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June 13, 2023

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

Via E-Mail: rule-comments@sec.gov

Re: Proposed Regulation SCI Revisions; Release No. 34–97143; File No. S7-07-23; RIN 3235-AN25

Dear Ms. Countryman:

MarketAxess Holdings Inc. ("MarketAxess") appreciates the opportunity to provide the Securities and Exchange Commission ("SEC" or "Commission") with our comments regarding the proposed amendments to Regulation Systems Compliance and Integrity (''Regulation SCI'') under the Securities Exchange Act of 1934 (''Exchange Act'').[1] MarketAxess operates the leading institutional electronic trading platform for corporate bonds and other fixed income securities. Through its registered broker-dealer, MarketAxess Corporation, and its global affiliates, more than 2,000 firms traded a record $8.4 trillion of U.S. investment-grade bonds, U.S. high yield bonds, emerging market debt, Eurobonds, Treasuries, and other fixed income securities on the MarketAxess platform in 2022. MarketAxess' Open Trading™ marketplace is regarded as the premier all-to-all trading solution in the global credit markets, creating a unique liquidity pool for a broad range of credit market participants.

I. Background.

Pertinent to our comments below, the Proposed Rules would expand the scope of Regulation SCI to include SCI broker-dealers.[2] Under the Proposed Rules, an "SCI broker-dealer" would be defined as a broker-dealer that: (1) in at least two of the four preceding calendar quarters has total assets in an amount that equals five percent (5%) or more of the total assets of all security brokers and dealers; or (2) transacted ten percent (10%) or more of the reported average daily dollar volume in NMS stocks, exchange-listed options, U.S. Treasury securities or Agency securities during at least four of the preceding six calendar months. While these volume thresholds would not include corporate debt securities or municipal securities, the Commission has also requested comment on whether ATSs and broker-dealers that trade significant volume in these securities should be subject to Regulation SCI, and, if so, what an appropriate volume threshold would be.

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[1] See 88 Fed. Reg. 23146 (April 14, 2023) (the "Proposed Rules").

[2] The SEC has also proposed to make a number of other amendments to Regulation SCI, and our comments on certain of these proposed amendments are set forth below.

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II. Application of Regulation SCI to Fixed Income ATSs

As discussed in more detail below, we do not believe that it is necessary or appropriate for the Commission to require ATSs that facilitate the trading of corporate debt securities or municipal securities (hereafter, "Fixed Income ATSs")[3] to be subject to Regulation SCI at this time.

A. Timing Concerns.

The Commission's rules relating to alternative trading systems[4] are currently under review. In January 2022, the Commission proposed to expand the definition of "alternative trading system" by revising Rule 3b–16 to include communication protocol systems that bring together buyers and sellers through the use of non-firm trading interest.[5] In April 2023, the Commission reopened the comment period on the 2022 Proposal in response to comments regarding its potential impact on trading systems for crypto asset securities, and requested further information and public comment on other aspects of the 2022 Proposal.[6] We note in particular that in the Reopening Release, the Commission raised the question of whether it should replace the proposed term "communication protocols" with the term "negotiation protocols" and define the latter term to mean a "nondiscretionary method that sets requirements or limitations designed for multiple buyers and sellers of securities using trading interest to interact and negotiate terms of a trade."

As the foregoing discussion indicates, the definition of "alternative trading system" is in flux. The application of Regulation SCI to fixed income trading platforms may cause them to revisit their business models, thus potentially altering the competitive landscape in this market. However, it is not possible for these platforms to determine whether such action may be necessary or whether they would even be an ATS subject to the potential application of Regulation SCI until the Commission finalizes the definition of "alternative trading system." Thus, we believe that before the Commission can determine whether and to what extent Regulation SCI should apply to Fixed Income ATSs, it must conclude its Rule 3b-16 rulemaking process.

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[3] For purposes of this discussion, any reference to a "Fixed Income ATS" is intended to refer to an ATS that facilitates transactions in corporate debt securities and municipal securities and does not include an ATS that facilitates transactions in government securities.

[4] SEC Rule 300 defines the term "alternative trading system" by reference to SEC Rule 3b–16, which currently provides that an organization will fall within the definition of the term "exchange" under Section 3(a)(1) of the Exchange Act if it: (1) brings together the orders for securities of multiple buyers and sellers; and (2) uses established, non-discretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade.

[5] See 87 Federal Register 15496 (March 18, 2022) (the "2022 Proposal").

[6] See 87 Federal Register 29448 (May 5, 2023) (the "Reopening Release").

