



Bloomberg L.P.

731 Lexington Ave  
New York, NY 10022

Tel +1 212 318 2000  
bloomberg.com

March 1, 2021

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

Submitted via email: rule-comments@sec.gov

**Re: Regulation ATS for ATSS that Trade U.S. Government Securities, NMS Stock, and Other Securities; Regulation SCI for ATSS that Trade U.S. Treasury Securities and Agency Securities; and a Concept Release for Electronic Corporate Bond and Municipal Securities Markets (Release No. 34-90019; File No. S7-12-20)**

Dear Ms. Countryman:

Bloomberg L.P.<sup>1</sup> is grateful for the opportunity to provide the Securities and Exchange Commission (“SEC” or “Commission”) with our comments regarding the above-referenced proposed rule change (“Proposal”).

### **I. Executive Summary.**

The Securities and Exchange Commission has issued a request for comment on proposed amendments to Regulation ATS under the Securities Exchange Act of 1934 (“Exchange Act”) and a concept release on the regulatory framework for electronic platforms that trade corporate debt and municipal securities.

The Commission is requesting comment on six proposed amendments to Regulation ATS that would: (1) eliminate the exemption from compliance with Regulation ATS for alternative trading systems (“ATSS”) that limits its securities activities to government securities or repurchase and reverse repurchase agreements on government securities, and registers as a broker-dealer or is a bank; (2) require the filing of public Form ATS-G, which would require a Government Securities ATS to disclose information about its manner of operations and the ATS-related activities of the

---

<sup>1</sup> Bloomberg – the global business, financial information, and news leader – increases access to market data by connecting market participants of all stripes to a dynamic source of information, people, and ideas. The company’s strength – quickly and accurately delivering data, news, and analytics through innovative technology – is at the core of the Bloomberg Terminal. The Terminal provides financial market information, data, news, and analytics to banks, broker-dealers, institutional investors, governmental bodies, and other business and financial professionals worldwide.

registered broker-dealer or government securities broker or government securities dealer that operates the ATS and its affiliates; (3) require public posting of certain Form ATS-G filings and to provide a process for the Commission to review Form ATS-G filings and, after notice and opportunity for hearing, declare Form ATS-G filings ineffective; (4) apply the fair access rule under Rule 301(b)(5) of Regulation ATS to Government Securities ATSS that meet certain volume thresholds in U.S. Treasury Securities or in a debt security issued or guaranteed by a U.S. executive agency, or government-sponsored enterprise (“Agency Securities”); (5) modernize Regulation ATS, Form ATS, Form ATS-N, and Form ATS-R; and (6) apply Regulation Systems Compliance and Integrity (“Regulation SCI”) to ATSS that meet certain volume thresholds in U.S. Treasury Securities or Agency Securities.

Although the bulk of our comments concentrate on the regulatory framework for electronic platforms that trade corporate debt, we provide some feedback on the proposed changes to Regulation ATS that would eliminate the current exemption for U.S. Treasury and Agency Securities, and municipal securities. Our comments include:

1. Although the terms “electronic platform” and “electronic trading platform” are used interchangeably in the concept release, they are undefined term(s). Often electronic trading is conflated with the electronification of trading workflows. Table 1 in our comments describes that the threshold of electronic trading is where methods of electronification - directed discretionary trade messaging and order routing – crossover into rules-based, non-discretionary algorithmic routing, pricing and strategies and the formation of market places. The electronic trading threshold is where trader’s surrender discretion to automation and methods go from discretionary to brokerage and ultimately (central limit) order books, call auctions and crossing on ATSS. Therefore, an electronic trading platform is where communication and the commitment of parties to a transaction both occur on the same software platform.
2. We disagree with the assertion that the regulatory framework needs to be changed in order to define electronic trading and gather data so that market participants can understand where they can find liquidity. The equity market had similar data quality and reporting issues that FINRA solved with their ATS Transparency reporting initiative. That initiative evolved in successive iterations into OTC (ATS & Non-ATS) Transparency reporting. FINRA appears to be taking a similar approach to collect data that would provide insight into the market structure without a regulatory overhaul with their December 23, 2020 request for comment on a proposal of “Enhancements to TRACE Reporting for U.S. Treasury Securities” (Member notice 20-43 at <https://www.finra.org/rules-guidance/notices/20-43>).

Although FINRA currently is contemplating that the proposal would apply only to TRACE reporting of transactions in U.S. Treasury securities, they are in the process of querying their membership whether the proposal should be considered for other types of TRACE-eligible securities, such as corporate bonds. This initiative should be prioritized in order to conduct a data-driven conversation about market structure.

3. The fixed income market consists mainly of non-standard, small issues that are rarely traded and generally illiquid. The current regulatory framework under Rule 3b-16 strikes the right balance in creating a flexible and highly supervised regulatory framework that enables investors to discover liquidity in liquid and, more importantly, less-liquid securities. Rule 3b-16 sets out clear activity-based tests and enables the SEC to supervise and create conditions for competition to solve liquidity problems.
4. The Commission correctly observes that the dramatic changes in technology brought innovative electrified workflows and other non-ATS trading methods that enable market participants to find the liquidity they need. The lesson learned in the evolution to the NMS equity market is that a one-size-fit-all approach has created significant challenges to discovering liquidity in less-liquid small and micro-cap stocks. Traditional fixed income electrified workflows and methods are now helping liquidity seekers discover OTC liquidity in less-liquid NMS stocks, ETFs and options. The U.S. Treasury Report: A Financial System That Creates Economic Opportunities (“Treasury Capital Markets Report”) explained that liquidity in the corporate bond market is a mixed story (<https://www.treasury.gov/press-center/press-releases/documents/a-financial-system-capital-markets-final-final.pdf>).

The market is highly supervised. The changes contemplated to Rule 3b-16 could end up raising costs for new financial technology (FINTECH) entrants (liquidity solutions) to enter, stifle innovation and damage the current ability of market participants to locate liquidity in all illiquid security markets.

5. Market structures have developed to efficiently discover liquidity and trade liquid and illiquid instruments (See Table 1, Section III, Responses to the Concept Release, Introduction). Figure 1 depicts a highly resilient infrastructure that passed the COVID-19 trials with flying colors (see Section III, Responses to the Concept Release, Introduction). Figure 2 shows that along the continuum of illiquid to liquid securities, manual to varying degrees of automated methods have emerged amid three independent and distinct activities (1) workflow and directed communication

network technology (electronification), (2) discretionary brokerage and (3) non-discretionary brokerage all of which enable market participants to find the liquidity that they need to efficiently implement and execute their investment strategies (see Section III, Responses to the Concept Release, Introduction). The entire eco-system is highly supervised.

## **II. Responses in the Request for Comment on Regulation ATS.**

Question 6. Should the Commission amend Regulation ATS to eliminate the exemption from compliance with Regulation ATS under Rule 301(a)(4)(ii)(A) for all Currently Exempted Government Securities ATS, including those operated by banks?

If the Commission believes that the proposed Form ATS-G's public disclosures would help market participants "select the best trading venue based on their needs" by providing important information "that would help them better understand these operational facets" (Proposed rule at 84), then the Commission should consider, at a minimum, requiring bank operated electronic trading platforms provide greater disclosure on the operations by filing and making a Form ATS-G available. The Federal Reserve has proposed to collect transaction data from certain banking institutions through FINRA's TRACE system, so ATS disclosures would be a logical step in providing investors with greater transparency (<https://www.federalreserve.gov/boarddocs/press/foiadocs/2021/20210121/foia20210121.pdf>).

Question 13. Should the Commission require Currently Exempted Government Securities ATSs to comply with all of the requirements of Regulation ATS applicable to all ATSs that are currently required to comply with Regulation ATS? If not, which requirements should a Currently Exempted Government Securities ATS not be required to comply with and why?

All non-equity ATSs are undergoing tremendous innovation and change. The Commission should consider adopting a slightly different two- threshold test before lifting a Regulation ATS exemption and subjecting a non-equity ATS to fair access and SCI ATS requirements.

Rule 304(a)(1)(i) requires all ATSs to file an initial "Form ATS" with the Commission. This should not change. The first threshold – whether to lift a Regulation ATS exemption or not - should be based on whether ATS-trading is "developing" or is established as a "significant" liquidity channel in the asset class' market structure.

