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Invested in America

July 18, 2019

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

Re: ***SIFMA Comment Letter on Cboe EDGA Proposed Rule Change to Introduce a Liquidity Provider Protection; File No. SR-CboeEDGA-2019-012***

Dear Ms. Countryman:

The Securities Industry and Financial Markets Association ("SIFMA")[1] submits this letter to comment on Cboe EDGA's proposal[2] to introduce a liquidity provider protection—effectively, an asymmetric speed bump—that would not be protected by the Order Protection Rule ("OPR") of Regulation NMS.[3] Cboe's proposal, and the lack of OPR protection for the speed bump, raise significant questions on the resulting impact on broker-dealers' regulatory obligations, including best execution obligations, under a scenario in which an exchange operates continuously without OPR protection. Prior to deciding to approve or disapprove Cboe's proposal, the Commission should consider and address the impact of the speed bump on other regulatory obligations, and in particular should provide guidance on broker-dealers' best execution obligations for routing decisions involving exchanges not subject to the OPR.

As background, SIFMA has previously expressed concern with asymmetrical speed bumps and their impact on equity market structure.[4] We strongly support

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[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate for legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] Securities Exchange Act Release No. 86168 (June 20, 2019).

[3] 17 CFR 242.611.

[4] *See* Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, SIFMA to Brent J. Fields, Secretary, Securities and Exchange Commission dated May 17, 2017 ("SIFMA 2017 Letter");

innovation in the equity markets, and we appreciate the spirit of innovation behind Cboe EDGA's proposal. However, SIFMA remains concerned with the market implications of an access delay that discriminates based on type of order submitted (liquidity taking vs. liquidity providing).[5] The proposal does not explain the current harm to liquidity providers that needs amelioration through a delay and how this proposal incentivizes tighter quotes or other benefits. Allowing exchanges to intentionally delay quotes to benefit certain parties could result in market makers widening quotes in the broader market to account for displayed prices that are not actionable or predictable. For instance, a previous academic study evaluating the impact of a Canadian speed bump offered by an unprotected exchange that similarly delayed liquidity taking orders found that, in aggregate, liquidity was negatively impacted, with increased market-wide costs for liquidity takers.[6] Further, Commission approval of Cboe's proposal likely would encourage other exchanges to implement additional and longer delays, potentially resulting in exchanges competing to execute orders slower.

On the proposal itself, the speed bump would allow resting orders to be updated before other traders can execute at those quotes. All incoming executable orders that remove liquidity would be subject to the speed bump, while all orders that add liquidity (and any cancellations of such orders) would avoid the speed bump. Cboe EDGA has proposed a four millisecond delay, and because this delay exceeds the de minimis threshold for intentional access delays, these quotes cannot be executed "immediately and automatically" under the Commission's guidance.[7] Accordingly, Cboe EDGA seeks to disseminate a quotation that would not be protected by the OPR.[8] In this regard, we ask the Commission to consider whether suspending OPR for this venue would alleviate our previously expressed concerns with intentional asymmetric access delays potentially resulting in increased market complexity and costs, without providing sufficient benefits to the market.[9]

In addition, the proposal raises questions about the application of the duty of best execution, which is a fundamental part of broker-dealer regulation. A broker-dealer's obligation to obtain best execution is partly based on the common law agency duty of

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Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, SIFMA to Brent J. Fields, Secretary, Securities and Exchange Commission dated December 16, 2016 ("SIFMA 2016 Letter") .

[5] SIFMA 2017 Letter at 2 – 3.

[6] See The Value of a Millisecond: Harnessing Information in Fast, Fragmented Markets (Chen, Foley, Goldstein, Ruf, 2016).

[7] SEC Staff Guidance on Automated Quotations under Regulation NMS (June 17, 2016).

[8] Rule 611 of Regulation NMS

[9] SIFMA 2016 Letter at 5.

loyalty, which obligates an agent to act exclusively in the principal's best interest, and has been incorporated explicitly in FINRA Rule 5310 and explained by the Commission. In particular, the Commission has provided a non-exhaustive list of factors that firms should consider as part of their best execution analysis, including: (1) the size of the order; (2) the trading characteristics of the security involved; (3) the availability of accurate information affecting choices as to the most favorable market center for execution; and (4) the cost and difficulty associated with achieving an execution in a particular market center. To our knowledge, there is no specific rule or guidance on applying best execution principles to routing quotes to an unprotected exchange compared to other protected exchanges.

When reviewing a broker-dealer's execution results under the current rules and guidance, an order routed to a venue where the quote is not immediately executable—could make it difficult to determine whether routing to or posting on Cboe EDGA would satisfy best execution and other related obligations. If Cboe EDGA displayed better prices, available size and fill rates, a broker-dealer presumably could route orders there consistent with its best execution obligations even though the quote is not immediately accessible. However, the question arises of whether a broker-dealer could really decide to route a liquidity taking order to another venue even if Cboe EDGA displays the best price when the Cboe EDGA quote is not protected. Considering that best execution does not require a broker-dealer to solely route to the venue displaying the best price, whether protected or not, the Commission should clarify that broker-dealers do not necessarily have to access or route to an unprotected venue that displays the best quote. Further, the Commission should provide recommendations on how retail broker-dealers and asset managers should measure the execution quality of broker-dealers routing (or not routing) orders to a non-OPR venue displaying the best price when the quote is not immediately executable and obtainable. Simply put, the Commission should provide guidance on best execution in a non-OPR environment and in a U.S. equities marketplace that would support both protected and non-protected quotes prior to any approval of the proposal.

Additionally, the Commission should consider the following issues in considering whether to approve or disapprove the proposal:

- The calculation of Rule 605 statistics with the speedbump of 4 milliseconds;

- The inclusion of Cboe EDGA's non-protected quote in the National Best Bid and Offer ("NBBO"), and whether the SIPs will disseminate a new Protected Best Bid and Offer ("PBBO") that would not include Cboe EDGA's non-protected quote; and

- How Cboe EDGA's non-protected quote should be used in calculating mid-point values, and whether the mid-point will be calculated based on NBBO or PBBO.

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SIFMA greatly appreciates the Commission's consideration of the issues raised above and would be pleased to discuss these comments in greater detail. If you have any questions or need any additional information, please contact me (at 202-962-7383 or tlazo@sifma.org).

Sincerely,

Theodore R. Lazo
Managing Director and
Associate General Counsel

cc: The Honorable Jay Clayton, Chairman
The Honorable Robert J. Jackson Jr., Commissioner
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner
The Honorable Allison Herren Lee, Commissioner

Brett Redfearn, Director, Division of Trading and Markets