CITADEL | Securities

March 31, 2023

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

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

Dear Ms. Countryman:

The Securities and Exchange Commission's proposals to abruptly and unilaterally redesign the U.S. equity markets are a dangerous, baseless experiment that (1) exceed the Commission's legal authority, (2) would harm investors and damage the resiliency and efficiency of our markets; and (3) otherwise violate the Administrative Procedure Act several times over.

The U.S. equity markets are the fairest, most transparent, resilient, and competitive markets in the world. Today, sixteen stock exchanges and numerous alternative trading systems and individual market makers vie to provide the best execution experience to market participants, including both retail and institutional investors. Over the past nearly two decades, vibrant competition and innovation, fostered by Regulation NMS, has greatly enhanced market quality and lowered transaction costs across the board. This increased market efficiency has reduced the cost of capital and optimized the allocation of capital, in turn better financing the groundbreaking companies and technology that have been vital ingredients to our global economic strength. The Commission should not jeopardize these substantial gains through reckless experimentation. The complete overhaul of the U.S. equity markets that the Commission proposes, without evidence of any real benefits, is the definition of arbitrary and capricious action.

In a series of ill-conceived, half-baked proposals, the Commission would drastically slash quoting increments for many stocks and would set—*for the first time ever in the Commission's history*[1]—the minimum pricing increments at which any investor could trade.[2] Further, the Commission would require virtually every retail equity order to be routed to a new exchange auction mechanism of the Commission's own invention.[3] It would also override the best-

[1] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. 128, 143 (Jan. 3, 2023) (current SEC rules do "not … prohibit a sub-penny trade"); *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. 80,266, 80,339 (Dec. 29, 2022) (pricing increments do not currently apply "to trading").

[2] *See Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. 80,266.

[3] *See Order Competition Rule*, 88 Fed. Reg. 128.

execution standard that has guided broker-dealers for many decades.[4] These proposals would not better our markets, but rather risk creating a market structure that is far more fragile, opaque and inefficient. Retail and institutional investors alike will suffer from poorer market quality and increased trading costs, while American businesses will face a higher cost of capital.

These proposals will benefit no one, certainly not retail investors. Under the current market structure, retail broker-dealers often route client orders to wholesale broker-dealers, such as Citadel Securities, that provide fast, reliable executions—not only filling retail investor orders at *better* prices than those quoted on-exchange, but also executing at those better prices for *more size* than is publicly displayed. In 2022 alone, based on data collected under the Commission's own Rule 605, wholesale broker-dealers delivered ***more than $3 billion in savings*** to retail investors, and filled more than 90% of orders at prices that were better than those available on-exchange.[5] Correcting for Commission-acknowledged inaccuracies in the Rule 605 data would reveal a total 2022 wholesale broker-dealer price improvement of ***$15 billion*** according to academic research.[6] The Commission's proposals would greatly decrease or eliminate these savings, and likely result in higher costs and fees to investors.

The proposals will similarly adversely impact institutional investors, who will face worse pricing and liquidity. They will suffer in particular from the decrease in displayed liquidity associated with extremely narrow tick sizes. Larger orders will be more complex to execute, as filling the entire order will require accessing multiple price levels, which can increase price impact. The increased likelihood that displayed quotes can be jumped by economically insignificant amounts will likewise impair institutional investors' use of limit orders and add complexity for institutional order routing algorithms. The need to access liquidity beyond the NBBO more often to fulfill liquidity needs will necessitate an increased use of ISOs, forcing market participants to bear the costly complexity and regulatory burden associated with their use. Finally, the proposed retail auction mechanism, which is ill-suited to institutional investor participation, will actually reduce opportunities for institutional investors to interact with retail order flow compared to today's market.

Retail broker-dealers will suffer as well. The cumulative impact of the proposals will likely leave retail broker-dealers responsible for building and maintaining connections to nearly fifty market centers, developing bespoke and costly order routing systems, building the required market access controls, and bearing the associated operational risk and complexity. Retail broker-dealers would also have to cover the costs associated with exchange trading fees, venue memberships, and market data subscriptions. Barriers to entry for new retail broker-dealers will significantly

[4] *See Regulation Best Execution*, 88 Fed. Reg. 5440 (Jan. 27, 2023).

[5] *See* Robert Battalio & Robert Jennings, Why Do Brokers Who Do Not Charge Payment for Order Flow Route Marketable Orders to Wholesalers? at abstract (Dec. 14, 2022), https://ssrn.com/abstract=4304124.

[6] *See id.* (finding that real price improvement is about five times more than would be estimated with current Rule 605 data); *see also* Charles Schwab, *U.S. Equity Market Structure: Order Routing Practices, Considerations, and Opportunities* at 13, https://content.schwab.com/web/retail/public/about-schwab/Schwab-2022-order-routing-whitepaper.pdf ("Using publicly available exchange data, we estimate that routing to wholesalers saved Schwab's clients [alone] at least $3.4B in 2021, vs. what their outcomes would have been from utilizing exchanges.").

increase, which will cause competition and innovation within the retail broker-dealer community to suffer.

As for wholesale broker-dealers, the Commission's proposals can be read in only one way—a targeted effort to, if not eliminate their business model, shift the competitive playing field decisively in favor of exchanges—all the while ignoring the collateral damage to retail investor execution quality.

The Commission's proposals are thus unwise, unwarranted, and unlawful. They will damage the quality and resiliency of our nation's capital markets, raise the cost of capital, and impair companies' ability to raise money and finance new investments, harming capital formation and economic innovation. The Commission should not go down this risky route, especially when there is no apparent reason to do so.

The spirited competition among wholesaler broker-dealers and among retail brokers-dealers has been transformational for the retail investor experience. A significant portion of trading in America's equity markets is now driven by retail investors who no longer pay commissions and who enjoy extraordinarily low transaction costs. Based on little more than an ill-informed visceral dislike for wholesale broker-dealers, the Commission risks wiping out the tremendous gains enjoyed by retail investors under today's competitive system.

We have filed separate comments detailing the significant deficiencies in each of the Commission's proposals and incorporate those comments by reference here.[7] We submit this letter to address the overarching, cross-cutting flaws in the Commission's broader approach. In particular, and as discussed below, the Commission does not have the statutory or constitutional authority to unilaterally rework the configuration of the U.S. equity markets merely to take away wholesale broker-dealers' market share—a market share they have earned based on the compelling value proposition they have competed to create for retail investors. This is a lose-lose situation, and would be no different than the government, in response to the success of the big three auto manufacturers in the mid-20th century, having decided to force everyone to use horse and buggies. And even if the Commission did have authority, the Commission has not—and cannot—justify the radical changes it proposes. The Commission *admits* that it "lacks" the data "to predict" the impact of its changes[8] and *acknowledges* that it has no idea what the "net effect for retail price improvement" would be, stating it "could be positive, negative, or neutral."[9] In fact, the economics run entirely against the proposals. If adopted, the proposed rules would cost retail investors

[7] In addition to commenting on the Order Competition Rule, Regulation Best Execution, and Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, Citadel Securities suggested technical revisions to the proposal titled *Disclosure of Order Execution Information*, 88 Fed. Reg. 3786 (Jan. 20, 2023).

[8] *Regulation Best Execution*, 88 Fed. Reg. at 5523 ("[T]he Commission lacks detailed data on broker-dealers' current order handling practices and documentation practices that would allow it to predict the extent of changes as a result of this proposal."); *see also Order Competition Rule*, 88 Fed. Reg. at 203 ("The Commission acknowledges considerable uncertainty in the costs and benefits of this rule because the Commission cannot predict how different market participants would adjust their practices in response to this rule.");

[9] *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,326.

billions of dollars in price savings that they currently enjoy, likely eliminate commission-free trading, slow execution times by up to 83x,[10] and massively fragment displayed liquidity, among a multitude of other drawbacks. The Commission should not—and, under the Administrative Procedure Act, cannot—go down this path.