“Significant” can be defined with an objective data-driven measure. For example, ATSS as a liquidity channel could be considered significant if total ATS par value traded in the asset class, for four months over the prior six months, averaged at least 30% of total par value trade in the asset class. The Commission may recognize 30% as the threshold for “significant” threshold as equity-NMS ATSS were matching about 30% of the total share volume and 40% of total dollar volume in NASDAQ-listed securities when Regulation ATS was implemented. (see SEC Division of Market Regulation, “Special Study: Electronic Communications Networks and After-Hours Trading” at <https://www.sec.gov/news/studies/ecnafter.htm>). When ATSS become a significant liquidity channel, then the Commission should make all Form ATSS in that asset class transparent.

The second test to determine if a specific ATS should be subject to fair access and SCI ATS requirements depends on whether the ATS itself is a “significant” source of liquidity. An objective data-driven measure to determine whether an ATS represents a significant source of liquidity could be, for example, if its par value traded in the asset class, for four months over the prior six months, averaged at least 10% of par value traded in the asset class. This is an initial threshold that can be lowered in a similar manner to how the Commission lowered the threshold in NMS stock trading. 10% is an appropriate level for developing market structures.

U.S. Government securities as an asset class are a special case because the market is bifurcated – dealer-to-customer (D2C) and dealer-to-dealer (D2D) are linked but operate separately. The bifurcation, as the Treasury Capital Markets report observes, is due to some extent to structural issues in clearing.

In addition to the dealer and customer bifurcation, on-the-run securities are liquid trading on central limit order books. Off-the-run securities are less liquid and tend to trade using other methods. The Commission may apply the ATS thresholds to securities that are “likely” to trade on an ATS – the on-the-run securities. FINRA’s aggregated weekly data report currently segments the data into on-the-run/off-the-run and D2D/D2C (<https://www.finra.org/filing-reporting/trace/data/trace-treasury-aggregates>).

**Question 15.** Should the proposed five percent fair access threshold for U.S. Treasury Securities be applied to all types of U.S. Treasury Securities or only to a subset(s) of U.S. Treasury Securities? For example, should the five percent fair access threshold be applied to transaction volume in only on-the-run U.S. Treasury Securities? Should the five percent fair access threshold be applied to all Agency Securities or only to a subset(s) of Agency Securities?

Please see response to question 13.

Additionally, currently the fair access calculation threshold is based on the “average *daily* volume threshold for a category of securities” (Proposal at 26). It is the ATS’s obligation to monitor their activity and report when they have crossed the threshold and are obligated to offer fair access. However, FINRA publishes segmented on-the-run/off-the-run and D2D and D2C TRACE volume data on an aggregated *weekly* basis, so the proposal would need to be amended to the “average *weekly par value traded* threshold for a category of securities during at least four of the preceding six calendar months” (<https://www.finra.org/filing-reporting/trace/data/trace-treasury-aggregates/about>).

We support FINRA providing the same aggregated trading data reports but on an end-of-day daily basis.

Question 16. Should the proposed five percent fair access threshold for U.S. Treasury Securities be set higher or lower than five percent? If so, what should that percentage threshold be? Should there be no threshold? Please support your views. Is the five percent threshold an appropriate threshold to capture ATSS that are significant markets for trading in U.S. Treasury Securities or Agency Securities? Would the five percent threshold capture ATSS that are not significant markets for U.S. Treasury Securities and Agency Securities? If there should be a percent threshold for a subset of U.S. Treasury Securities, for example on-the-run U.S. Treasury Securities or off-the-run U.S. Treasury Securities, what should that threshold be?

With developing market structures, the ATS liquidity channel should first prove to be significant – in response to question 13, we proposed a 30% threshold.

Once the ATS liquidity channel proves to be significant, an ATS-specific threshold should apply for fair access. Generally, in our experience, most market participants view 10% as the market share threshold where a specific ATS’s liquidity is significant and needs to be accessible for risk management, best execution, and market making profitability purposes.

Question 19. If the average weekly dollar volumes were to include transactions for U.S Treasury Securities by non-FINRA members, which currently are not reported to, or collected by, the SRO that makes public average weekly dollar volume statistics, should the fair access threshold change? If so, what should be the appropriate threshold?

We support FINRA publishing aggregated U.S. Treasury on-the-run and off-the-run volume data segmented by D2D and D2C on a daily basis. However, the same thresholds described in response to question 13 would continue to apply if only weekly aggregated data is available.

With the Federal Reserve proposing to have certain banking institutions report to TRACE (see response to question 6), all U.S. Treasury transactions will be reported to FINRA, making TRACE a real-time trade reporting facility. Consultation on real-time TRACE trade data dissemination should begin soon.

FINRA is using TRACE to collect more and more data for surveillance purposes. Not all of the data needs to be collected in real-time. The SEC and FINRA should also consider separating TRACE into two reporting vehicles - a real-time (last) trade reporting function (i.e., price, size, time, capacity, special consideration flags, etc.) as a feeder for real-time trade transparency dissemination and an end-of-day transaction data reporting function for the surveillance and market structure data collection (i.e., trading desk identifier, clearing arrangement indicator, fee reporting indicator, trading method, etc.)

Question 45. Are there any other requirements that should apply to making public a Form ATS-G report filed by a Government Securities ATS? Please support your arguments, and if so, please list and explain such procedures in detail.

Applying Rule 304(b)(3), “Each NMS Stock ATS shall make public via posting on its website a direct URL hyperlink to the Commission's website...” to all ATS is sufficient.

Question 49. A Legal Entity Identifier (“LEI”) is a 20-character reference code that uniquely identifies legally distinct entities that engage in financial transactions and is used by numerous domestic and international regulatory regimes. Although several existing ATS broker-dealer operators currently have an LEI, not all broker-dealers have an LEI. An LEI can be obtained for a \$65 initial cost and a \$50 per year renewal cost. Should the Commission require a Government Securities ATS to disclose the LEI of its broker-dealer operator, in addition to its CRD Number and the MPID for the Government Securities ATS, on Form ATS-G?

FINRA assigns identification numbers to all broker-dealers. When non-FINRA members (banks) are required to report to TRACE, FINRA will presumably assign an identification number to them.

Although an LEI requirement would add a level of specificity to the affiliate disclosure of ATS-related activities of the broker-dealer operator and its affiliates through the reference to an international standard, if LEI isn't going to replace FINRA assigned identification numbers, then it isn't clear what the use case is to ask brokers to attain another ID number.

Question 63. Are there any critical services or functionalities (e.g., matching engine, market data) that, if provided by a third party, should be required to be described in a higher level of detail than the proposed “summary” level? If so, which services and functionalities?

We believe that the disclosure of outsourced technology provider relationships is appropriate to the SEC and FINRA to determine that the regulated entity, the broker-dealer operator, is monitoring its third-party service provider(s).

Question 64. Should the Commission require the disclosure of the information in Part II of Form ATS-G? If so, what level of detail should be disclosed?

NMS Stock ATS subscribers believe that they have the right to know if (1) their orders are interacting with an affiliate of the Broker ATS operator's principal liquidity; (2) if there are any formal or informal arrangements with any of the affiliated business to provide orders or trading interest; (3) if there is any information leakage of orders inside the ATS to another subscriber or affiliate of the broker ATS operator; and (4) segmentation options (for example what, if any, options are available for ATS subscribers to opt-out from interacting with certain types of orders and/or trading interest). Presumably, as the fixed income market structure continues to develop, these types of segmentation options may occur in U.S. Government security ATSs and should be disclosed.

Question 87. What are commenters' views on the relationship between markets for government securities and Related Markets and how investors may use these markets together with a Government Securities ATS to achieve their trading objectives?

The Joint Staff Report on the U.S. Treasury Market on October 15, 2014 recognizes that the markets are connected through cross-market "automated trading strategies that involve a nearly instantaneous response to common trading signals or that seek to arbitrage short-lived opportunities across related interest-rate products" ([https://www.treasury.gov/press-center/press-releases/Documents/Joint\\_Staff\\_Report\\_Treasury\\_10-15-2014.pdf](https://www.treasury.gov/press-center/press-releases/Documents/Joint_Staff_Report_Treasury_10-15-2014.pdf)). Linkages between the Treasury ATSs and the related markets are similar to those "witnessed in other markets ...for example between equity index futures and the cash equity market."

The report concludes that "...the U.S. Treasury market comprises the secondary market trading of cash Treasury securities as well as the futures and options on Treasury securities." Analysis of the data concluded that "[p]rices are tightly linked across these markets, and linked as well to activity in related markets such as short-term U.S. interest rate futures and U.S. interest rate swaps."



