October 22, 2013

**Via Electronic Mail (rule-comments@sec.gov)**

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: Comments on Decimalization Roundtable (Release No. 34-68510; File No. 4-657)

Dear Ms. Murphy:

Citigroup Global Markets Inc. ("CGMI") and its affiliates, Automated Trading Desk Financial Services, LLC ("ATD"), LavaFlow, Inc. ("FLOW"), and Citigroup Derivatives Markets Inc. ("CDMI" and, together with CGMI, ATD and FLOW, "Citi")[1] appreciate the opportunity to comment on the above-referenced Decimalization Roundtable hosted by the U.S. Securities and Exchange Commission (the "SEC" or "Commission"). In particular, Citi supports the adoption of a pilot program to widen tick sized in certain securities and offers the following suggestions for how such a pilot program may operate.

As stated in our comment letter on the SEC's Concept Release on Equity Market Structure in 2010[2], Citi's view continues to be that the U.S. equity markets remain the most robust in the world. Trading in most equity securities – especially large cap names – seems to be functioning well, with ample liquidity, narrow spreads, low transaction costs (in large part because of the availability of off-exchange venues), quick and efficient executions, and plentiful opportunities for price/size improvement (especially

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

[2] Letter from Daniel Keegan, Managing Director, Citigroup Global Markets Inc. (May 5, 2010), available at http://www.sec.gov/comments/s7-02-10/s70210-174.pdf ("Citi Comment Letter on the SEC Concept Release").

for retail investors). The data shows that execution quality continues to improve across investor classes, especially in less than block size trading.

Even with such robust markets, we do see room for improvement in some small to mid-cap names, where liquidity can be scarce, making trading more difficult. Citi continues to be supportive of a pilot program in wider tick sizes for illiquid and high-priced securities, with a goal of improving liquidity in such names.[3] We feel this is a more targeted and nuanced approach to improving current market structure (the so-called "scalpel" approach), as opposed to some more draconian measures like a "Trade-At" Rule (the so-called "sledgehammer" approach).

## GOAL OF A TICK SIZE PILOT PROGRAM

We believe wider tick sizes would help enhance liquidity and therefore we support a tick size pilot program with such a measurable goal, one that can be evaluated at the end of the pilot program to determine its relative success or failure. Measurements of enhanced liquidity should include the size of quotes/orders available at the NBBO (National Best Bid or Offer), as well as the amount of overall trading which occurs in the security (corrected for overall market share variances during the period of the pilot versus the comparison period). In addition, we would look to other measures such as average trade size (which we would expect to increase as liquidity is concentrated at wider increments) and intraday volatility (which we expect to dampen as the market offers more liquidity at each price point). We do not feel that we should look at more indirect measures such as proliferation of research on companies included in the pilot program, as Citi believes this would take longer to manifest. In particular, many firms may be reticent to increase research coverage unless and until the pilot program becomes permanent.[4]

In some cases, increasing the minimum quoting increment from a penny to a nickel makes sense; in other cases, increasing the increment to a dime (depending on average daily volume traded and stock price) or even a quarter (particularly for very high-priced securities) may be warranted. One of the outcomes of a potential pilot program

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[3] Please note our comments in the Citi Comment Letter on the SEC Concept Release: "[F]or stocks that trade over a sufficiently high threshold (e.g., $20.00 per share), CGMI suggests that the Commission should consider a minimum increment in excess of a penny (e.g., $0.02, or perhaps $0.05 in higher-priced securities). CGMI believes that an increased minimum increment for high dollar value stocks would improve market quality by reducing the 'penny jumping' effect that allows stepping ahead of lit orders by economically insignificant amounts. CGMI believes such an initiative would encourage participants to display more public quotations."

[4] To be sure, Citi believes that these indirect benefits are likely to result from such a program. However, the primary focus for the analysis of the pilot program should be whether or not liquidity was enhanced in the subject securities.

should be to create objective standards for determining the appropriate quoting increment for particular types of securities.

## OVERALL PARAMETERS

Citi supports an expansive view of which issuers would be eligible for inclusion in such a pilot program. Congress has already determined the scope of companies eligible for inclusion in such a pilot via the JOBS Act definition of an "emerging growth company" – defined in the Securities Act and the Exchange Act as an issuer with "total annual gross revenues" of less than $1 billion during its most recently completed fiscal year." We believe this definition may provide an appropriate starting point for a tick size pilot program. However, this would not address the issue of illiquid trading in many other securities in the market today. For that reason, Citi proposes that such a pilot should include a representative sample of other issuers as well.

