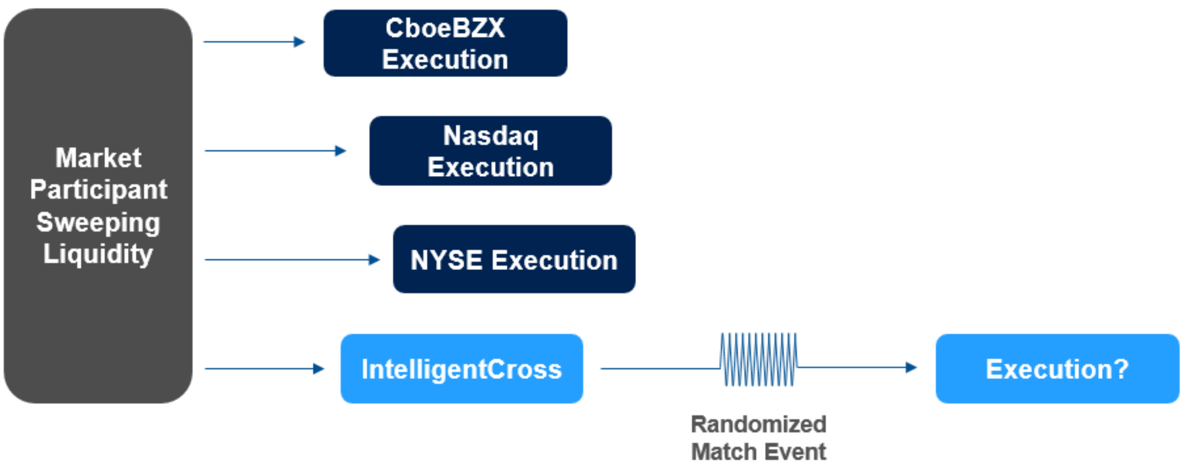
[20] In the example above (*supra note 17*), given that the IntelligentCross quote suddenly jumps from 9.95 by 10.00 to 9.99 by 10.00, this almost certainly means that the 9.99 order is in a delayed state waiting to be matched. Anyone can see this, and if you are quoting at 10.00 on IntelligentCross, you will be aware that you are about to be matched (and can decide to cancel your quote accordingly). Thus, under certain circumstances, parties will be able to "see" orders that are in a pre-match state and can respond accordingly.

[21] *See* IntelligentCross July Response at FN 19 ("one commenter states that 'IntelligentCross appears to be advancing a novel approach to complying with the intermarket sweep order exception under Rule 611 in suggesting that these orders could be immediately cancelled by the sender before execution.' See Citadel Letter II. That is not the case.").

[22] Citadel Securities May 2023 Letter at 2-7.

Rule 611 was designed to avoid. This is particularly relevant when a market participant is attempting to execute a larger order, such as an ISO, across multiple market centers. We provided the following example (with a router located at the NY4 data center in Secaucus):

> *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).*



IntelligentCross has questioned whether this is likely, but the data make clear that it is. Set forth below are the typical routing latencies using fiber infrastructure between datacenters.

Time *(microseconds)*	Event
0	Liquidity seeker sends an order from the NY4 data center (Secaucus) to CboeBZX, Nasdaq, NYSE, and IntelligentCross
90	CboeBZX execution message disseminated on the public feed and received at the NY4 data center (the CBOE-to-market data time is 90 microseconds)
175	Order arrives at Nasdaq (the one-way fiber time between NY4 and Carteret is 175 microseconds)
200	Nasdaq execution message disseminated on the public feed (the Nasdaq-to-market data time is 25 microseconds)
210	Order arrives at NYSE (the one-way fiber time between NY4 and Mahwah is 210 microseconds)
260	NYSE execution message disseminated on the public feed (the NYSE-to-market data time is 50 microseconds)
375	Nasdaq execution message received at the NY4 data center (the one-way fiber time between NY4 and Carteret is 175 microseconds)
470	NYSE execution message received at the NY4 data center (the one-way fiber time between NY4 and Mahwah is 210 microseconds)
800-900	**IntelligentCross match occurs (vast majority of IOC executions in the ASPEN Fee/Fee order book have an intentional delay of more than 800 microseconds)**

This example demonstrates that, based on fiber infrastructure between datacenters, as long as the intentional delay is at least 470 microseconds, a liquidity provider on IntelligentCross has ample time to observe the trades executed on other U.S. equities exchanges before determining whether to cancel its resting order. Interestingly, an analysis of our trading activity on IntelligentCross 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.