### **III. Responses to the Concept Release on Electronic Corporate Bond and Municipal Securities Market.**

#### **Introduction**

When electronic trading is defined it becomes clear that the SEC and FINRA currently have the right regulatory framework, structure and balance in place (see Figure 1).

Anindya Basu of Citi explained in an FT Alphaville Blog, “Most Bonds Don’t Trade” that:

“... on average, only 18% of the entire corporate bond universe (by CUSIP) traded on any given day. For issues that traded 5 times or more on a given day, the percentage was in the single digits at about 8%.... Furthermore, most of these CUSIPs trade in small size – more than 75% of the total volume traded during this period can be attributed to only 15% of the CUSIPs.

The daily churn (or turnover) in bonds is also fairly low (less than 1%) when expressed as a percentage of outstanding notional of the traded bonds ... For IG bonds, the average daily churn is 0.35%, for HY it is somewhat higher at 0.56%. The graphs also show that the churn can vary between as low as 0.10% to as high as 0.70%, all of which is well below a 1% threshold. Given that most bonds do not even trade on any given day, the daily churn expressed as a percentage of the total bond universe is another order of magnitude lower”

(<https://www.ft.com/content/3175772a-7ea0-3b61-ae53-063459e78c42>).

Perhaps, more than any other asset class, fixed income and specifically corporate bonds have a heterogeneous structure that efficiently trades liquid and, more importantly, less-liquid securities. Electronification and digitization of the workflows, including directed communication network technology, enable the transfer of data and communication that deliver insights and directed orders to discretionary brokerage and certain non-discretionary brokerage activities that enable market participants to discover the liquidity that they need to efficiently implement and execute their investment strategies (Figure 1). The entire eco-system is highly supervised.

#### **Electronification and Electronic Trading**

Electronification is digitizing of manual workflows and discretionary interactions and putting them on an electronic highway (Figure 1). Electronification provides efficiencies such as trade capture and new data sources such as timestamps for surveillance. The Commission and FINRA have long recognized that the electronification of manual

methods including data organization, insights from data analytics to make sense of the markets, straight-through processing, trade messaging (discretionary directed order routing) and order negotiation messaging are all examples of workflow electrification that, as the Treasury Capital Markets report expressed “create operational efficiencies, but they do not fundamentally change the nature of corporate bond liquidity because they rely on the same dealers and customers interacting through a different medium.” Electrification introduces new digitized workflows not new intermediaries.

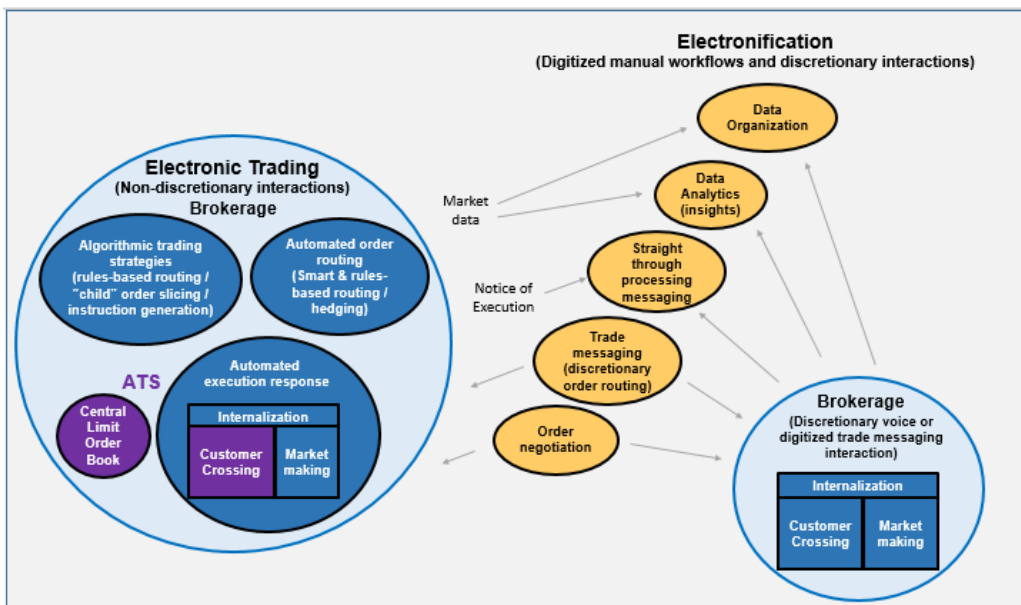


Figure 1.

The current regulatory framework enables financial technology (FINTECH) firms to innovate and compete fiercely. As markets evolve, sometimes some technology providers will opt-to cross the threshold to perform brokerage activities. Others may choose to remain technology providers. The regulatory framework is flexible, allowing markets to develop organically at their own pace and developing solutions for their own set of circumstances. For example, in the non-standardized somewhat illiquid fixed income market, electrified workflows assist in the efficient trading of less-liquid fixed income instruments and liquid security block order sizes efficiently. As the Treasury Capital Market’s report notes, this is in contrast to the equity markets where “... the current “one-size-fits-all” market structure is not working well for smaller companies that are currently experiencing *limited liquidity* for their shares” (emphasis added). NMS stocks and ETFs are now beginning to borrow from established methods in fixed income, such as RFQ, to bridge these liquidity gaps.

Table 1 is a bottom-up level of automation view of liquidity seeking methods. It is tailored to the fixed income market. Figure 2 shows that methods diverge depending upon security liquidity. Fixed income has focused on electronification because of the (less liquid) nature of fixed income liquidity. The methods in Table 1 are similar to the equity market that began with the changes in 1996 to the order handling rules and the 1999 introduction to Regulation ATS. Table 1 shows that the regulatory thresholds of non-brokerage activities, and discretionary and non-discretionary brokerage are clear – and customer agreements reflect these activities and thresholds. In July 2020, SEC Staff provided new guidance for Footnote 74 to the July 30, 2013 Exchange Act Release No. 34-70073 recognizing that there are different types (categorizations) of broker-dealers – such as broker-dealers that offer non-brokerage (technology-only) activities - and that it is appropriate to require different levels of capital, reporting and supervision (<https://www.sec.gov/rules/final/2013/34-70073.pdf>).

The basis of the over the counter (OTC) market was the telephone. Basic conversations with manual workflows were digitized with chat and voice-processing – digitizing parts of the voice trading process for quicker trade confirmation to reduce communication (trading) errors and facilitate straight-through processing for more efficient settlement, clearing and risk management.

|                            |   | Method  | Activity Type                   |                     | Operator                               | Regulatory Framework   |   |
|----------------------------|---|---|---------------------------------|---------------------|--|--|---|
| High                       | Electronic Trading                          | Direct Market Access (DMA)  | Auction                         | Electronic Trading  | Trading Technology                     | ATS (Broker-Dealer)  | Executing broker is supervised. If the auction algorithm is developed by a 3rd party, broker has obligation to "supervise" the technology provider. Non-manual (automated) crossing may be subject to Regulation ATS and potentially SCI ATS. |
|                            |   |   | Central Limit Order Book (CLOB) | Electronic Trading  | Trading Technology                     | ATS (Broker-Dealer)  |   |
|                            |   |   | Crossing (non-manual)           | Electronic Trading  | Trading Technology                     | Broker-Dealer or ATS   |   |
|                            | Algorithmic Strategy                        | Auto-hedge  | Electronic Trading              | Trading Technology  | Broker-Dealer responsible for the algo | Broker operating the algorithm is supervised. If the broker algorithm is developed by a 3rd party, broker has obligation to "supervise" the technology provider. |   |
|                            |   | Non-discretionary order routing tactics and execution result strategies (e.g., rules-based order routing and order slicing) | Electronic Trading              | Trading Technology  | Broker-Dealer responsible for the algo |  |   |
|                            |   | Portfolio Pricing Algo (multi-security single price)  | Electronic Trading              | Trading Technology  | Broker-Dealer                          |  | Broker receiving directed discretionary request(s) and reply with an algorithmically generated price(s) is supervised. Broker has obligation to "supervise" the technology provider for business continuity purposes.                         |
|                            |   | Auto single security inquiry-response pricing   | Electronic Trading              | Trading Technology  | Broker-Dealer                          |  |   |
| Workflow Electronification | Discretionary Trade Messaging Order Routing | Single order RFQ - Undisclosed  | Electronification               | Workflow technology | Broker-Dealer                          | All brokers (intermediary and destination) receiving the directed discretionary order are supervised.  |   |
|                            |   | Portfolio trade order routing ticket (multi-security single price)  | Electronification               | Workflow technology | FINTECH                                |  |   |
|                            |   | Multi security disclosed Bids/Offer Wanted (RFQ)  | Electronification               | Workflow technology | FINTECH                                | Broker receiving the directed request(s) is supervised. Broker has obligation to "supervise" the technology provider for business continuity purposes.           |   |
|                            |   | Disclosed single security directed order routing response to Streaming Price  | Electronification               | Workflow technology | FINTECH                                |  |   |
|                            |   | Disclosed single security RFQ and directed order routing  | Electronification               | Workflow technology | FINTECH                                |  |   |
|                            |   | Single dealer order routing (ticket)  | Electronification               | Workflow technology | FINTECH                                |  |   |
| Manual                     | Voice                                       | Voice processed trade confirmation and straight through processing  | Electronification               | Workflow technology | FINTECH                                | Broker receiving the order is supervised. Broker has obligation to "supervise" the technology provider for business continuity purposes.                         |   |
|                            |   | Chat  | Electronification               | Workflow technology | FINTECH / Telcom                       |  |   |
|                            |   | Phone   | Manual                          | --                  | Telcom                                 |  |   |