Within that defined group, there are certain companies whose stocks already effectively quote at nickels, dimes or quarters. We believe that a pilot should include some securities that already effectively trade in nickels, dimes and quarters, as well as some securities that do not (in order for the test to be effective). We do not support the notion that issuers should be permitted to choose either their threshold involvement in the pilot program or the specific size of their tick increment. In our view, inclusion in the program and size of the tick increment should be based on objective standards that are agreed upon by regulators and market participants. Having an objective standard makes the process more predictable and we believe reduces the threat of gaming the pilot.

The duration of the pilot should be one year, with the opportunity to extend for an additional one year if more data is needed for a proper analysis. We believe this would give enough time and data to measure the effects of the wider quoting increments, but is not so long that it becomes unclear to market participants whether the pilot would ever become permanent. Again, we believe some of the more indirect benefits of wider increments, such as proliferation of research on companies included in the pilot program, may take longer to occur given that firms may be reticent to increase research coverage unless and until the pilot program becomes permanent.

Citi notes that there seems to be conceptual support for a pilot program in wider increments among a broad swath of market participants, including many issuers, buy-side investors, sell-side firms, exchanges, academics and certain members of Congress. In our view, the most controversial aspect of such a pilot program appears to be the issue of "Quote vs. Trade" – i.e., whether to allow trading at increments smaller than the new, wider quoting increments.

Citi respectfully offers that an analogy exists in the current equity market structure, which provides for quoting in penny increments in most names yet allowing for internalizers (such as ATD) to trade within those penny spreads, thereby offering price

improvement to a majority of retail orders it executes. The benefits of internalization of order flow by broker-dealers are widely accepted, including those noted above: enhanced liquidity, narrower spreads, lower transaction costs, quicker and more efficient executions, and increased opportunities for price/size improvement (especially for retail investors).[5]

## CITI'S PROPOSAL

Therefore, Citi proposes that any potential pilot program should provide for the ability to quote in wider increments; in addition, it should also allow for market centers to trade at the midpoint of the wider spread; and lastly, it should allow for registered market makers handling retail order sending firms' orders in the marketplace to trade at various levels within the wider spread, offering an opportunity for price improvement to incoming orders.[6] This is no different than what wholesale internalizers/retail market makers (such as ATD) do today to provide price/size improvement to retail orders.

We feel this would also serve as a proxy for the "Trade-At" debate, which the SEC inquired about as part of its 2010 Concept Release on Equity Market Structure and has recently resurfaced in the public discourse.[7]

**Citi's proposed pilot program would include three discrete "buckets", or "Experimental Groups", with the following characteristics:**

**BUCKET I: securities quoted in wider increments but that trade only at the NBBO. (Please note that while we are including this bucket, we are concerned that eliminating any opportunity for price improvement might prove detrimental to retail investors and could lead to higher trading costs. Nonetheless, we believe it is important at the very least to consider this bucket for purposes of a pilot program, if only for the sake of comparison to the other two buckets.)**

**BUCKET II: securities quoted in wider increments but market centers can trade at the midpoint of the wider spread.**

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[5] Please note our comments in the Citi Comment Letter on the SEC Concept Release: "CGMI believes that internalization helps provide demonstrably better execution quality to investors...Internalization is a direct benefit to the investing public. For example, one CGMI affiliate provided more than $70 million in price improvement on approximately 29.3 billion shares in 2009. Moreover, internalization also helps to dampen volatility by providing size improvement opportunities to customers."

[6] There is some precedent for preferential treatment of retail orders under the various retail liquidity programs offered by certain exchanges (as recently approved by the SEC Staff).

[7] See, e.g., the Public Roundtable on Equity Market Structure Issues hosted by Rep. Scott Garrett (R-NJ) on May 13, 2013.