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B. Fixed Income Market Considerations

In the Proposing Release, the Commission asked whether the gap between the equity and fixed income markets with respect to their reliance on automation and electronic trading strategies has narrowed to the point that significant Fixed Income ATSs should be subject to increased technology oversight under Regulation SCI. We believe that this gap remains significant and that the equity markets differ from the fixed income markets in that the equity markets are almost entirely electronic and are completely dependent on sophisticated technology systems relating to the provision of consolidated market data, intermarket connectivity, and order routing and complex audit trail mechanisms that aggregate trading data across the various exchanges.

In this regard, it seems clear that the interconnectedness of the equity markets was one of the main factors behind the adoption of Regulation SCI. For example, when the Commission adopted Regulation SCI, it specifically rejected the idea of applying Regulation SCI only to those exchanges that crossed a certain transaction activity threshold. In making this determination, the Commission noted that all exchanges are subject to a variety of specific public obligations under Regulation NMS which, among other things, (x) designates the best bid or offer of such exchanges to be protected quotations, and (y) requires market participants to send orders to any one of these exchanges at any given time if such exchange is displaying the best bid or offer. As a result, the Commission determined that it was important for the safeguards of Regulation SCI to apply equally to all exchanges irrespective of trading volume.[7] By contrast, the fixed income markets lack such interconnectivity because, among other things, no similar obligations apply in these markets.

The Commission chose not to apply Regulation SCI to the fixed income markets because it believed that a systems issue in these markets would not have had as significant an impact as in the equity markets. Among other things, the Commission observed that the fixed income markets relied much less on automation and electronic trading than the equities markets, and that they also tended to be less liquid than the equity markets, with slower execution times and less complex routing strategies.[8]

The current technology divide between the equity and fixed income markets is exemplified by the Commission's recent equity market structure proposals. Among other things, these proposals address items such as: (1) revising the content of the SEC's Rule 605 reports to include highly granular statistical measures of execution quality measured in increments of a millisecond or finer;[9] (2) the adoption of four tiers of minimum pricing increments for NMS stocks which are based on the time-weighted average quoted spread for these stocks over an evaluation period;[10] and (3) the imposition of substantial new duties on broker-dealers by requiring pre-internalization

[7] See Securities Exchange Act Release No. 73639 (Nov. 19, 2014).
[8] Id.
[9] See 88 Federal Register 3786 (January 20, 2023).
[10] See 87 Federal Register 80266 (December 29, 2022).

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auctions lasting from 100 to 300 milliseconds for certain types of retail orders.[11] It is evident that proposals of this type are not relevant to the fixed income markets due to differences in automation, liquidity, and market structure.

It is our experience that the current level of electronic trading in the fixed income markets is still relatively low. For example, in four of our largest product areas, we estimate that the level of electronic trading as a percentage of all means of trading for U.S. high-grade bonds, U.S. high-yield bonds, municipal bonds, and emerging market debt are approximately 40%, 30%, 15%, and 10%, respectively. In addition, on average, the fifty most liquid U.S. investment grade bonds trade just fifty times per day in the entire market—this is worlds' apart from the equity market.

While the fixed income markets have certainly evolved since the adoption of Regulation SCI, their use of equity market mechanisms such as limit order books and algorithmic trading strategies is still in the preliminary stages. Moreover, liquidity in the fixed income markets varies significantly across different securities as many securities trade episodically. The liquidity that does exist is often dispersed across a number of different trading venues, electronic and voice, that lack the intermarket connectivity that is present in the equity markets. In addition, most trading volume on fixed income platforms occurs through the use of the RFQ protocol, which is a relatively low speed, high-touch, one-to-many order delivery mechanism that does not present the same systemic risk concerns as the high-speed data access, processing, and execution mechanisms utilized in the equity markets.[12] Thus, we are concerned that applying Regulation SCI to Fixed Income ATSs at this time would be premature and would potentially discourage innovation in the fixed income markets. Accordingly, we believe that it would not be necessary or appropriate for the Commission to apply the requirements of Regulation SCI to Fixed Income ATSs at this time.

However, we believe that there are less prescriptive means of achieving the Commission's goals. As we have previously noted,[13] the capacity, integrity, and security requirements set forth in SEC Rule 301(b)(6) apply when an ATS, during at least four of the preceding six months, had 20 percent or more of the average daily volume of corporate debt securities or municipal securities traded in the United States. As we have previously stated, we believe that the Commission should revise Rule 301(b)(6) so that it applies to all Fixed Income ATSs regardless of volume. One benefit of this approach is that it would level the playing field between Fixed Income ATSs regardless of trading protocol. Second, it is unlikely that any current ATS will ever hit the 20% threshold in SEC Rule 301(b)(6) unless the definition of ATS is expanded to include communication or negotiation protocols. We also believe the requirements of SEC Rule 301(b)(6) are more appropriate for fixed income platforms and that the market has not evolved enough to alter the SEC's original logic for relying on SEC Rule 301(b)(6) rather than Reg SCI.