Table 1. Methods of workflow electronification and electronic trading

Electronic communications developed from single dealer order routing. The “three quote rule” – institutional investors placing three dealers in competition by seeking three quotes – was recognized as one of the tenants of best execution. To assist in seeking best prices in competition, electronic request for quote (RFQ) emerged. FINTECH companies brought dealers and their customers together with (at the time) unique, innovative proprietary digital communication protocols and associated workflows through data organization. In more liquid securities, digitization enabled indicative pre-trade data to be organized to assist in dealer selection. Soon, communication protocols enabled multiple-security trade messaging inquiries.

Electronification of workflows is not electronic trading and FINTECHs were providing directed communications rather than brokerage services. The technology providers were not intermediaries or a part of the trade. Technology providers brought electronification – efficiency, risk reduction and digitized audit trails for compliance and relationship

management to manual workflows. Is it really electronic trading when picking up a phone is replaced with an electronic communication message performing the same substantive activity? As the Treasury Capital Markets report observes, in the electronification of workflows, technology providers (FINTECHs) do not fundamentally alter the relationship or change the nature of liquidity between a liquidity provider and a liquidity seeker. Directed discretionary RFQ order routing in less-liquid NMS equities and ETFs is not considered electronic trading and should not be considered electronic trading in other asset classes either. The electronification of workflows, emergence of technology solutions such as execution management systems and the greater reliance on FIX communications infrastructure, combined with buy side cost pressures is resulting in a consolidation of trading desks. Methods, described in Table 1 are being replicated in other asset classes. Creating asset class security-specific regulatory frameworks would introduce confusion.

In an effort to reduce potential adverse market impact from disclosing identities and widen the pool of liquidity providers to non-brokers willing to fill that role, some technology providers began to leverage their communication network and change that relationship, crossing over the brokerage threshold by becoming intermediaries and a part of the trade by offering undisclosed request for quote.

Electronic trading begins at the stage after electronification - where trading technology such as auto-pricing, auto-hedging and other automated non-discretionary brokerage decisions are clearly taking place. These activities firmly cross the broker-dealer threshold. The act of disseminating an auto-price to an inquiry and the auto-hedging are brokerage activities but brokers can outsource the development of the capabilities to a technology provider. A broker that relies on such outsourced (algorithmic) technology, as they do when using electronified workflow communication network order delivery protocol functionality, has obligations to monitor the technology. These algorithmic solutions developed as single security tactics and expanded to multi-security tactics in a manner to offer liquidity solutions to less-liquid instruments. For example, submitting multiple securities as a portfolio of liquid and less-liquid securities enables a liquidity provider to price the portfolio based on the characteristics of the unit and potentially offering better overall prices than trading each security individually (for example in a list).

Liquidity providers may rely on outsourced (algorithmic pricing) technology providers to offer this portfolio trading service. The algorithmic pricing activity on the submitted portfolio is an example of electronic trading. However, the delivery of the portfolio in a disclosed discretionary manner continues to be an example of an innovative electronified

workflow - independent from the algorithmic pricing activity - that brings dealers and their customers together to discover liquidity in less-liquid issues by combining them with more liquid issues. The investor continues to request prices by submitting directed requests to their broker(s) even though the pricing may be determined or supported by an algorithmic process. FINRA, in their desire to gather more data on electronic trading and provide more transparency into TRACE disseminated prices, proposed changes to TRACE reporting of portfolio trades (see FINRA request for comment, Regulatory Notice 20-24, September 15, 2020 at <https://www.finra.org/sites/default/files/2020-07/Regulatory-Notice-20-24.pdf>).

From this point, there is a divergence in trading methods driven largely by liquidity considerations. Larger issues are more liquid and therefore more conducive to trading electronically. As Table 1 shows, technology providers can opt to engage in electronic trading in order to court traders who want to surrender their discretion to automation. Methods then go from discretionary to brokerage and ultimately (central limit) order books, call auctions and crossing on ATSs.

Along the continuum of illiquid and liquid securities and methods that are manual to varying degrees of automation lies workflow electronification, brokerage and ATS activities (Figure 2). Figure 2 shows how technology provider liquidity seeking electronified workflows interact with liquidity provider electronic trading methods and the clarity of the activity thresholds that constitute brokerage and ATS activity.

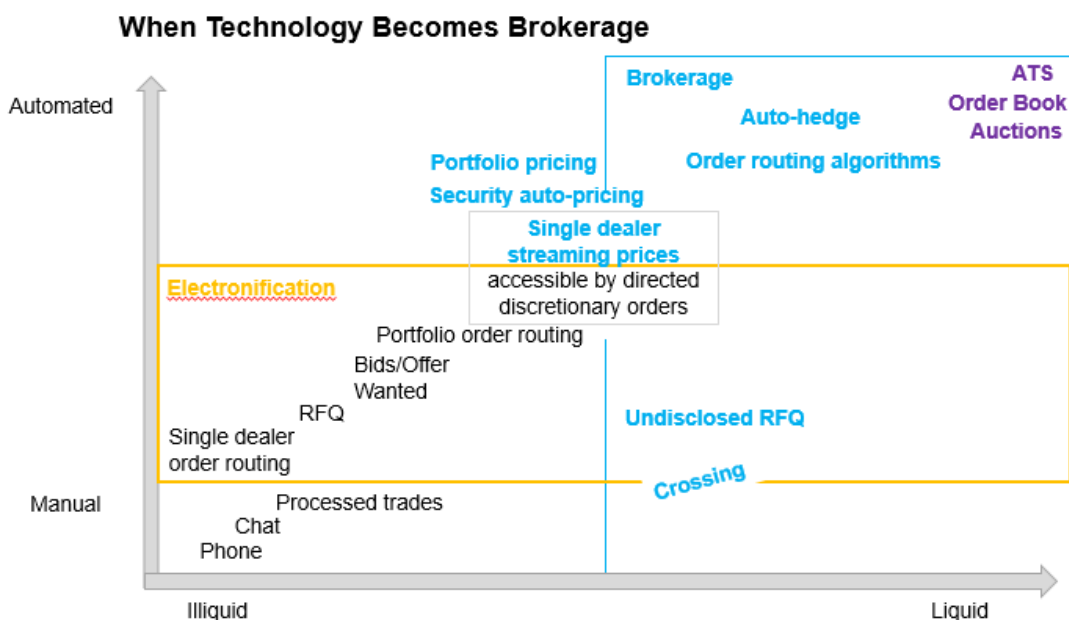


Figure 2.

## **Transparency**

We support FINRA's efforts in their September 15, 2020 Regulatory Notice 20-24, and December 23, 2020 Regulatory Notice 20-43 request for comment on changes to TRACE to consider changes to reporting rules to gather data to provide accurate market share statistics to help "the public to better understand the liquidity, market share and transaction cost trends across the wide variety of electronic trading venues currently in existence" (<https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-recommendation-definition-of-electronic-trading.pdf>). We do not believe that the regulatory framework needs to be changed to solve a reporting problem. We are supportive of FINRA's incremental approach but echo our comments in response to Question 19 in the Section II, Response to Comments on Regulation ATS, that as TRACE becomes a full corporate bond trade reporting facility, like equities reporting, special consideration should be given to separating real-time reporting requirements to facilitate trade transparency from end-of-day transaction (details) reporting for surveillance efforts.