The Commission should instead look to the consensus position of the NYSE Group, Inc., Charles Schwab & Co., and Citadel Securities—which incorporates some of the Commission's suggestions—as an obvious, reasonable, more efficient path forward. Numerous other market participants, representing significant, diverse sectors of the overall U.S. equity markets—including Cboe Global Markets, State Street Global Advisers, T. Rowe Price, UBS Securities LLC, and Virtu Financial, LLC—have offered similar proposals.[11] All recognize that the Commission in its current proposals has gone far astray.

I. The Proposed Rules exceed the Commission's legal authority.

The Commission's plan to redesign the configuration of the equity markets—and to force almost every retail-equity order into a novel, Commission-contrived auction—fails at the outset because it exceeds the Commission's statutory authority and raises significant constitutional issues.[12]

A. The Commission does not have statutory authorization to unilaterally dictate the configuration of the retail-equity markets.

The Commission itself has long recognized that "Congress did *not* intend that the Commission dictate the ultimate configuration of the national market system or, through regulatory fiat, force all trading into a particular mold."[13] Yet that is *exactly* what the Commission proposes to do here. It does not have that authority.

Congress gave the Commission a supporting role with respect to trading markets. In the 1970s, Congress (and the Commission) had grown concerned that the nation's securities markets were too "fragmented."[14] Securities could be traded on a multitude of venues—from the two predominant stock exchanges (the New York and American Stock Exchanges), to eleven regional exchanges, to the so-called third market (*i.e.*, over-the-counter).[15] The problem with this fragmentation was that investors could not be sure that they were getting the "best prices"; the

[10] The Commission acknowledges that the median execution time for internalized retail-customer orders is 3.6 milliseconds. *Order Competition Rule*, 88 Fed. Reg. at 196. By arbitrarily preventing wholesalers from executing customer orders as quickly as possible, and by forcing those orders to first be routed to an auction potentially lasting as long as 300 milliseconds, the Commission would cause execution times to slow by up to 83 times.

[11] *See* Letter from Cboe Global Markets, State Street Global Advisers, T. Rowe Price, UBS Securities LLC, and Virtu Financial, LLC, File Numbers S7-29-22, S7-30-22, S7-31-22, S7-32-22 (Mar. 24, 2023).

[12] *See N.Y. Stock Exch. LLC v. SEC*, 962 F.3d 541, 553 (D.C. Cir. 2020) ("An agency literally has no power to act unless and until Congress confers power upon it." (cleaned up)).

[13] *Development of a National Market System*, 44 Fed. Reg. 20,360, 20,360 (Apr. 4, 1979) (emphasis added).

[14] H.R. Rep. No. 94-123, at 50 (1975).

[15] *See id.* at 49-50.

"most willing buyer" could be in one venue, and the "most willing sellor" in another.[16] The Commission responded to this concern in 1972 by proposing the establishment of a "system of communications" to "tie[] together" the various trading venues.[17] And, in 1975, Congress acted on the Commission's proposal. In the Securities Acts Amendments of 1975,[18] Congress instructed the Commission to "facilitate the establishment of a national market system"[19] by "link[ing] together" the various venues.[20]

The Commission's authority was focused on inter-venue communication. As the 1975 Amendments provided, the Commission could regulate the "distribution"[21] and "transmit[al]"[22] of "quotations,"[23] "orders,"[24] and certain trade-related "information."[25] Thus, although the Commission could create a "composite quotation system" or a "consolidated transactional reporting system,"[26] for example, other matters, such as the "development"[27] and "evol[ution]"[28] of the trading venues themselves, remained the province of "private interests" and the "vigor of competition" between them.[29]

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[16] *Id.* at 50.

[17] SEC, *Future Structure of the Securities Markets* 8 (1972).

[18] Pub. L. No. 94-29, 89 Stat. 97.

[19] 15 U.S.C. § 78k-1(a)(2).

[20] *Regulation NMS*, 69 Fed. Reg. 11,126, 11,130 (Mar. 9, 2004).

[21] 15 U.S.C. § 78k-1(c)(1)(A), (B), (C).

[22] *Id.* § 78k-1(c)(1)(E).

[23] *Id.* § 78k-1(c)(1)(A), (B), (C), (D).

[24] *Id.* § 78k-1(c)(1)(D).

[25] *Id.* § 78k-1(c)(1)(A), (B), (C), (D); *id.* § 78k-1(c)(2).

[26] H.R. Rep. No. 94-229, at 92 (1975).

[27] S. Rep. No. 94-75, at 12 (1975).

[28] H.R. Rep. No. 94-229, at 92.

[29] S. Rep. No. 94-75, at 12; *see also Regulation NMS*, 69 Fed. Reg. at 11,130 ("Although Congress set out broad principles to govern the development of an NMS, it did not dictate a specific form that it should take."); S. Rep. No. 94-75, at 12 ("This is not to suggest that under S. 249 the SEC would have either the responsibility or the power to operate as an 'economic czar' for the development of a national market system. Quite the contrary, for a fundamental premise of the bill is that the initiative for the development of the facilities of a national market system must come from private interests and will depend upon the vigor of competition within the securities industry as broadly defined."); H.R. Rep. No. 94-229, at 92 ("It is the intent of the conferees that the national market system evolve through the interplay of competitive forces as unnecessary regulatory restrictions are removed. The conferees expect, however, in those situations where competition may not be sufficient, such as the creation of a composite quotation system or a consolidated transactional reporting system, the Commission will use the powers granted to it in this bill to act promptly and effectively to insure that the essential mechanisms of an integrated secondary trading system are put into place as rapidly as possible."); *id.* ("The Senate bill did not direct the Commission to create the national market system. Instead, it directed the Commission to facilitate the establishment of the system in accordance with enumerated Congressional findings and objectives.").

The Commission's proposals would turn this nearly half-century-long division of authority on its head. Instead of "assuring that all of the[] markets are linked together … in a unified system,"[30] while letting the markets evolve and compete on their own, the Commission would unilaterally supplant the structure of the retail-equity markets. It would eliminate the robust competition between trading venues envisioned by the 1975 Amendments, dictate the prices at which securities could trade, and force virtually every retail order into never-before-seen, Commission-contrived auctions, among other changes. This would constitute a "fundamental revision" to the statutory scheme.[31]

Under well-established Supreme Court precedent, one would expect to see "clear congressional authorization" for the Commission to regulate in this manner.[32] All the Commission can point to, however, is "a variety of … provisions"[33] of the Securities Acts Amendments of 1975[34] (Section 11A of the Exchange Act[35]). But if Congress had *really* intended to delegate such "sweeping and consequential authority" to the Commission—the power to unilaterally rework the entire structure of the U.S. retail-equity markets—Congress would not have done so "in so cryptic a fashion."[36] When Congress intends for an agency "to regulate a significant portion of the American economy," Congress says so "clear[ly]."[37] It does not chop up and sprinkle that authority across nearly a dozen ancillary provisions buried throughout a statute,[38] waiting for an enterprising agency to find and piece it together decades later.[39]

A closer look at the statutory text further undermines the Commission's position. Take, for example, the Commission's claim that, absent any Commission-defined exceptions, it can prohibit wholesale broker-dealers from internally executing an investor's order unless the wholesale broker-dealer first routes the order to a Commission-contrived, on-exchange auction. The Exchange Act explicitly *bars* the Commission from "prohibit[ing] brokers and dealers from effecting transactions … otherwise than on a national securities exchange," unless and until the Commission makes specific findings in a formal procedure that the Commission here has not even

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[30] *Regulation NMS*, 70 Fed. Reg. 37,496, 37,498 (June 29, 2005).

[31] *West Virginia v. EPA*, 142 S. Ct. 2587, 2596 (2022).

[32] *Id.* at 2614.

[33] *Order Competition Rule*, 88 Fed. Reg. at 136.

[34] Pub. L. No. 94-29, 89 Stat. 97.