**BUCKET III: securities quoted in wider increments but market centers can trade at the midpoint of the wider spread, and registered market makers handling retail order sending firms' orders in the marketplace can trade at various levels within the wider spread, offering an opportunity for price improvement to incoming orders. Functionally, this is how the market operates today.**

We have heard some criticism that price improvement offered by market makers is, in many cases, *de minimis* or not "meaningful". Therefore, in this third bucket, Citi would consider the possibility of requiring a minimum level of price improvement in the wider-spread stocks, perhaps 10% of the spread (so for stocks that trade in nickels, a minimum price improvement of half a penny per share, and for stocks that trade in dimes, a minimum price improvement of a full penny per share). We believe such a level of price improvement is quite meaningful, especially to retail investors. Another alternative would be a minimum size obligation for market makers, perhaps 500 shares instead of 100 shares currently. We believe such a minimum size obligation would make it difficult for automated market makers to continue to provide as much liquidity as they currently do, thereby having the opposite of the intended effect of this pilot program. As such, Citi would support a minimum level of price improvement in wider-spread stocks over a minimum size obligation, but we welcome further debate on this issue. In no event could we support both heightened obligations.

Some issuers may strenuously object to our belief that they should not be permitted to choose either their threshold involvement in the pilot program or the specific size of their tick increment. In that case, then we may consider the possibility of issuers being able to choose which of the three buckets they wish to be in during the duration of the pilot program. That said, it remains our recommendation to base all such decisions on objective standards that are agreed upon by regulators and market participants.[8]

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[8] For reference, we thought it might be useful to review how the SEC chose the securities to be included in a previous pilot program like the short sale pilot. While the specific methodology may not be entirely applicable in this case, it is a good example of where the SEC used a data-driven procedure to select stocks for a pilot program: "A pilot that includes a subset of securities from the Russell 3000 provides a balanced and targeted approach to assessing the efficacy of a price test for short sales for a broad range of securities. The average daily dollar volume for the securities in the Russell 3000 index in 2003 was $22.9 million dollars. We selected the securities to be included in the Pilot by first excluding the 32 securities in the Russell 3000 index as of June 25, 2004 that are not Nasdaq national market securities ("NNM"), listed on the American Stock Exchange ("Amex"), or listed on the New York Stock Exchange ("NYSE") because short sales in these securities are currently not subject to a price test. We also excluded issuers whose initial public offerings commenced after April 30, 2004. We then sorted the remaining securities into three groups -- Amex, Nasdaq NNM and NYSE -- and ranked the securities in each group by average daily dollar volume over the one year prior to the issuance of this order from highest to lowest for the period. In each group, we then selected every third stock from the remaining stocks." *SEC Release No. 50104 / July 28, 2004:* http://www.sec.gov/rules/other/34-50104.htm

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We expect that other critics of this proposal will point out the added complexity that it brings to bear on the markets. Further, we recognize the systems and technology work that would be required to program for the three distinct Experimental Groups we are proposing, which may be especially daunting given there is no guarantee that the pilot would become permanent.

While we recognize the merits of such arguments, we believe that this approach could potentially resolve many disputes in our industry regarding both small and mid-cap liquidity problems, as well as provide valuable feedback on the broader "Trade-At" debate. We are aware that there is an incremental increase in the cost of a pilot program that includes our unique three-bucket approach, but we believe that this incremental cost difference is preferable to conducting a narrower pilot study, only to realize later that the pilot did not solicit enough data to draw definitive conclusions. By providing a pilot program that includes these three "Experimental Groups" – rather than only one, predetermined group – the Commission would have more data to review, providing the opportunity to decide which of the three "buckets" had the most positive impact on liquidity. The pilot program we are conceiving is finite, its goals are measurable and its conclusions would ultimately be very defensible. In the end, the data would decide the best path for the markets to follow on a permanent basis.

## CONCLUSION

We sincerely appreciate the opportunity to comment on a potential tick size pilot, and we welcome feedback from all market participants on our proposal for its structure. Citi respectfully requests that the Commission consider its suggestions for such a tick size pilot program. We look forward to discussing the matter further with the Commission and its staff. If you have any comments or questions, please do not hesitate to contact me at 212.723.1812 or daniel.keegan@citi.com.

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Sincerely,

Daniel Keegan
Managing Director,
Head of Equities for the Americas

cc: The Honorable Mary Jo White, Chair
The Honorable Daniel M. Gallagher, Commissioner
The Honorable Luis A. Aguilar, Commissioner
The Honorable Kara Stein, Commissioner
The Honorable Michael Piwowar, Commissioner
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