## **Market Share Attribution**

"To better understand the liquidity," market share attribution should be from the liquidity seeker's perspective. Liquidity seekers want and need statistics to identify "where" liquidity is located. The operating principle to market share attribution should be that market share is based on the true execution activity (not give-up but the actual act of committing of a buyer and seller together). Executing brokers-dealers that either "own" an order or are "suppliers" of liquidity should be credited.

When considering market share attribution of trade messaging communication methods, such as disclosed-RFQ, Table 2 seeks to clarify appropriate market share attribution. Disclosed-RFQ market share should not be credited to an ATS just because the workflow has been registered with the ATS. Similarly, disclosed-RFQ market share should not be credited to either a FINTECH or broker-dealer operator of a communication messaging network. Trades associated with electrification methods, such as disclosed-RFQ, should be credited to the broker-dealer that "owned" the order or provided the liquidity, and was a party to the trade. Undisclosed-RFQ should be credited to the broker intermediary in the undisclosed-RFQ flow, and not the ATS.

Table 2. RFQ market share attribution

| Method           | Operator        | RFQ Destination | Market Share Credit | Comment  |
|------------------|-----------------|-----------------|---------------------|--|
| Disclosed RFQ    | FINTECH         | Broker-dealer B | Broker-dealer B     | FINTECH is the technology provider and not a party to the trade;<br>Broker-dealer B is the "owner" of the liquidity and a party to the trade.  |
| Disclosed RFQ    | Broker A's ATS  | Broker-dealer B | Broker-dealer B     | Broker-dealer B is the "owner" or provider of the liquidity and a party to the trade.  |
| Un-Disclosed RFQ | Broker-dealer A | Broker-dealer B | Broker-dealer A     | Although Broker-dealer B is the "owner" or provider of the liquidity, Broker-dealer A is the arranger/intermediary and a party to the trade.   |
| Un-Disclosed RFQ | Broker A's ATS  | Broker-dealer B | Broker-dealer A     | The interpretation of market share is "who can I go to get liquidity?"<br><br>It would be misleading to credit share to the ATS because it could be interpreted that the ATS has native liquidity when, in fact, Broker-dealer B is the "owner" or provider of the liquidity away from the ATS;<br><br>To avoid any confusion, Broker-dealer A should be credited with the share because they were the arranger/intermediary and a party to the trade. |

The principles in Table 2 provide a market share perspective from the liquidity seeker's point of view. Liquidity seekers want and need statistics to identify "who" they should be sending their orders to - who is actually willing to provide liquidity.



## Responses to Questions

**Question 146.** Given the technological developments in the fixed income electronic trading markets and electronic trading of fixed income securities, do commenters believe that the current regulatory framework for fixed income electronic trading platforms best promotes the growth of fair and efficient markets for investors? If not, what regulatory approach(es) would best address the needs of the market and market participants? Does the current regulatory structure for national securities exchanges, broker-dealers, and ATSs cover the full range of fixed income electronic trading platforms operating today? If not, please explain any gaps in the regulatory structure and to which platforms it does not apply.

As we explain on our Introduction and the “regulatory framework” in Table 1, the current regulatory structure is flexible to promote competition, enables innovation to discover liquidity in both liquid and less-liquid securities, makes appropriate distinctions between electronified workflows, brokerage, market-making and alternative trading. The activities are both highly and appropriately supervised across the eco-system.

It is important to note that the term “electronic trading platform” is an undefined term. Electronic trading is often conflated with the electronification of trading workflows, but there is a clear difference between the two (Figure 1). Electronic trade messaging communication networks are not a form of electronic trading. Rather, they are an example of electronification or digitization of workflows. An electronic trading platform, on the other hand, is where communication and the commitment of parties to a transaction both occur on the same software platform. An ATS is a form of an electronic trading platform. Electronic anonymous request for quote protocols, where a technology provider acts as a broker and become a party to the trade, is another form of an electronic trading platform. Electronic trading platforms may also contain a measure of non-discretionary activities which makes them regulated either as brokerage or ATS activities.

Electronic trade messaging communication networks are an example of electronification or digitization of workflows. The Treasury Capital Market report is a useful reference that makes similar distinctions. The report notes that trade messaging communicates order requests and instructions, such as request for quote, between counterparties which “create operational efficiencies, but they do not fundamentally change the nature of corporate bond liquidity because they rely on the same dealers and customers interacting through a different medium.” Communication networks that direct discretionary requests through electronic trade messaging protocols to facilitate execution are not a party to the transaction. These communications networks provide similar services that order and execution management systems, routing networks, and independent service vendors (ISVs) provide today.

We agree with the Treasury Capital Market report that regulators have struck the right balance with where direct supervision is required. It is inaccurate to suggest that the electronified fixed income workflows, such as directed discretionary order routing and directed discretionary trade messaging, are not supervised – they are. Similar to voice orders, the digitized messages are supervised when they are received by the broker/dealer. Brokers and dealers are supervised and are required to ensure that technology providers are able to support their business.

The FIMSAC July 16, 2018 Recommendation for the SEC to Review the Framework of the Oversight of Electronic Trading Platforms for Corporate and Municipal Bonds seems troubled by the “varying regulatory treatment to which credit and municipal bond trading platforms in the U.S. are subject based on differences in trading protocols or business models... For example, some platforms are regulated as alternative trading systems (ATSSs), some are regulated as broker-dealers, and other significant platforms operating the same or similar models are not regulated at all” (<https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-electronic-trading-platforms-recommendation.pdf>). Without any articulated basis, FIMSAC claims that “[t]hese distinctions in regulatory oversight complicate efforts to improve the efficiency and resiliency of the fixed income electronic trading markets.”

The period of COVID-19 volatility was an enormous clinical trial testing the infrastructure of fixed income electronified workflows and electronic trading. Fixed income infrastructure – data, information, execution and clearing – passed with flying colors. In October, 2020, the committee relayed “how well the market performed given the magnitude of stress” during the March 2020 COVID-19 induced volatility. The committee further noted the resiliency and efficiency of the fixed income market and how well the market structure responded to working in remote environments (Transcript of the October 5, 2020 meeting, page 48 at line 15 and page 67 at lines 21-22: <https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-100520-transcript.pdf>). This was particularly evident, in of all places, the secondary market for new issue corporate bonds. Analysis of FINRA’s TRACE corporate bond data shows that there was a surge, to record levels, during the pandemic in electronic (ATS) trading of new issues on the day they were priced after they were “free-to-trade.”

Focusing on new issues with an issue-size at least \$250 million (those new issues conducive to trade electronically), in Q2 2018 about 12% of new issues experienced a secondary market trade electronically on an ATS if the issue traded in the secondary market on the same day after it was priced and “free-to-trade.” During the COVID-19

trials, on the week-ending March 27, 2020, following the Federal Reserve's announcement of the Secondary Market Corporate Credit Facility (SMCCF), 73% of jumbo-sized (1bn+) new issues and 61% of all new issues (250mm+) traded electronically on an ATS, if they traded in the secondary market on the same day after they were priced and "free-to-trade." The percentage remained high through May, June and July 2020 with around 45% of all 250mm+ sized new issues and 60% of jumbo-sized new issues trading electronically on an ATS, if they traded in the secondary market on the same day after they were priced and "free-to-trade."

Why did the market fare so well? The regulatory structure has the right focus, and both the appropriate level of supervision and amount of flexibility which has enabled the markets and the market infrastructure to develop.

As we noted in our Introduction, FINRA is undertaking a transparency initiative similar to the OTC (ATS & Non-ATS) Transparency they implemented in the equity markets (<https://www.finra.org/filing-reporting/otc-transparency>). Through changes in reporting to TRACE, FINRA is seeking to gain data that could be published to help market participants locate the liquidity that they need. As we noted in our Introduction, attention needs to be taken on the appropriate assignment of market share "credit" such that attribution is given to the executing broker, dealer or ATS that "owned the order" or "supplied the liquidity" rather than crediting the give-up broker or a broker's ATS affiliate.