[35] 15 U.S.C. § 78k-1.

[36] *West Virginia*, 142 S. Ct. at 2608.

[37] *Util. Air Regulatory Grp. v. EPA*, 573 U.S. 302, 324 (2014).

[38] *Cf. Whitman v. Am. Trucking Ass'ns, Inc.*, 531 U.S. 457, 468 (2001) ("Congress, we have held, does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not, one might say, hide elephants in mouseholes.")

[39] *See Util. Air Regulatory Grp.*, 573 U.S. at 324 ("When an agency claims to discover in a long-extant statute an unheralded power to regulate 'a significant portion of the American economy' … we typically greet its announcement with a measure of skepticism."); *Chamber of Commerce of U.S. v. U.S. Dep't of Labor*, 885 F.3d 360, 380 (5th Cir. 2018) ("[T]hat it took DOL forty years to 'discover' its novel interpretation further highlights the Rule's unreasonableness.").

attempted to invoke.[40] The Commission does not mention this statutory bar anywhere in its 118-page auction proposal. Instead, the Commission claims to have found authority to end-run the statutory bar in Sections 11A(c)(1)(E), 11A(c)(1)(F), and 15(c)(5) of the Exchange Act.[41] But those sections instead *confirm* the limited nature of the Commission's authority. Section 11A(c)(1)(F) authorizes the Commission to "assure equal regulation of all markets,"[42] not to force all trading into a particular Commission-contrived market. And Sections 11A(c)(1)(E) and 15(c)(5) concern the linkages between markets; they authorize the Commission to assure that "orders" are "transmit[ted]" and "direct[ed]" "in a manner consistent with the establishment and operation of a national market system,"[43] and to "remove impediments" to the orderly operation of that market system.[44] Nowhere do those provisions authorize the Commission to order the creation of its own auction mechanism, and then force all trading there.[45]

The Commission's proposal to set a minimum pricing increment at which securities may trade, both on- and off-exchange, is equally devoid of statutory authority. As noted, Congress authorized the Commission to adopt "rules and regulations" to, for example, "assure" that "orders" are "transmit[ted]" in a way that is "consistent with the establishment and operation of a national market system."[46] This provision can reasonably be read to authorize the Commission to set *quoting* increments—the prices at which "orders" may be "transmit[ted]" between trading centers—increments the Commission has already set.[47] There is no similar authorization for *trading* increments.[48] Price regulation is a significant and often controversial regulatory authority; Congress knows how to confer it when it wishes to—as, for example, in Section 4 of the Natural

[40] To bar off-exchange transactions, the Commission would need to make a number of findings "on the record after notice and opportunity for hearing." 15 U.S.C. § 78k-1(c)(3). The Commission cannot meet this standard for two reasons. *First*, the phrase "on the record after notice and opportunity for hearing" is a term of art that requires *formal* rulemaking under 5 U.S.C. § 556. *See* 5 U.S.C. § 553(c); *United States v. Fla. E. Coast Ry. Co.*, 410 U.S. 224, 241 (1973). In a formal rulemaking, the Commission (or a hearing officer) must preside over a "hearing" and allow interested parties to submit "oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts." 5 U.S.C. § 556(d). The Commission has not called such a hearing. *Second*, even if the Commission *were* to call such a hearing, the Commission could not show: (1) that off-exchange transactions affect "the fairness or orderliness of the markets for such securities … in a manner contrary to the public interest or the protection of investors;" (2) that no rule of an exchange "unreasonably impairs the ability of any dealer" to transact in securities for his own account; *and* (3) that "the maintenance or restoration of fair and orderly markets in securities may not be assured through other lawful means." 15 U.S.C. § 78k-1(c)(3)(i)-(iii); *see also* Comments of Citadel Securities on Order Competition Rule 27-28, File No. S7-31-22 (Mar. 31, 2023).

[41] *Order Competition Rule*, 88 Fed. Reg. at 137.

[42] 15 U.S.C. § 78k-1(c)(1)(F).

[43] *Id.* § 78k-1(c)(1)(E).

[44] *Id.* § 78*o*(c)(5).

[45] *See* SEC, *Future Structure of the Securities Markets*, *supra* n.17, at 8 ("To mandate the formation of a central market system is not to choose between an auction market and a dealer market.").

[46] 15 U.S.C. § 78k-1(c)(1)(E) (emphasis added).

[47] *See* 17 C.F.R. § 242.612(a).

[48] *See* Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders 19, File No. S7-30-22 (Mar. 31, 2023).

Gas Act[49]—but has not done so here. In fact, in 2012 Congress *did* authorize the Commission to set minimum "quot[ing] *and trad[ing]*" increments for a specific, narrow set of companies: "emerging growth companies."[50] This delegation of authority would have been superfluous—and the express limitation to emerging growth companies entirely ineffective—if the Commission *already* had the authority to set minimum trading increments for *all* companies. The Commission, again, points to its authority to assure "equal regulation of all markets,"[51] but all markets are already equally regulated in terms of trading increments: *there are no minimum trading increments*.[52]

Finally, the Commission's proposal to adopt its own standard of best execution also lacks statutory authority.[53] The Commission cites various policy objectives from the Securities Acts Amendments of 1975,[54] but it is blackletter law that an agency action cannot "rest merely on the 'policy objectives of the Act.'"[55] The Commission must find a specific grant of rulemaking authority to justify its action, but, here, there is none. Congress, to be sure, authorized the self-regulatory organizations to set a standard of best execution,[56] and the Commission can supervise *those* standards[57]—an arrangement that no one objects to. But Congress never authorized the Commission to unilaterally dictate a standard of best execution in its own name. Tellingly, Congress had considered authorizing the Commission to promulgate best-execution rules in 1973,[58] but rejected that idea.[59] The standard of best execution has thus *always* been set, not by the Commission, but by the self-regulatory organizations[60]—a division of authority the

[49] 15 U.S.C. § 717c(a); *see also* 16 U.S.C. § 824d; 7 U.S.C. §§ 206-07, 212; 46 U.S.C § 9305.

[50] 15 U.S.C. § 78k-1(c)(6)(B) (emphasis added).

[51] *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,278 (quoting 15 U.S.C. § 78k-1(c)(1)(F)).

[52] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 143 (current SEC rules do "not … prohibit a sub-penny trade"); *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,339 (pricing increments do not currently apply "to trading").

[53] *See* Comments of Citadel Securities on Regulation Best Execution 22-23, File No. S7-32-22 (Mar. 31, 2023).

[54] *See Regulation Best Execution*, 88 Fed. Reg. at 5442 (citing 15 U.S.C. § 78k-1(a)).

[55] *Georgia v. President of U.S.*, 46 F.4th 1283, 1298 (11th Cir. 2022); *accord Comcast Corp. v. FCC*, 600 F.3d 642, 654 (D.C. Cir. 2010).

[56] *See* 15 U.S.C. § 78*o*-3(b)(6) ("The rules of the association are designed to … promote just and equitable principles of trade ….").

[57] *See id.* (requiring Commission review of SRO rules); *id.* § 78s(c) (authorizing the Commission to amend SRO rules); *see also, e.g.*, *Self-Regulatory Organizations*, 76 Fed. Reg. 77,042, 77,043 (Dec. 9, 2011) (finding that FINRA's best-execution rule "promote[s] just and equitable principles of trade").

[58] *See* 119 Cong. Rec. 6070 (1973) (proposing to authorize the Commission to "adopt rules which assure that any transaction by any registered broker or dealer or member of an exchange is executed at a net price to such member's customer which is better than or equivalent to the net price which would have been obtainable if such transaction were to have been executed … on any other exchange or otherwise than on an exchange").

[59] When Congress wants to authorize the Commission to set a standard of conduct, it knows how to say so. In 2012, for example, Congress authorized the Commission to subject a specific class of broker-dealers—broker-dealers that provide "personalized investment advice … [to] retail customer[s]"—to the same "standard of conduct … applicable to … investment adviser[s]." 15 U.S.C. § 78*o*(k)(1).