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[11] See 88 Federal Register 128 (January 3, 2023).
[12] See SEC Staff Report on Algorithmic Trading in U.S. Capital Markets (August 5, 2020).
[13] See letter from Scott Pintoff, General Counsel, MarketAxess, to Vanessa Countryman, Secretary, Commission, dated March 1, 2021.

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III. Issues Arising under Proposed Rules.

A. Scope

It is not clear under the Proposed Rules whether a broker-dealer that sponsors an ATS and executes transactions on the ATS as matched principal (a "Matched Principal ATS") should count this trading activity towards determining whether it is an SCI broker-dealer or an SCI ATS, or both. In order to resolve this matter, we believe that the Commission should revise the Proposed Rules to clarify that a Matched Principal ATS should count the volume it executes in this capacity only towards determining whether it is an SCI ATS, and not toward determining whether it is a SCI broker-dealer. In this regard, we note that under the MarketAxess Open Trading protocols, MarketAxess Corporation conveys the trading interest communicated among platform participants in its own name and is interposed as the counterparty to all transactions to preserve the anonymity of the parties. From the lack of any discussion regarding ATS activity or protocols in the Proposing Release, it seems clear that the proposed expansion of Regulation SCI to SCI broker-dealers was not intended to include the ATS activity of a broker-dealer that merely acts as a conduit between trading counterparties to facilitate ATS activity. Thus, we believe that the Commission should revise the Proposed Rules to clarify that a Matched Principal ATS should count the transaction volume it effects in this capacity only towards determining whether it is an SCI ATS. In addition, since a broker-dealer that operates an ATS is required to use a single, unique MPID to report all transactions executed on the ATS,[14] it should be relatively easy for the broker-dealer to separate this activity from its other trading activities.

Separately, we note that the Commission has proposed to limit the definition of ''SCI systems'' with respect to a broker-dealer that crosses a transaction activity threshold, and that Regulation SCI would apply to only those of such broker-dealer's SCI systems that relate to the trading of the securities that caused it to exceed the threshold.[15] As the Commission noted, because a broker-dealer may engage in many lines of business, the application of Regulation SCI should be limited to the activity that raises the concerns that it is meant to address. If a broker-dealer uses other distinct systems to support trading activity in other securities and this activity does not cause it to cross an SCI transaction activity threshold, then the unavailability of these systems is not likely to impact the maintenance of fair and orderly markets.

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[14] See FINRA Rule 6720(c)(1).

[15] Under the Proposed Rules, the definition of the term "SCI systems" currently set forth in Rule 1000 would be revised to add the language underlined below: "SCI systems means all computer, network, electronic, technical, automated, or similar systems of, or operated by or on behalf of, an SCI entity that, with respect to securities, directly support trading, clearance and settlement, order routing, market data, market regulation, or market surveillance; provided, however, that with respect to an SCI broker-dealer that satisfies only the requirements of paragraph (2) of the definition of ''SCI broker-dealer'' (e.g., the volume threshold requirement), such systems shall include only those systems with respect to the type of securities for which an SCI broker-dealer satisfies the requirements of paragraph (2) of the definition."

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The reasoning set forth above also applies to a broker-dealer that sponsors a Matched Principal ATS. In this regard, a Matched Principal ATS may utilize separate trading systems to engage in unrelated trading activity that does not cross an SCI transaction activity threshold. Because the unavailability of these systems would not have widespread implications, we believe that the limitation set forth in the proposed definition of "SCI systems" should apply to ATSs as well. Otherwise, the Proposed Rules would appear to disadvantage a broker-dealer that sponsors an ATS relative to one that does not, even if they both have similar risk profiles.