Question 147. Exchange Act Rule 3b-16(a) sets forth a functional test of whether a system meets the definition of an exchange. Specifically, Rule 3b-16(a) provides that an organization, association, or group of persons meets the Exchange Act definition of "exchange" 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. Is the Commission's approach under Exchange Act Rule 3b-16(a) appropriate for fixed income electronic trading platforms? If not, what elements of the definition of exchange under Rule 3b-16(a) do commenters believe that the Commission should consider changing and why? For example, should or should not the element of "orders" in Rule 3b-16(a) be included in the definition of exchange with regard to fixed income electronic trading platforms?

The Commission got it right with Rule 3b-16's use of the word "and" - "Brings together the orders for securities of multiple buyers and sellers". "And" is what provides the flexibility in the market structure rather than creating a one-size-fits-all approach. The question of whether it is appropriate to bring discretionary electronified workflows and trading methods, such as RFQ, into an exchange or ATS regulatory construct by

changing “and” to “or” (“brings together the orders for securities of multiple buyers or sellers.”) is a question to which we would emphatically answer “no”.

As we quoted Anindya Basu in our Introduction, the Treasury Capital Markets report also highlighted that the corporate bond market is non-standard consisting “of tens of thousands of distinct securities, as companies have issued bonds at different times, with different tenors, and in different structures.” And, because of the vast array of distinct securities, “Treasury believes that market making serves a critical function in financial markets.” In fact, as we noted in our Introduction, less-liquid ETFs and small/micro-cap NMS stocks, and the market for certain NMS equity options, are now finding liquidity through newly introduced RFQ trade messaging protocols. As shown in fixed income, these protocols help discover OTC liquidity when applied to less-liquid NMS stocks, ETFs and options.

A change in the definition or the wording of Exchange Act Rule 3b-16 would insert unnecessary intermediation between dealers and their customers and threaten to distort the market structure by creating a one-size-fits-all that is biased against the trading of less-liquid instruments damaging liquidity formation.

The Exchange Act appropriately segments order routing and market making activities from exchange activity. This was specifically noted in the Regulation of Exchanges and Alternative Trading Systems (17 CFR Parts 202, 240, 242 and 249 Release No. 34-40760; File No. S7-12-98 RIN 3235-AH41 at <https://www.sec.gov/rules/final/34-40760.txt>).

“The Commission proposed to exclude from proposed Rule 3b-16 those trading systems that merely route orders to an exchange or broker-dealer for execution... The Commission does not believe that these routing systems meet the two-part test in paragraph (a) of Rule 3b-16 because they do not bring together orders of multiple buyers *and* sellers. Instead, all orders entered into a routing system are sent to another execution facility. In addition, routing systems do not establish non-discretionary methods under which parties entering orders interact with each other.” Dealer systems were also excluded from Rule 3b-16. “System L allows a dealer to disseminate its proprietary quotations to its customers and permits customers to transmit orders to buy from or sell to that dealer at those quoted prices. System L is not included under Rule 3b-16 because it falls within the exclusion in paragraph (b)(2) of Rule 3b-16.”

The regulatory framework is not broken. There has been no demonstrated market structure failure to consider. The Commission got it right in the Regulation of Exchanges

and Alternative Trading Systems when they recognized that activities such as order routing and market maker systems were outside the Rule 3b-16 activities (17 CFR Parts 202, 240, 242 and 249 Release No. 34-40760; File No. S7-12-98 RIN 3235-AH41 at <https://www.sec.gov/rules/final/34-40760.txt>).

Question 148. Are there particular elements of the definition of exchange under Exchange Act Rule 3b-16(a) that should or should not be changed with respect to fixed income electronic trading platforms, or more specifically, the corporate debt markets or municipal debt markets? What are commenters' views on the potential consequences of expanding or limiting the definition of exchange under Rule 3b-16(a) with regard to these trading platforms or markets? For instance, what are commenters' views on how changing Rule 3b-16(a) could benefit or harm investors and the market participants that use fixed income electronic trading platforms? Should the Commission, rather than amending Rule 3b-16(a), issue guidance on the elements of Rule 3b-16(a) regarding considerations relevant to the definition of exchange in the context of a fixed income platform? If so, what elements of Rule 3b-16(a) should the Commission issue guidance on and why? For example, should the Commission issue guidance on what is considered an "order" under Rule 3b-16(a)? Given the technological changes in the securities industry since Regulation ATS was adopted in 1998, should the Commission revise, or provide additional, examples in Regulation ATS of systems that fall within or outside the definition of exchange under Rule 3b16?

There have been dramatic changes in technology since 1998. NMS stock markets trade liquid stocks well. However, the one-size-fits-all approach presents significant challenges in small and micro-cap stocks. Trading in small and micro-cap stocks have always been difficult, but Nasdaq in their Revitalize initiative to Improve the Trading Environment in Small and Medium Growth Companies and Investors explains that it has not gotten any better even with the technological changes (<https://www.nasdaq.com/articles/nasdaqs-proposal-improve-trading-environment-small-and-medium-growth-companies-and>). The equity market is beginning to borrow workflow electronification technology solutions such as RFQ methods with communication messaging networks to solve them.

As we note in response to question 13 in Section I, the U.S. Treasury market has developed to the point where ATSS are a significant source of liquidity for on-the-run U.S. Treasury securities. U.S. Treasury market ATS market share - in relation to the over-all market - is at a similar level (30%) that NMS equities ATS market share was in 1999 when Regulation ATS was adopted. The exemption gave Treasury market structure time to develop, with the liquid segment of on-the-run Treasury securities evolving along a similar path as NMS stocks, and maturing to a point where the data suggests that it may be appropriate to amend the exemption. The proposal also acknowledges that the less-liquid off-the-run securities continues to face challenges. Market participants in this less-

liquid segment, however, are able to find the liquidity they need through electrified workflows and other non-ATS trading methods.

All of this is possible because, as we note in response to question 147, Rule 3b-16 strikes the right balance. A change in the definition or the wording of Exchange Act Rule 3b-16 would insert unnecessary intermediation between dealers and their customers and threaten to distort the market structure by creating a one-size-fits-all that works for the trading of liquid instruments but damages liquidity formation in other less-liquid securities.

We believe that the Commission should have empirical data to inform regulatory and market structure changes. The approach in corporate bonds should be to solve data gathering and reporting problems to inform and demonstrate problems before making dramatic wholesale changes to regulatory structure based on commercially driven statements, inferences, anecdotes and supposition. Wholesale changes to the regulatory framework of the U.S. Treasury market was not needed for FINRA to obtain descriptive data on the U.S. Treasury market. The current regulatory structure works and is the envy of other securities markets.

Question 149. As noted above, fixed income electronic trading platforms offer a variety of different trading protocols and business models, and the FIMSAC expressed concern about varying regulatory treatment among these trading platforms.

It is easy in these discussions to lose sight of what regulation is supposed to do. Certainly, to protect investors, and to promote innovation and competition. But as the Treasury Capital Market's report explained, regulatory frameworks are also supposed to promote liquidity formation. "The U.S. capital markets are the most liquid in the world and a powerful force in promoting economic growth and investment. Liquidity is difficult to define precisely, and its characteristics vary by asset class. However, it generally relates to the ease, speed, and cost with which investors can buy or sell assets."

To promote competition and match supervision with the risk to investors, the SEC and FINRA have regulated based on the activity performed. Consistent with that approach, as we noted in our Introduction, the Staff issued new guidance to Footnote 74 to the July 30, 2013 to Exchange Act Release No. 34-70073 recognizing that there are different types (categorizations) of broker-dealers – such as broker-dealer that offer non-brokerage (technology-only) activities - and that it is appropriate to require different levels of capital, reporting and supervision (<https://www.sec.gov/rules/final/2013/34-70073.pdf>).

As we also note in our Introduction, technology suppliers and brokers are competing and innovating to bring forth new ways for liquidity seekers to find the liquidity they need. It is a misnomer to infer that somehow different regulatory treatment is an indication of a failure. The current regulatory framework promotes innovation and fierce competition with appropriate supervision for the efficient trading of generally illiquid securities. This structure has provided numerous companies relatively low costs to enter (and exit) the market place to develop new technologies that electronify workflows for efficient liquidity discovery and delivery of orders in liquid and less-liquid instruments. In fact, in other markets, such as equities, technology providers are beginning to deploy traditional fixed income technology solutions to promote market making and improve liquidity in less-liquid stocks and ETFs.