[60] For example, the NASD adopted its best-execution rule in May 1968 as part of its Rules of Fair Practice.

Commission itself has repeatedly found to be consistent with the purposes of the Exchange Act.[61] It is more than a little doubtful that the Commission's *own* authority to set a standard of best execution—to supplant the work of the self-regulatory organizations and to knock aside decades of their interpretations and guidance—has been sitting in the Commission's back pocket—unused and unacknowledged—for nearly half a century.[62]

The Commission's proposals are without statutory authority and should be abandoned for this reason alone.

B. The Proposed Rules raise significant non-delegation problems.

The Commission's proposals are also premised on a view of the Commission's rulemaking authority that cannot be squared with the Constitution's separation of powers. In particular, the proposals offend the nondelegation doctrine, which bars Congress from transferring its legislative power to another branch of Government."[63]

It is well-settled that a congressional conferral of rulemaking authority upon a regulatory agency is constitutionally permissible only if Congress sets out an "intelligible principle" to guide the agency's exercise of that authority.[64] As traditionally understood, the intelligible-principle standard requires "Congress, and not the Executive Branch, to make the policy judgments."[65] And while Congress may authorize the Executive Branch "to make factual findings," Congress, not the Executive, must "set forth the facts that the executive must consider and the criteria against which to measure them."[66] When it comes to agencies such as the Commission, which are "independent" of the Executive,[67] the concerns about accountability for policy judgments that undergird the nondelegation doctrine are heightened. A majority of the Supreme Court has indicated its support for enforcing the safeguards provided by the non-delegation doctrine,[68] and the Fifth Circuit has recently struck down Commission authority that transgresses it.[69]

The Commission's claimed authority to unilaterally dictate the configuration of the retail-equity markets violates the well-established understanding of the intelligible-principle requirement in a number of ways. First, the Commission's proposals fail the "most important[]" consideration in the test: They reflect (in Chair Gensler's words) "policy" judgments of the "five folks" on the

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[61] *See, e.g.*, *Self-Regulatory Organizations*, 61 Fed. Reg. 1419 (Jan. 19, 1996); *Self-Regulatory Organizations*, 76 Fed. Reg. 77,042.

[62] *Cf. Util. Air Regulatory Grp.*, 573 U.S. at 324.

[63] *Gundy v. United States*, 139 S. Ct. 2116, 2121 (2019).

[64] *J.W. Hampton, Jr. & Co. v. United States*, 276 U.S. 394, 409 (1928).

[65] *Gundy*, 139 S. Ct. at 2141 (Gorsuch, J., dissenting).

[66] *Id.*

[67] *See Humphrey's Ex'r v. United States*, 295 U.S. 602 (1935).

[68] *See Gundy*, 139 S. Ct. at 2131 (Alito, J., concurring in the judgment); *id.* (Gorsuch, J., dissenting) (joined by Roberts, C.J., and Thomas, J.); *Paul v. United States*, 140 S. Ct. 342, 342 (2019) (mem.) (Kavanaugh, J., statement respecting the denial of certiorari).

[69] *See Jarkesy v. SEC*, 34 F.4th 446, 462-63 (5th Cir. 2022).

Commission,[70] not of "Congress."[71] Moreover, in forcing virtually all retail-equity orders into an auction of the Commission's own, custom design, the proposed rules do not merely fill in "gaps" in the statutory scheme or "mak[e] factual findings,"[72] but craft an entirely new, generally applicable regulatory framework. Proceeding with the proposals would therefore transgress the constitutional separation of powers.

II. The Proposal is unnecessary, unjustified, and would have serious adverse consequences.

Lack of statutory authority aside, the Commission should abandon the proposals because they will do serious harm to the U.S. equity markets—for no offsetting benefit. Thus, the proposals are not just poor policy, they would be arbitrary and capricious under the APA if adopted as final rules.

The Commission does not identify—beyond "sheer speculation"[73]—any real problem that is "worthy of regulation."[74] Although the Commission now speculates that forcing virtually all retail-customer orders into an exchange-run auction mechanism *could* result in better execution quality, the Commission has for decades recognized the "distinct," "vital" benefits that flow from fostering competition *between* exchanges and other venues, including wholesale broker-dealers.[75] The data confirms the enormous benefits investors have received from this competition.[76] The Commission even *admits* that orders "routed to wholesalers appear to have higher fill rates, lower effective spreads, and lower E/Q ratios"; retail investors are "more likely to receive price improvement" than when executed on-exchange.[77] There is little to fix here, and the Commission has presented "no evidence"[78] that the market structure that has been in place for decades, supported by the considered judgment of every previous Commission, needs to be entirely redone.

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[70] *See SEC Chair Gensler Talks Markets, Regulation and More*, Bloomberg (Mar. 2, 2023), https://twitter.com/i/broadcasts/1mrGmkgOgoVxy (Chair Gensler: "Weigh in. Give us your best advice. But it doesn't– It would not surprise me. Our client is different than your clients. … There are policy differences, but we also have a different role in our society, our great nation, and our role. The five folks that really come down to is Commissioner Pierce, Commissioner Uyeda, Commissioner Crenshaw, Commissioner Lizárraga, and this guy that's privileged to be chair.").

[71] *Gundy*, 139 S. Ct. at 2141 (Gorsuch, J., dissenting).

[72] *Id.*

[73] *Sorenson Commc'ns Inc. v. FCC*, 755 F.3d 702, 708 (D.C. Cir. 2014).

[74] *N.Y. Stock Exchange LLC v. SEC*, 962 F.3d 541, 545 (D.C. Cir. 2020); *see also Nat'l Fuel Gas Supply Corp. v. FERC*, 468 F.3d 831, 843 (D.C. Cir. 2006) (Kavanaugh, J.) ("Professing that an order ameliorates a real industry problem but then citing no evidence demonstrating that there is in fact an industry problem is not reasoned decisionmaking.").

[75] *Concept Release on Equity Market Structure*, 75 Fed. Reg. 3594, 3597 n.19 (Jan. 21, 2010) (quoting *Regulation NMS*, 70 Fed. Reg. at 37,499).

[76] *See* Comments of Citadel Securities on Order Competition Rule, at Appendix A, File No. S7-31-22 (Mar. 31, 2023).

[77] *Order Competition Rule*, 88 Fed. Reg. at 186.

[78] *Nat'l Fuel Gas Supply*, 468 F.3d at 843.

To the contrary, large portions of the Commission's proposal, particularly the auctions proposal and the Commission-level best-execution rule, are "solution[s] in search of a problem."[79]

Even the Commission—which speculates that its proposals "*could* result in better execution quality"[80]—*acknowledges that the opposite could also be true*.[81] The Commission's pessimism is appropriate. As we have detailed in our comments on each individual rule proposal, the proposals, if adopted, would seriously weaken our markets and harm investors. By targeting wholesale broker-dealers, and preferencing exchanges, the Commission would cause order execution times, for instance, to be 83 times longer than they are currently.[82] Displayed liquidity would also fragment and become less stable.[83] Investors would lose out on billions of dollars in price improvement[84] and "pay more for their transactions."[85] And the client services that wholesale broker-dealers offer, such as accommodating client errors and handling special order types, would become unavailable to the vast majority of retail investors.[86] Moreover, far from making markets more efficient—a vital consideration in any Exchange Act rulemaking[87]—the Commission's proposals would *reduce* efficiency, replacing the straightforward system in place today, where retail broker-dealers route orders to wholesale broker-dealers, with a convoluted, never-before-tried system of the Commission's own imagination.[88] The Commission should not—and under the APA cannot—go down this road.