B. Application of SCI Volume Threshold to Disclosed RFQ Trading Protocols

If the Commission determines to apply Regulation SCI to Fixed Income ATSs, we respectfully request that the Commission exclude transactions effected under a disclosed RFQ trading protocol against any applicable Regulation SCI volume threshold requirement. Disclosed RFQ involves connecting clients directly to dealers on a fully disclosed basis for the purposes of requesting and receiving executions, and thus is functionally equivalent to the order routing functionality that is currently excluded from consideration in determining whether an organization is an "exchange" under SEC Rule 3b-16. Accordingly, we believe that, as a matter of regulatory parity, an ATS that facilitates disclosed RFQ transactions should not be required to count these transactions towards any volume threshold requirements that may otherwise apply to it under Regulation SCI.[16]

C. Third Party Oversight Requirements

Proposed Rule 1001(a)(2)(ix) would require each SCI entity to have a program to manage and oversee third-party providers that provide functionality, support, or service for its SCI systems, including "a risk-based assessment of each third-party provider's criticality to the SCI entity and analysis of key dependencies if the third-party provider's functionality, support or service were to become unavailable or materially impaired." By contrast, proposed Rule 1001(a)(2)(v) would require an SCI entity to have business continuity plans in place that address the unavailability of such providers where such unavailability would have a material impact on any of its critical SCI systems. We believe that this latter requirement is more than sufficient to address any concerns the Commission may have relating to an SCI entity's ability to ensure continuity of service, and that the more expansive requirements set forth in Proposed Regulation 1001(a)(2)(ix) would not assist an SCI entity in addressing these concerns in any meaningful way. Accordingly, we

[16] Our position on this matter is consistent with the treatment of a platform that facilitates these transactions as operating in a technology vendor capacity (rather than in a broker-dealer capacity) under the Consolidated Audit Trail rules. In this regard, Section 3.4.1 of the CAT Reporting Technical Specifications for Industry Members (April 11, 2023) generally provides that the parties to disclosed RFQ transactions, rather than the platform on which these transactions are effected, are responsible for reporting these transactions to the Consolidated Audit Trail. See 04.20.2023_CAT_Reporting_Technical_Specifications_for_Industry_Members_v4.0.0r19_CLEAN.pdf (catnmsplan.com).

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recommend that the Commission revise Proposed Regulation 1001(a)(2)(ix) by deleting the language quoted above.

In addition, Proposed Rule 1001(a)(2)(ix) also provides that an SCI entity's policies and procedures must include a program to manage and oversee third party providers that, **directly or indirectly,** provide functionality, support, or service for its SCI systems. Although it is not clear, this language appears to require SCI entities to manage and oversee "fourth party" service providers with whom they have no relationship (i.e., those who indirectly provide functionality, support, or service). In order to achieve this result, SCI entities would likely need to rely on their third-party vendors to manage and oversee these fourth parties. Because it is unclear whether these third-party vendors would be willing to do so, this requirement could have a negative impact on SCI entities by narrowing the pool of third-party vendors available to them. Accordingly, we recommend that the Commission revise Proposed Regulation 1001(a)(2)(ix) so that it does not require an SCI entity to oversee and manage its indirect service providers.

D. Elimination of materiality test for systems intrusions

Rule 1000 of Regulation SCI currently defines a "systems intrusion" as any unauthorized entry into the SCI systems or indirect SCI systems of an SCI entity. Under the Proposed Rules, this definition would be expanded to include (i) any cybersecurity event that disrupts or significantly degrades the normal operation of an SCI system, such as denial of service attacks and (ii) any significant attempted (but unsuccessful) unauthorized entry into the SCI systems or indirect SCI systems of an SCI entity.

In general, when a systems intrusion occurs, an SCI entity must take corrective action, immediately notify the SEC, maintain certain records with respect to the event and promptly disseminate information about the event to its members or participants.[17] While Regulation SCI currently permits an SCI entity to report de minimis systems intrusions on a quarterly basis, the Proposed Rules would eliminate this ability and thus require all systems intrusions to be reported to the SEC immediately.

In our view, the Proposed Rules would impose serious burdens on SCI entities by requiring the reporting of multiple immaterial events, especially in light of the fact that this would include the reporting of unsuccessful attempts to enter the direct or indirect SCI systems of an SCI entity. It also would require responsible SCI entity personnel to turn their attention from more important tasks and expend considerable time and effort in reporting relatively minor events that have no meaningful impact on the operational capability of an SCI entity or on its ability to satisfy its regulatory obligations. Because this aspect of its proposal would impose significant costs on SCI

[17] However, under the Proposed Rules, unsuccessful attempts at unauthorized entry would only be required to be reported to the SEC but not to members or participants.

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entities without providing clear corresponding benefits, we believe that the Commission should continue to permit SCI entities to report de minimis systems intrusions on a quarterly basis.

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MarketAxess appreciates the opportunity to comment on the Proposed Rules. We would be happy to discuss our comments with the Commission or its staff. If you have any comments or questions concerning this letter, please feel free to contact us.

Sincerely,

Scott Pintoff

General Counsel, MarketAxess