As Table 1 and Figures 1 and 2 show, RFQ is an example of workflow electrification. It consists of discretionary directed order communication network messaging. This not an ATS function. RFQs lack a non-discretionary commitment to trade. As we also note in our Introduction, special attention should be paid to market share credit. With respect to FIMSAC's stated concern, a technology provider that has chosen to become a broker performing non-brokerage activities such as RFQ electronified workflows and that also operates an ATS will have different regulatory obligations under the same roof. This is appropriate because an ATS has higher regulatory obligations because it is a market place.

Without offering any data or evidence, a conclusion is reached that "these distinctions in regulatory oversight complicate efforts to improve the efficiency and resiliency of the fixed income electronic trading markets" (<https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-electronic-trading-platforms-recommendation.pdf>). The observations and recommendation were made in July 2018. The record from the October 5, 2020 meeting included numerous examples and data demonstrating the resiliency, robustness of the market structure and, as we noted in our Introduction, how the fixed income market passed the trials of COVID-19 volatility and remote working with flying colors (<https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-100520-transcript.pdf>).

We caution the Commission that changes to Rule 3b-16 could introduce new dramatic, unintended and adverse impacts. At the July 16, 2018 FIMSAC meeting, former Director of Trading and Market's Brett Redfearn set out a series of principles when considering new regulation, such as the FIMSAC's recommendations. These included to be very focused in a value-added way, accurately determining cost-benefit, and making sure that regulation is not overly prescriptive and not potentially restricting competition but

encouraging competition. “The most important thing in this process is effectively, do no harm” (see transcript at 0250: 2-15 <https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-071618transcript.txt>).

There are no pressing failures to mitigate. Rather we concur with FINRA, that there is a reporting gap that it is now proposing to fill.

Question 151. What do commenters believe are the key common characteristics of a fixed income electronic trading platform that should merit their common regulation under the securities laws? Do these inconsistencies create risks to the integrity of the market for fixed income securities, and if so, how? Do these inconsistencies create burdens on competition among market participants, and if so, how?

Most of our comments in response to this question are in our Introduction. The regulatory framework is based on a series of activity-based “triggers” that define increasing levels of direct supervision. It is this framework that encourages innovators to enter the market. As Figures 1 and 2, and Table 1 show, the activities are very clear. It isn’t clear where harmonization is needed.

In our Introduction, we present three ways of looking at the methods of electronification that lead to electronic trading. Figure 1 depicts electronification of the manual methods (market infrastructure) that connect the islands of automated and non-automated brokerage activities together. Figure 2 shows how these methods fall along continuums of automation and instrument liquidity and where electronification (or infrastructure) becomes brokerage. Table 1 provides a detailed view of the methods, the operators and the regulatory framework to illustrate that investor interests are being robustly protected regardless.

Question 150. As noted above, securities intermediaries generally are regulated either as exchanges or as brokers or dealers. What do commenters believe are the key regulatory standards that should apply to fixed income electronic trading platforms? Are there aspects of the current regulatory structure, other than regulatory treatment, that should not apply to these trading platforms? Are there other standards not addressed in the current regulation that should be considered? How could the current regulatory structure for these trading platforms be improved?

Exchanges bind parties to a trade and dealers execute a trade. Technology suppliers (FINTECHs), on the other hand, create efficiencies in infrastructure and workflow, and, as the Treasury Capital Market’s report notes, do not fundamentally alter those relationships or change the nature of liquidity. However, we note again that it is a



misnomer to suggest that the market is not supervised because the receivers of directed orders – the brokers and dealers – are supervised. FINRA has been diligent in reminding its members of their obligations to perform due diligence, testing, business continuity verification and supervision when outsourcing activities, such as information technology and operations functions to third party vendors (i.e., see FINRA’s June 1999 Notice to Members 99-45 at <https://www.finra.org/sites/default/files/NoticeDocument/p004311.pdf> and July 2005 Notice to Members 05-48 at <https://www.finra.org/sites/default/files/NoticeDocument/p014735.pdf>).

The SEC and FINRA have laid-out clear lines of demarcation (Figure 1 and 2) for where brokerage begins (when there are non-discretionary decisions made on an order) and where ATS regulation begins (when their non-discretionary activities result in matching/binding orders). The focus is not on data organization, electronified workflows or trade messaging communication protocols but appropriately on where there is non-discretionary/automated order decision making and execution. Supervision is appropriate for the level of risk of the activity.

Question 151. What do commenters believe are the key inconsistencies in the regulation of fixed income electronic trading platforms? Do these inconsistencies create risks to the integrity of the market for fixed income securities, and if so, how? Do these inconsistencies create burdens on competition among market participants, and if so, how?

Please see our Introduction and response to question 149. We agree with the recent SEC Staff guidance that the regulatory supervisory framework in the Exchange Act focused on activity performed does not create inconsistencies in the regulation of fixed income electronified workflows and electronic trading. Also, please refer to our Introduction where we discuss both the importance of and how “market share credit” should be given - that is consistent with those principles.

Question 152. Is the current regulatory framework for fixed income electronic trading platforms unfairly promoting or impeding specific trading platforms or trading protocols over others, and if so, how? How, if at all, is the current regulatory structure hindering automation of the markets?

The current regulatory framework promotes competition and innovation, and imposes supervision and other requirements at the point of execution (liquidity location) when there are certain brokerage and potentially non-discretionary order handling and execution activities that are being performed. This an appropriate and balanced approached.

The concept release implicitly is trying to determine whether electrified workflows and trade messaging communications networks should all (a) be regulated as brokerage activity or (b) be subject to Regulation ATS with a change to Rule 3b-16. As we note in our Introduction market share credit discussion, these suggestions mistakenly conflate trade messaging communication networks with liquidity location.

Trade messaging communications networks are exactly that – messaging networks. They offer data organization and communication for efficient liquidity discovery and discretionary order routing. Technology providers operate these communications networks. Since these networks do not contain natural liquidity, they cannot commit parties to an execution. The liquidity is “held” or “owned” by the order routing destinations – brokers, dealers or ATSS. This is why a trade messaging network’s market share is irrelevant to better understand liquidity. Of course connectivity to the relevant liquidity is important but trade messaging networks really compete on providing superior analytics and data visualization that provide insights to implement investment strategies, and innovative and unique ways that they enable the parties to communicate with each other to negotiate terms. The competitive dynamics of trade messaging communication networks are similar to execution management systems.

Prior to workflow electrification, telephony was how “color” was exchanged prior to order communication and trade negotiation. As the Treasury Capital Markets Report highlighted, electrification does not fundamentally change the nature of liquidity because they rely on the same dealers and customers interacting through a different medium.

Question 154. Should the Commission consider a definition of exchange that is unique for fixed income electronic trading platforms? If so, what should that definition be and what aspects of the fixed income electronic trading markets should the definition address or not address? What are commenters’ views on how such a definition would be advantageous or disadvantageous to market participants that use fixed income electronic trading platforms and investors? How would a definition of exchange tailored for fixed income electronic trading platforms promote fair and orderly markets? How could such a definition be crafted in a way that would account for potential changes in technology that could be applied to fixed income markets and trading in the future? Would a separate definition of exchange for fixed income conflict, or create investor confusion, with regard to a definition of exchange for other asset classes, such as government securities, NMS stock, or OTC equity securities?

A unique fixed income definition is counterproductive and would create confusion. The Exchange Act recognizes the importance of market making and the OTC market. The definition of exchange and ATS works in multiple asset classes because it defines the

interactions as the basis for the activity. By doing this, the Exchange Act acknowledges that liquid and illiquid securities trade very differently. Figure 2 show how liquid securities beget highly automated markets conducive to modern ATS and exchange limit order books. Less-liquid securities, on the other hand, rely on manual and electrified workflows to discover liquidity.

Having certain activities in fixed income regulated differently than in other securities markets, such as equities (and ETFs) and options, would create confusion. Back in 2017, a Celent report “Buy Side Cross-Asset Trading Technology: Putting the Pieces Together” noted that the buy side was beginning to remap their trading desks because of the growing similarities in market structure across equities, options, derivatives, fixed income, and FX. (<https://www.celent.com/insights/923454815>). In 2018, Rob Hegarty, Managing Partner at Hegarty Group, in The Desk Newsletter noted that this evolution – trading desk consolidation and migration to multi-asset trading was driven by “increasing cost pressures; opportunities for collaboration; the availability and ubiquity of data; the rise of quantitative methods resulting in cross-asset strategies; and advancements in available technologies such as Execution Management Systems” (<https://www.marketsmedia.com/buy-side-multi-asset-trading-challenges-and-opportunities/>).