The Commission's proposals are not just wrongheaded, but also dangerous. There is no escape hatch here. The Commission is not just proposing to change one extremely consequential rule or to allow a change, even a radical change, at a single trading venue. The Commission is proposing, market-wide, to fundamentally redraw, from stem to stern, how the market functions for both retail and institutional investors. But what if it doesn't work? The Commission itself admits that the effects of its proposals are "uncertain."[89] And even more modest Commission proposals have

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[79] *District of Columbia v. U.S. Dep't of Agriculture*, 444 F. Supp. 3d 1, 31 (D.D.C. 2020). For example, the Commission's proposals have nothing to do with the recommendations of the majority or minority of the House Financial Service Committee concerning the "meme stock" event of January 2021. *See* H. Fin. Servs. Comm., Game Stopped 11-13 (2022); Memorandum from Republican Staff to Republican Members, H. Fin. Servs. Comm. (June 24, 2022), https://financialservices.house.gov/uploadedfiles/memorandum_for_fsc-rs_re_meme_stock_event_final.pdf.

[80] *Regulation Best Execution*, 88 Fed. Reg. at 5523 (emphasis added).

[81] *See, e.g.*, *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,326 ("To the extent that OTC market makers choose to not offer as much price improvement, total price improvement received by retail investors might decrease.").

[82] Comments of Citadel Securities on Order Competition Rule 17, File No. S7-31-22 (Mar. 31, 2023).

[83] Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders 5-6, File No. S7-30-22 (Mar. 31, 2023).

[84] Comments of Citadel Securities on Order Competition Rule 6, File No. S7-31-22 (Mar. 31, 2023).

[85] *Regulation Best Execution*, 88 Fed. Reg. at 5524.

[86] Comments of Citadel Securities on Regulation Best Execution 18, File No. S7-32-22 (Mar. 31, 2023).

[87] *See* 15 U.S.C. §§ 78c(f), 78k-1(a)(1)(B), (a)(1)(C)(i), (a)(1)(D).

[88] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 147 (offering "[f]or illustrative purposes" an "example" of how an order "could be handled and executed in compliance with Proposed Rule 615").

[89] *See infra* p. 13 & n.96.

shown themselves not to be immune from abject failure.[90] The Commission should not—and under the APA, is not permitted to—just roll the dice with the fate of the U.S. equity markets on the hope that some dangerous, ill-conceived thought-experiment actually works out.

III. The Proposed Rules are unlawful for other reasons.

The proposed rules independently run afoul of other statutory restrictions on the Commission's rulemaking authority.

A. The Commission's cost-benefit analysis is deeply flawed.

The Exchange Act requires the Commission to determine whether a rulemaking will "promote efficiency, competition, and capital formation"[91] and prohibits any rulemaking that "would impose a burden on competition not necessary or appropriate in furtherance of the purposes" of the statute.[92] Neglecting these statutory duties—failing to "apprise itself … of the economic consequences of a proposed regulation"—constitutes an arbitrary and capricious failure to consider statutorily required factors.[93]

We have already detailed significant, fatal shortcomings in each of the Commission's cost-benefit analyses;[94] we write here to highlight a number of overarching deficiencies between the Commission's various proposals.

Foremost, the Commission has failed to reasonably attempt to quantify the estimated costs and benefits of the proposal. The Commission repeatedly admits that it is "unable to quantify," "estimate," or "know" the economic effects.[95] And it states nearly 100 times that it is "uncertain" of the impacts its proposals will have.[96] Indeed, the tick-size limits the Commission proposes

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[90] *See* Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders 4, File No. S7-30-22 (Mar. 31, 2023) (discussing the Commission's two-year tick-size pilot program).

[91] 15 U.S.C. § 78c(f).

[92] *Id.* § 78w(a)(2).

[93] *Chamber of Commerce v. SEC*, 412 F.3d 133, 144 (D.C. Cir. 2005).

[94] *See* Comments of Citadel Securities on Order Competition Rule 5-16, File No. S7-31-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders 4-13, File No. S7-30-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation Best Execution 5-20, File No. S7-32-22 (Mar. 31, 2023).

[95] *See Order Competition Rule*, 88 Fed. Reg. at 179, 202 n.466, 217, 218, 220, 223, 224, 225; *Regulation Best Execution*, 88 Fed. Reg. at 5483, 5520 n.531, 5521, 5536; *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,303, 80,331, 80,334; *Disclosure of Order Execution Information*, 88 Fed. Reg. at 3830, 3876, 3877, 3878, 3882, 3883, 3896.

[96] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 179 ("The Commission acknowledges considerable uncertainty in the costs that would arise from Proposed Rule 615 …."); *Regulation Best Execution*, 88 Fed. Reg. at 5532 ("[T]he Commission is uncertain about these costs associated with the business practice changes needed to convert a self-directed trading business from a riskless principal to agency based model …."); *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,325 ("Requiring trades to occur at the minimum pricing increment would have uncertain net effects on total price improvement …."); *Disclosure*

appear to be based on little more than guesswork; the Commission offers no data or other evidence to explain why it picked one level over another.[97] All of this is plainly insufficient. The Commission cannot just throw up its hands and fail to "make [the] tough choices" needed to properly estimate the economic impacts of its proposals.[98]

The deficiencies in the Commission's analysis flow from an underlying issue: the Commission's refusal to acknowledge what exactly it is doing here. The Commission is attempting to eliminate payment for order flow by wholesale broker-dealers (but not from exchanges) and reduce wholesale broker-dealer internalization of retail-customer orders. It is impossible to read the proposals in any other way. Chair Gensler has been determined to eliminate payment for order flow "from the time he entered office."[99] And the proposals are all uniquely aimed at that exact purpose.[100] But the Commission refuses to say it—likely because a ban on payment for order flow could not possibly be justified. The indirect nature of the Commission's approach—to eliminate payment for order flow through other means—operates as a "distraction," preventing the Commission from "offer[ing] genuine justifications" for the decision it is actually attempting to make.[101] This is not "[r]easoned decisionmaking,"[102] as the Commission's deeply flawed economic analysis makes clear.

Among other fundamental errors, the Commission has entirely failed to consider the relationship between its pending market-structure proposals. The four proposals are overlapping and interrelated ("a package," as Commissioner Crenshaw put it[103]). Significant portions of the Commission's economic analysis are largely copied-and-pasted between proposals,[104] and the Commission encourages commenters on numerous occasions "to determine whether" one proposal

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of Order Execution Information, 88 Fed. Reg. at 3838 n.613 ("The effects on spread, price impact, and realized spread statistics in these stocks is uncertain ….").

[97] *Cf. Comcast Corp. v. FCC*, 579 F.3d 1, 8 (D.C. Cir. 2009) (finding that a "30%" limit was arbitrary and capricious because the agency could not "satisfactor[ily]" explain why it picked that level)

[98] *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1150 (D.C. Cir. 2011).

[99] *Dep't of Commerce v. New York*, 139 S. Ct. 2551, 2574 (2019); *see, e.g.*, Gary Gensler, Market Structure and the Retail Investor (June 8, 2022), https://www.sec.gov/news/speech/gensler-remarks-piper-sandler-global-exchange-conference-060822.

[100] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 225 (acknowledging that the auctions proposal is "likely" to "reduc[e]" payment for order flow and "could pose a competitive threat to retail brokers that are dependent on" payment for order flow).

[101] *Dep't of Commerce*, 139 S. Ct. at 2575-76.

[102] *Id.* at 2576.

[103] Comm'r Caroline A. Crenshaw, Statement on Proposals Related to Equity Market Structure, SEC (Dec. 14, 2022), https://www.sec.gov/news/statement/crenshaw-insider-trading-20221214-0.

[104] There is extensive overlap between the economic analysis sections in the Best Execution and Order Competition proposals. For example, nearly half of the data tables in the Best Execution proposal's economic analysis are essentially identical to tables presented in the Order Competition proposal. Approximately 25% of the Best Execution proposal's economic analysis is largely copy-and-pasted from the Order Competition proposal. *Compare Regulation Best Execution*, 88 Fed. Reg. at 5488-503, *with Order Competition Rule*, 88 Fed. Reg. at 180-211. And, perhaps most egregiously, in analyzing the impact of the Best Execution proposal on market competition, the Commission largely copy-and-pasted certain paragraphs of the Order Competition proposal's economic analysis and replaced "lower-volume exchanges" with "smaller brokers."