This option to cancel has significant commercial value for liquidity providers on IntelligentCross, imposes an unwarranted tax on liquidity takers (as incoming orders are likely to be filled only when commercially beneficial for the liquidity provider), and hurts market competition across venues (as liquidity providers on IntelligentCross can free-ride on the pricing heuristics and risk-taking capabilities of others by price-matching, with a free option to cancel later). Moreover, according to data provided by IntelligentCross, liquidity providers are already frequently exercising this option to cancel, a rate which should only be expected to increase if market participants are compelled by the Commission to route orders to the venue.[23] And the randomized, unpredictable nature of the intentional delay makes it practically impossible for market participants to stagger order routing such that orders are executed at IntelligentCross and

[23] In addition, as noted by another commenter, "[t]he potential value of this option [to cancel a displayed quotation] lies in being able to determine whether or not to cancel, not just how often the option is exercised." https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-20164234-334053.pdf at 6.

other venues at precisely the same time.[24] All of these factors support the conclusion that the IntelligentCross displayed quotations are the type of "maybe" quotations that could simply disappear, and which the Commission excluded from the definition of a "protected quotation" in Regulation NMS. These quotations, with an intentional delay, are not "immediately and automatically" executable, and the delay is in no way *de minimis*.

IntelligentCross continues to have no real response, apart from asserting that this scenario is "a hypothetical example that may or may not take place" even though this is precisely how market participants are required to use ISOs under Commission regulations.[25] Instead, it attempts to divert attention by making arguments that have no bearing on whether the intentional delay is *de minimis* or whether the quotations are automatically and immediately executable.

First, IntelligentCross argues that its displayed quotations should be classified as "protected quotations" because market participants are supposedly ignoring better prices available on its venue.[26] This claim is at odds with its separate statements that "IntelligentCross is already widely used by most major US broker-dealers and electronic trading firms" and "our average daily market share has continued to grow."[27] IntelligentCross also fails to consider that, when taking into account the impact of the intentional delay mechanism (including on fill rates), the execution experience on its venue may be far worse than advertised, which may explain why more orders are not routed to the venue. Furthermore, by not taking order size into account, its data is fatally flawed and cannot show that market participants are executing at *all-in prices* worse than those available on its venue. Even more fundamentally, unsubstantiated claims regarding trade-throughs are completely irrelevant to the definition of a "protected quotation" under Commission regulations.

Second, even though the intentional delay already prevents (according to IntelligentCross's own data) nearly 9% of transactions from successfully executing, IntelligentCross argues that such non-match events "are not 'material'" and that other factors, such as "software, telecommunication resources, geography, and the number of ports" may affect execution outcomes more than the intentional delay.[28] Again, identifying other aspects of U.S. equities market structure that may be

[24] *See also* comments submitted in response to the Nasdaq filing on "Dynamic M-ELO Holding Periods," available at: https://www.sec.gov/comments/sr-nasdaq-2022-079/srnasdaq2022079.htm. In addition to the books and records concerns raised in that file, there is also a more general concern about the potential for IntelligentCross, as an ATS, to make subsequent material changes to its methodologies regarding the matching of displayed quotations without the ability of the Commission to consider such changes through a notice-and-comment process.

[25] https://www.sec.gov/comments/sr-finra-2022-032/srfinra2022032-20157506-325781.pdf at 8. We note that many of the statistics cited by IntelligentCross, including its daily market share, are not specific to the ASPEN Fee/Fee order book that is the subject of this filing.

[26] IntelligentCross also suggests firms may be acting in a manner that is inconsistent with best execution requirements by ignoring better prices available on its venue, but fails to consider that these purported "trade-throughs" may come from proprietary trading activities. IntelligentCross July Response at 2-3.

[27] *Id.*

[28] IntelligentCross July Response at 4 and 6.

relevant to how market participants transact has no bearing on whether IntelligentCross displayed quotations meet the definition of a "protected quotation" under Commission regulations given the presence of an intentional delay. As noted in our prior letters, geographic and technological latencies are applicable to all market participants and do not provide liquidity providers with a clear structural advantage – namely, the option to cancel a displayed quote after an incoming order reaches the IntelligentCross matching engine. That is why the Commission has recognized that intentional delays – as opposed to generally applicable geographic delays – raise unique regulatory questions and must be carefully scrutinized for consistency with the Exchange Act and Commission regulations. Rule 611 is only intended to protect "quotations that are truly firm and fully accessible" and the IntelligentCross data shows that its displayed quotations are "maybe" quotations that do not provide market participants with execution certainty.[29]

Third, the statistics cited by IntelligentCross are based on the current *status quo*, where market participants are not required to route to IntelligentCross. Neither FINRA nor the Commission can conclude this proposal is consistent with the Exchange Act without determining the impact that granting IntelligentCross "protected quotation" status would have on these figures, including the non-match event rate resulting from the intentional delay.

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FINRA has not met its burden, and we respectfully 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

[29] Regulation NMS at 37518.