Table 1 describes communications and trading methods in the markets generally. These are not exclusive to fixed income but are present in equities, ETF and options markets. The Commission and FINRA recognize that the framework for regulation of the securities markets is based on “activity.” The activity being performed determines regulatory supervision rather than asset class. Asset class specific definitions would add confusion, complexity and change the nature of liquidity formation.

Question 155. Some electronic platform providers offer their customers a suite of different types of electronic trading protocols (e.g., auctions, request for quotes, central limit order books) that are designed to find and match counterparties. These electronic platform providers might also offer voice protocols or a hybrid of voice and electronic protocols and pricing data and facilitate trade reporting and clearing services. Do electronic platform providers such as these provide fixed income market participants with a market place for buying and selling fixed income products? Should all the protocols and services offered by electronic platform providers be considered together for purposes of the definition of exchange under federal securities laws?

Market places are specifically defined under the Rule 3(b)-16(a) and (b) of the Exchange Act and communications networks and associated protocols do not bring multiple buyers and sellers together or commit/bind parties to trades. Table 1 describes that the threshold of electronic trading is where methods of electrification - directed discretionary trade

messaging and order routing – crossover into rules-based, non-discretionary algorithmic routing, pricing and strategies and the formation of market places. The electronic trading threshold is where trader’s surrender discretion to automation and methods go from discretionary to brokerage and ultimately (central limit) order books, call auctions and crossing on ATSS. While operators of these auctions and central limit order book trading market places may also offer non-market place trading methods or FINTECH electrified workflows, such as RFQ, that should not automatically require all FINTECH operators or those methods to become regulated as market places. FINTECH, brokerage and ATS customer agreements make clear the relationships between the parties. Such a change would erect high regulatory hurdles for innovation and new FINTECH entrants. As noted in our Introduction, The Commission and FINRA recognize that supervision is proportional to the risk of the activity being performed. Moreover, the recent July 2020 guidance on Footnote 74 confirms that there are different types (categorizations) of broker-dealers, such as broker-dealer that offer non-brokerage (technology-only) activities, and that it is appropriate to require different levels of capital, reporting and supervision.

Question 156. Are the current conditions to the exemption from the definition of an “exchange” under Regulation ATS appropriate for ATSS that trade corporate or municipal debt securities (“Fixed Income ATSS”)? For example, should Fixed Income ATSS that file a confidential Form ATS with the Commission be subject to the similar operational transparency rules as an NMS Stock ATS that files a public Form ATS-N with the Commission and disclose similar detailed information about the ATS’s manner of operations and ATS-related activities of the broker-dealer operator and its affiliates? If yes, what types of disclosures should such a form solicit? What type of disclosures should such a form not solicit? How should the form compare to Form ATS-N?

As we discussed in Section II, Question 13, fixed income market structure is still developing. ATSS should continue to register with the Commission and be supervised for the non-discretionary activity in the systems. To determine whether the Form ATS should be made public and whether the ATS should comply with the fair access and ATS SCI requirement, the Commission should consider adopting a two-threshold test that we proposed in response to Section II, question 12. The first threshold – whether to lift a Regulation ATS exemption - should be based on whether ATS-trading is “developing” or is established as a “significant” liquidity channel in the market structure. The second test to determine if the ATS should be subject to fair access and SCI ATS requirements depends on whether the ATS itself is a “significant” source of liquidity. Using these thresholds provides the Commission with an objective framework to introduce the obligations in Regulation ATS incrementally to allow market structures and ATS liquidity to develop.

Question 163. Do commenters believe that it is clear when a fixed income electronic trading platform meets the definition of a broker-dealer under the Exchange Act? Should the Commission provide guidance? Are there particular fact patterns that commenters believe would be helpful for the guidance to address?

We do not believe that there is a lack of clarity. There are a set of facts and circumstances for when activities require broker-dealer registration (Figure 2). The activities are clear when a broker-dealer needs to become an ATS and the list of broker-dealers is available on FINRA's website. Moreover, subscribers know that they are dealing with a broker-dealer because it is clearly stated in the customer agreements.

Question 165.

Do commenters believe that there are fixed income electronic trading platforms that are not registered as either a broker-dealer or a national securities exchange and that do not operate as an ATS but perform similar market functions as a broker-dealer, national securities exchange, or an ATS? If so, please explain what these systems are and how they may be different or the same as a broker-dealer, national securities exchange, or ATS that operates as a fixed income electronic trading platform.

"Electronic trading platform" is not a term with clear legal definition. That said, if electronic trading platform is to be defined, we believe that an electronic trading platform is where communication *and* the commitment of parties to a transaction both occur on the same software platform.

Our securities laws are defined by activity and provide clear delineation of activities that define brokers, exchanges, ATSs (which fall within the definition of an exchange but are provided an exemption from exchange registration provided they comply with the requirements of Regulation ATS), electronic communications network (an ATS with displayed orders Rule 600(b)(24)) and dealers. These classifications are geared to the activity being performed, the level of risk being taken, the existence of supervision and complementary regulation. These are defined terms and whether a particular activity falls under the definition of any of these entities is dependent on the facts and circumstances. In our Introduction, Figure 2 shows the activity thresholds that constitute brokerage and ATS activity. Figure 2 shows where technology crosses the threshold into brokerage activity and where brokerage crosses the threshold into ATS activity.

The premise of the question conflates the electrification of workflows with electronic trading. There are no activities in the electrified workflows that are not supervised.

For example, technology providers of electronified workflow activities that do not meet the standard of brokerage activity are still supervised under the obligations that brokers and dealers have when they use outsourced technology to run their business. As we noted in response to other questions, at the October 5, 2020 FIMSAC meeting the committee unanimously agreed that the regulatory framework works and that the market passed the challenges presented from COVID-19 volatility and remote-working with flying colors. This reflects the consensus of the outside world as well.

The question also infers that since some technology providers elected to become brokers for business model or other purposes and then decided to build or acquire an ATS market place, that all technology providers, regardless of activity performed, should be regulated as an ATS. The regulatory framework is based upon the specific activity being performed. Perhaps the question should be whether there is a proper segmentation of activities occurring with brokerage and an ATS. An ATS should only perform brokerage activities that are related to an ATS. The affiliated broker-dealer should perform the “non-brokerage” electronification workflow activities.

Do commenters believe that such platforms should or should not be required to register with the Commission? Do commenters believe that such platforms should or should not be required to operate pursuant to an exemption from the definition of an exchange, such as Regulation ATS? Should such platforms be required to register as something other than a broker-dealer or national securities exchange? Should such systems be subject to the same operational transparency requirements for broker-dealers, national securities exchanges, or ATSs? What aspects of these systems would be important to market participants who may use these platforms?

Neither the FINTECH providers nor electronified workflows should be required to register with the Commission or FINRA. Messaging networks perform directed discretionary communications to a regulated entity. It is not clear what disclosures are needed. Brokers enable their customers on these networks to send and receive their communications. There are no non-discretionary activities being performed that would not only constitute brokerage but also would require disclosures of the rules of how the algorithmic activity functions.

The regulatory structure focuses on what activity is being performed and whether that activity should be supervised. There is a clear pathway of regulation based on the level of non-discretionary interactions and brokerage activity (Figure 2). The SEC and FINRA have traditionally focused on how orders are delivered (direct discretion vs. non-discretion order decision making) as the demarcation of brokerage and the type of activity at the point of execution (brokerage vs. brokerage ATS). There is a difference between manual, electronification and workflow automation or electronic trading. For

example, methods that organize and analyze data simply create operational efficiencies. Similarly, electronic messaging infrastructure and processes that digitize execution data for record keeping and improve operational risk mitigation, trade confirmation, settlement and clearing are examples of electronification.

The question infers that the FINTECHs and the electronified workflows are not supervised. As we noted before, they are monitored by the regulated entities that are using them. FINRA has set out standards for broker's relying on outsourced technology. There are powerful incentives for brokers to meet their obligation. Broker-dealers perform this monitoring as a matter of competitive differentiation to provide the best possible customer services and business continuity to ensure that the technology can scale. Broker customers also monitor technology providers because of their fiduciary duty for business continuity. Together customers and their dealers are incentivized to work with and vet technology providers.

\* \* \* \* \*

We appreciate the opportunity to provide our comments on the Proposal and Concept Release, and would be pleased to discuss any questions that the Commission may have with respect to this letter.

Very truly yours,



Gregory Babyak  
Global Head of Regulatory Affairs, Bloomberg L.P.