"might affect their comments on" another.[105] Yet at no point does the Commission consider for *itself* how the proposals will interact with each other, such as whether one rule would undermine, or make it particularly costly or difficult to implement, another.

For example, the Commission proposes to impose its own novel best-execution standard, on the one hand, and to require broker-dealers to route virtually all retail-customer orders to an auction mechanism, on the other, *even if the broker-dealer determines, under its duty of best execution, that the auction will deliver an inferior outcome*.[106] In fact, the Commission, in one proposal, states that price improvement of at least 0.1 cents is meaningful,[107] but, in the auctions proposal, provides that retail orders must be routed to an auction, even if the wholesale broker-dealer were offering 0.1 cents of price improvement.[108] This makes no sense. Likewise, in the auctions proposal, the Commission states that price improvement as low as 0.1 cents would be acceptable, as this would supposedly improve competition by giving participants the ability to "quote in finer increments than they could on exchange."[109] But, in the tick-size proposal, the Commission proposes to allow potentially thousands of stocks to be quoted on exchange at 0.1 cents,[110] thereby undermining the stated benefit of the auctions proposal.[111]

The Commission's failure to consider the relationship between its various proposals is entirely illogical, and seemingly contrary to the Commission's approach in other recent rulemakings.[112] In ignoring the relationship between its pending proposals, the Commission missed "an important aspect of the problem."[113]

In a related error, the Commission's economic analyses also failed to consider the correct "baseline." As the D.C. Circuit has explained, the Commission cannot "accurately assess" the

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[105] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 139 n.98, 142 n.130, 144 n.147, 146 n.173, 159 n.245, 178 n.343, 221 n.631, 227 n.681, 228 n.698; *Regulation Best Execution*, 88 Fed. Reg. at 5537 n.610; *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,302 n.425.

[106] *See* Comments of Citadel Securities on Regulation Best Execution 24, File No. S7-32-22 (Mar. 31, 2023).

[107] *See Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,280.

[108] *See Order Competition Rule*, 88 Fed. Reg. at 147.

[109] *Order Competition Rule*, 88 Fed. Reg. at 222.

[110] *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,269.

[111] In a similar conflict between proposals, the Commission states that the tick-size proposal would "level the playing field" between trading centers. *Id.* at 80,274. But, under that proposal, only *some* stocks could be quoted at 0.1 cents off-exchange, *id.* at 80,269, whereas, under the auctions proposal, *all* stocks could be quoted at 0.1 cents in (exchange-based) auctions, *Order Competition Rule*, 88 Fed. Reg. at 159.

[112] In February and September 2022, the Commission proposed amendments to Form PF. File Nos. S7-01-22, S7-22-22. The Commission was scheduled to hold a vote on whether to adopt one of the Form PF proposals, but abandoned that effort after market participants highlighted the absurdity of adopting one Form PF proposal without first considering the impact of and relationship with the other, "intertwined" proposal. *See* Comments from Managed Funds Association, File No. S7-22-22 (Mar. 16, 2023), https://www.sec.gov/comments/s7-22-22/s72222-20159964-328328.pdf; Douglas Gillison, *U.S. SEC delays vote on private investment reporting rule*, Reuters (Mar. 21, 2023), https://www.reuters.com/markets/us/us-sec-delays-vote-private-investment-reporting-rule-2023-03-21/.

[113] *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

economic impact of a rule on, say, efficiency or competition, without first "assess[ing] the baseline level" of efficiency or competition.[114] Here, the Commission's baseline analysis is triply flawed. *First*, the Commission's analysis is superficial—at times copied and pasted from other proposals.[115] *Second*, the Commission relies on data the Commission *admits* is inaccurate. In its Rule 605 proposal, for instance, the Commission concedes that the size improvement wholesale broker-dealers provide to retail investors is so significant that it must be included in future Rule 605 disclosures.[116] But, in the auctions proposal, the Commission uses *current* Rule 605 data to estimate the effects of the sweeping changes the Commission proposes,[117] thus entirely ignoring, as part of the Commission's baseline analysis, the size improvement wholesale broker-dealers currently provide. *Finally*, putting data issues aside, the Commission considers the relevant "baseline" to be "*existing* … practices and execution quality."[118] But even that is not accurate. The Commission is proposing to simultaneously implement four proposals. Thus, to accurately "assess any potential increase or decrease" in efficiency, competition or the like *from one of the rules*, the Commission would need to analyze the "baseline" from the assumption that *the other rules* have gone into effect.[119] Otherwise one proposal might be credited with purported benefits that another proposal would supposedly have achieved, and vice versa. That would paint an inaccurate picture of both rules.

For example, in its tick-size proposal, the Commission assumes that reducing tick sizes and implementing the new round-lot definitions would lead to reduced transaction costs for investors.[120] But, simultaneously, the Commission asserts that, under the *current* tick-size environment, its auction proposal would create $1.5 billion in investor savings.[121] The Commission cannot claim both benefits simultaneously. It cannot reasonably assert that its auctions proposal would save investors money in a regulatory environment that the Commission proposes to eliminate. Instead, to determine whether *either* the tick-size or auctions proposals were economically justifiable, the Commission would need to factor into its baseline-analysis for each rule the potential costs savings and other changes brought about by the *other* rule. The Commission, in fact, *admits* elsewhere that the proper baseline must take account of other regulatory amendments that "have not been implemented" yet,[122] but the Commission inexplicably fails, when analyzing the economic impact of each of the four proposals, to factor in the changes

[114] *Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 178 (D.C. Cir. 2010).

[115] *See supra* note 104.

[116] *See Disclosure of Order Execution Information*, 88 Fed. Reg. at 3817-19.

[117] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. 188-91, 206-09.

[118] *E.g.*, *Order Competition Rule*, 88 Fed. Reg. at 179 (emphasis added).

[119] *Am. Equity*, 613 F.3d at 178.

[120] *See Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,303.

[121] *See Order Competition Rule*, 88 Fed. Reg. at 209.

[122] *See id.* at 179 n.356.

required by the others. This incomplete, "inconsistent[]," and "contradict[ory]" analysis is not sufficient.[123]

The Commission, similarly, fails to consider the costs and benefits of its proposals "at the margin"—the same "unacceptable" error that caused the D.C. Circuit to invalidate the Commission's proxy-access rule.[124] Regarding the purported benefits of the proposals, the Commission failed to consider the proper economic baseline (factoring in all of the pending rules), and therefore failed to accurately consider the marginal benefit of each individual rule. On the cost side, likewise, the Commission failed to consider the impact on marginal costs of implementing all four market-structure rules simultaneously—changes that will pull resources from the same sources. In these circumstances, where compliance, technology, and other capacities are being used on multiple projects, marginal costs will *rise* and marginal benefits (to the extent there are any), will *fall*. The Commission, however, fails to consider this dynamic.

Finally, the Commission's economic analyses are improperly based on non-public data. The Administrative Procedure Act requires that an agency give notice of a proposed rule by setting forth "either the terms or substance of the proposed rule or a description of the subjects and issues involved,"[125] and "give interested persons an opportunity to participate in the rulemaking through submission of written data, views, or arguments."[126] "Integral" to the public's right to participate in this process "is the agency's duty 'to identify and make available technical studies and data that it has employed in reaching the decisions to propose particular rules.'"[127] A failure to reveal the "'studies and data' upon which the agency relies"[128] is a "serious procedural error" imperiling the entire proceeding.[129] The Commission made just such a serious procedural error here. The Commission, throughout its proposals, repeatedly cites Consolidated Audit Trail ("CAT") data.[130] But CAT data is not publicly available,[131] and the Commission, through subjective adjustments to the data, has otherwise made it impossible for others to scrutinize its work.[132] This is not to say that the Commission should release *raw* CAT data—it should not—but, rather, that there are certain anonymized subsets of CAT data—identified by the Securities Industry and Financial

[123] *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1149 (D.C. Cir. 2011).

[124] *Id.* at 1151.

[125] 5 U.S.C. § 553(b).

[126] *Id.* § 553(c).

[127] *Solite Corp. v. EPA*, 952 F.2d 473, 484 (D.C. Cir. 1991) (quoting *Conn. Light & Power Co. v. Nuclear Regulatory Comm'n*, 673 F.2d 525, 530 (D.C. Cir. 1981)).

[128] *Chamber of Commerce v. SEC*, 443 F.3d 890, 899 (D.C. Cir. 2006).

[129] *Solite Corp.*, 952 F.2d at 484.

[130] *See, e.g.*, *Order Competition Rule*, 88 Fed. Reg. at 150 n.194; *Regulation Best Execution*, 88 Fed. Reg. at 5496; *Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders*, 87 Fed. Reg. at 80,315.

[131] To be clear, we are not requesting that CAT data be provided in a manner that would include any personally identifiable information or an individual firm's trading data. That information is—and should be kept—confidential.

[132] *See* Comments of Citadel Securities on Order Competition Rule 16, File No. S7-31-22 (Mar. 31, 2023).

Markets Association[133]—that the Commission could easily release to allow the public to review and comment on the Commission's analysis. That is the information the Commission should release. And until it does so, it cannot proceed with a final rule.

B. The Proposed Rules cannot be squared with the Commission's own longstanding policies.

The Commission's proposal is arbitrary and capricious for another reason: it diverges, without acknowledgment or explanation, from decades of the Commission's own prior policies.[134]

For example, since the 1970s, the Commission has "resisted suggestions that it adopt an approach focusing on a single form of competition."[135] Even if that approach would be "easier to administer," the Commission has recognized that focusing on just a single form of competition—"competition among orders"—"would forfeit the distinct but equally vital, benefits associated with … competition among markets."[136] Thus, from the outset, the Commission acknowledged that it would not—and should not—"choose between an auction market and a dealer market."[137] The Commission, instead, would let competition among the various trading venues sort it out. Here, however, the Commission has taken the exact opposite approach. Without meaningfully grappling with decades of its own decisionmaking, the Commission proposes to force virtually all retail-customer orders into an auction market, thereby significantly diminishing, if not eliminating entirely, the benefit from competition among trading centers, including wholesale broker-dealers. The Commission has not explained, and cannot reasonably explain, this stark reversal.

Nor can the Commission square its current tick-size proposal with the positions it took in promulgating Regulation NMS or in connection with the transaction-fee pilot from just a few years ago. In *that* rulemaking, for example, the Commission acknowledged that it "lacks the data necessary to meaningfully analyze the impact that exchange transaction fee-and-rebate pricing models have on order routing behavior, market and execution quality, and our market structure generally."[138] The Commission, at that time, thus proposed a fee pilot. But, now, the Commission says, it has the answers after all. The Commission, however, does not reasonably explain how, today, it could reliably estimate the effects of transaction-fee changes on execution quality and the like, whereas just a few years ago, it could not even venture a guess.[139] Furthermore, when promulgating Regulation NMS, the Commission acknowledged that allowing sub-penny

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[133] *See* Letter from Securities Industry and Financial Markets Association, File No. S7-31-22 (Feb. 8, 2023), https://www.sec.gov/comments/s7-31-22/s73122-20156863-325026.pdf.

[134] *See, e.g.*, *Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 222 (2016) ("[A]n '[u]nexplained inconsistency' in agency policy is 'a reason for holding an interpretation to be an arbitrary and capricious change from agency practice.'" (second alteration in original)).

[135] *Concept Release on Equity Market Structure*, 75 Fed. Reg. at 3597 n.19 (quoting *Regulation NMS*, 70 Fed. Reg. at 37,499).

[136] *Id.* (quoting *Regulation NMS*, 70 Fed. Reg. at 37,499).

[137] SEC, *Future Structure of the Securities Markets*, *supra* n.17, at 8

[138] *Transaction Fee Pilot for NMS Stocks*, 84 Fed. Reg. 5202, 5203 (Feb. 20, 2019).

[139] *See, e.g.*, *N.Y. Stock Exch. LLC v. SEC*, 962 F.3d 541, 549 (D.C. Cir. 2020) ("The Commission expressed no views on these issues.").

quotations—exactly what the Commission proposes here—would create a variety of problems, including savvy market participants stepping ahead of competing limit orders by economically insignificant amounts, decreasing displayed liquidity (including quoted depth), increasing quote flickering, and reducing customer protections.[140] The Commission fails to adequately explain why it is taking the opposite position now.

Finally, the Commission, in other contexts, has adopted a far more measured approach to considering market changes than the Commission has employed here. When MEMX, for example, proposed to establish a retail midpoint liquidity program—a program that would impact just a single trading venue—the Commission called for an extended comment period and ultimately disapproved the idea. The Commission was concerned that retail orders under the new program would be given priority over pre-existing undisplayed orders[141] and objected that it lacked sufficient information about the program's likely effects.[142] But the Commission proposes to do the *exact* same thing here,[143] yet, in this case, is not bothered at all by the uncertainty. The Commission, in fact, has admitted nearly 100 times that it is "uncertain" about the likely effects of its proposals,[144] but it proposes to move ahead anyway. This makes no sense. The MEMX proposal was focused on the same thing the Commission is focused on here. But the MEMX proposal was far *less* risky. That proposal concerned just a single trading venue. If the proposal did not work out, trades could easily be executed elsewhere. Here, as noted, there is no escape hatch; if the Commission is wrong, *all* trades are in trouble.[145] The Commission cannot rationally explain why caution is warranted everywhere but here.

C. The Commission did not provide for meaningful public participation in the rulemaking process.

The Commission's errors are not just errors of substance, but of process. The Commission is doing too much too quickly. The 449-Federal-Register pages (1,600-normal-sized pages) of the Commission's market-structure proposals span more pages than the Commission has historically issued in rule proposals *in most years*.[146] The Commission has not given the public an adequate opportunity to meaningfully comment on all of these proposed changes, much less to fairly consider how they interact with each other.

(i) The comment period is too short.

The Commission is proposing to fundamentally restructure the nation's retail-equity markets and has provided no meaningful analysis as to how the various proposals would relate to one

[140] *See, e.g.*, *Regulation NMS*, 70 Fed. Reg. at 37,503.

[141] *See Self-Regulatory Organizations*, 87 Fed. Reg. 29,193, 29,194 (May 12, 2022).

[142] *See id.* at 29,193-94.

[143] *See Order Competition Rule*, 88 Fed. Reg. at 161 (explaining that auction responses "would be required to have priority at the same price over undisplayed orders resting on the continuous order book").

[144] *See supra* p. 13.

[145] *See supra* pp. 10-12.

[146] *See* David Woodcock et al., *How to Keep Up with the SEC's Breakneck Rulemaking Pace*, Law360 (Mar. 7, 2023), https://www.law360.com/articles/1583004/how-to-keep-up-with-the-sec-s-breakneck-rulemaking-pace.

another—leaving that task entirely to public commenters—but, at the same time, has given the public virtually no time to formulate meaningful comments. This is arbitrary and capricious.

The last time the Commission sought to do even a fraction of what it proposes here, the Commission—prior to even "formulating [its] proposals"—held "multiple public hearings and roundtables," convened "an advisory committee," issued "three concept releases," and entered a number of "temporary exemptions intended in part to generate useful data on policy alternatives."[147] Even then, the Commission extended the comment period,[148] and then re-proposed an improved version of the proposal, allowing for even more public input, six months later.[149]

The Commission has done none of that here, and has made no attempt to otherwise justify its breakneck pace or reconcile that pace with the Commission's prior, more deliberate approach.[150] Investors today are *profoundly better off* than they were when the Commission first proposed Regulation NMS in 2004. The Commission has provided no justification, let alone a reasonable justification, for barreling ahead with the radical changes it proposes here without offering at least the same level of public participation, under the same, more reasonable timeframe, the Commission decided was appropriate in 2004 and 2005.

(ii) The Commission must re-propose the rules.

The Commission's breakneck pace has hampered public participation in another way: the Commission has failed to perform its job adequately, which in turn is depriving the public of its right to notice and a meaningful opportunity to comment. The Commission has simultaneously issued four interrelated proposals that cannot all be finalized as is. The proposals, as we have demonstrated elsewhere, are not thought through[151] and contain purported analyses that are not only in some instances copied-and-pasted between proposals,[152] but also directly conflict with one another.[153] In these circumstances, it is impossible for the public to know what the Commission is *actually* proposing to adopt. Without that basic notice of what the Commission is actually proposing to do—notice required by the APA—the public cannot meaningfully participate in this rulemaking. Adding to the difficulty, the Commission, moreover, has asked hundreds of questions

[147] *Regulation NMS*, 69 Fed. Reg. 77,424, 77,425 (Dec. 27, 2004).

[148] *See Regulation NMS*, 69 Fed. Reg. 30,142 (May 26, 2004).

[149] *See Regulation NMS*, 69 Fed. Reg. 77,424.

[150] *See Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 222 (2016) (any "unexplained inconsistency in agency policy" is a reason to hold agency action arbitrary and capricious).

[151] *See* Comments of Citadel Securities on Order Competition Rule, File No. S7-31-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, File No. S7-30-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation Best Execution, File No. S7-32-22 (Mar. 31, 2023).

[152] *See supra* note 104.

[153] *Supra* pp. 14-16; *see also* Comments of Citadel Securities on Order Competition Rule 29-30, File No. S7-31-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders 28-29, File No. S7-30-22 (Mar. 31, 2023); Comments of Citadel Securities on Regulation Best Execution 24-25, File No. S7-32-22 (Mar. 31, 2023).

about potential alterations to the proposals. The number of permutations of potential final rules, and the interrelation between them, is incalculable; there is simply no way to meaningfully comment on the proposals as a whole.

The Commission, as it did when it first proposed Regulation NMS, must decide what it actually wants to do, and then re-propose *that* consolidated approach, so that the public can have a meaningful opportunity to comment on the "combined impact of" the Commission's proposals.[154] The APA's notice-and-comment requirements are not a mere box-checking exercise. The Commission, like any other agency, must make publicly available any facts or information that a person reasonably needs to offer "useful criticism" of the proposal.[155] Just as an agency would need to disclose the model on which it relied[156] or the technical studies underlying its analysis,[157] the Commission must also offer its four proposals in a "concrete and focused form."[158]

Without that, the opportunity for comment is meaningless. Each of the Commission's rule proposals would indisputably have wide-ranging effects on market liquidity, including with respect to quoted spreads, quoted size, market depth, order routing, and exchange market share.[159] But the magnitude and direction of those effects will turn on what the Commission ultimately chooses to do. *And all of that is in flux*. With hundreds of potential changes in play across four interlocking proposals, commenting in the current rulemaking is like trying to solve a Rubik's Cube when the colors keep changing depending on the angle at which the object is viewed. The Commission must determine what it actually proposes to do and then expose that unified, cohesive approach to public comment. Only then will the public have true notice of what the Commission proposes for the national market system; only then will it have the opportunity to meaningfully comment as guaranteed by law.

D. The Commission failed to adequately consider reasonable, less-burdensome alternatives.

Lastly, the Commission has failed to adequately consider reasonable, less-disruptive, lower-risk alternatives. The consensus position of NYSE Group, Inc., Charles Schwab & Co., and Citadel Securities is an obvious, reasonable, more efficient path forward.[160]

NYSE, Charles Schwab, and Citadel Securities are respectively the largest exchange group, retail brokerage firm, and wholesale broker-dealer, and thus represent significant, distinct aspects

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[154] *Immigrant Legal Res. Ctr. v. Wolf*, 491 F. Supp. 3d 520, 541 (N.D. Cal. 2020).

[155] *Am. Radio Relay League v. FCC*, 524 F.3d 227, 236 (D.C. Cir. 2008)

[156] *See Owner-Operator Indep. Drivers Ass'n, Inc. v. Fed. Motor Carrier Safety Admin.*, 494 F.3d 188, 201 (D.C. Cir. 2007)

[157] *See, e.g.*, *Am. Radio Relay League*, 524 F.3d at 236-40; *Lloyd Noland Hosp. & Clinic v. Heckler*, 762 F.2d 1561, 1565-66 (11th Cir. 1985); *United States v. Nova Scotia Food Prods Corp.*, 568 F.2d 240, 251-52 (2d Cir. 1977).

[158] *Home Box Off., Inc. v. FCC*, 567 F.2d 9, 36 (D.C. Cir. 1977).

[159] As discussed below, *infra* pp. 21-22, the Commission could take a measured, incremental approach and enhance execution-quality disclosures (Rule 605) before going further.

[160] *See* Letter from NYSE Group, Inc., Charles Schwab & Co., and Citadel Securities (Mar. 6, 2023) ("Consensus Letter").

of the overall U.S. equity markets. These firms do not agree on everything, but one thing is clear to them all: the Commission has failed to adequately assess the impact of its proposals and should withdraw the overwhelming majority of the proposed changes. The Commission could, without harming the markets, take a measured, incremental approach and enhance execution-quality disclosures, implement modest quoting-increment changes, and (but for the Commission's lack of legal authority[161]) set certain trading increments.[162] Beyond that, however, the rest of the Commission's proposals would create a massive "risk of negative outcomes for markets and investors, including the risk of firms retreating from being liquidity providers—which would be particularly detrimental to retail investors."[163]

The Commission has a duty to act thoughtfully. After the Commission implements the changes mentioned above, along with the revised round-lot definition *already* contained in the Commission's Market Data Infrastructure Rule, the Commission should take time "to assess the cumulative impact on market liquidity, efficiency, and competition."[164] The changes recommended here would, in and of themselves, "constitute one of the most significant changes to U.S. equity market structure since Regulation NMS was implemented in 2005."[165] The Commission should see what effect *those* changes have on the market before going further.

Other market participants support this approach. Cboe Global Markets, State Street Global Advisers, T. Rowe Price, UBS Securities LLC, and Virtu Financial, LLC—a diverse group of leading asset managers, exchanges, ETF issuers, broker-dealers, and liquidity providers—have put forth a similar proposal,[166] and recognize, like NYSE, Charles Schwab, and Citadel Securities, that the Commission's current proposals go too far, too quickly.

* * *

The rules, as proposed, would be an unprecedented, unauthorized, unwarranted, and ultimately harmful intervention in what are currently the most efficient and resilient markets in the world. A desire to target wholesale broker-dealers in no way justifies the radical, ill-conceived changes the Commission proposes. Based on insufficient evidence and analysis, the Commission threatens to upend current equity market structure in the United States and replace it with a collection of experimental proposals that could materially harm investor experiences and capital formation in the United States. To actually better our markets requires a thoughtful, sequenced path, and NYSE, Charles Schwab, and Citadel Securities have recommended exactly that.[167]

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[161] *See supra* pp. 7-8.

[162] Consensus Letter 1-2.

[163] *Id.* at 1.

[164] *Id.* at 3.

[165] *Id.*

[166] *See* Letter from Cboe Global Markets, State Street Global Advisers, T. Rowe Price, UBS Securities LLC, and Virtu Financial, LLC, File Numbers S7-29-22, S7-30-22, S7-31-22, S7-32-22 (Mar. 24, 2023).

[167] *See* Consensus Letter at 3.

Respectfully,

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