January 18, 2023

Via Electronic Comment Submission

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

COMMENT LETTER AND PETITION FOR SUSPENSION AND DISAPPROVAL

Re: Exchange Act File Nos. SR-NYSEAMER-2022-53; SR-NYSEARCA-2022-80; SR-NYSECHX-2022-30; SR-NYSENAT-2022-26; SR-NYSEARCA-2022-82; SR-NASDAQ-2022-080; SR-NASDAQ-2022-047

Dear Secretary Countryman:

Hyannis Port Research, Inc. ("HPR")[1] appreciates the opportunity to comment on the above-captioned notices, pursuant to which NYSE American LLC, NYSE Arca, Inc., NYSE Chicago, Inc., and NYSE National, Inc. (collectively, the "Exchanges") proposed amendments to their rules to make additional pre-trade risk controls available to certain members and, indirectly, non-members of the Exchanges (the "proposals").[2] The proposals purported to become immediately effective upon filing with the U.S. Securities and Exchange Commission ("SEC" or "Commission").[3] Nevertheless, at any time within 60 days of the filing of such a proposed rule change, the Commission summarily may temporarily suspend such proposals if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.

We respectfully submit that the Commission should suspend the proposals and institute disapproval proceedings.

We base our request on (1) several substantive arguments, including related to the significant anti-competitive effects that will likely result from the proposed risk controls, which the Exchanges

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[1] HPR is a leader in capital markets infrastructure products. HPR brought its first pre-trade risk product, RiskBot®, to market in 2011, shortly after the adoption of the "Market Access Rule" (Rule 15c3-5 under the Securities Exchange Act of 1934 ("Exchange Act")). Today, more than 1 billion shares of daily U.S. stock trading volume flows through HPR's pre-trade risk and market access products. HPR supports over 85 global markets and its clients include some of the world's largest banks and most elite proprietary trading firms.
[2] See Exchange Act Release Nos. 96403 (Nov. 29, 2022), 87 FR 74459 (Dec. 5, 2022) (SR-NYSEAMER-2022-53); 96499 (Dec. 14, 2022), 87 FR 77907 (Dec. 20, 2022) (SR-NYSEARCA-2022-80); 96504 (Dec. 15, 2022), 87 FR 78166 (Dec. 21, 2022) (SR-NYSEARCA-2022-82); 96488 (Dec. 13, 2022), 87 FR 77651 (Dec. 19, 2022) (SR-NYSECHX-2022-30); and 96487 (Dec. 13, 2022), 87 FR 77662 (Dec. 19, 2022) (SR-NYSENAT-2022-26).
[3] The Exchanges filed the proposed rule changes pursuant to Section 19(b)(3)(A) of the Exchange Act and Rule 19b-4(f)(6) thereunder, which requires that the proposed rule change effects a change that (A) does not significantly affect the protection of investors or the public interest; (B) does not impose any significant burden on competition; and (C) by its terms, does not become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest.

failed to address in the proposals; and (2) several procedural arguments, including that the Exchanges did not properly designate the proposals as rule changes for which immediate effectiveness is appropriate under Rule 19b-4(f)(6). We believe suspension and disapproval proceedings are necessary and in the public interest, for the protection of investors, and in furtherance of the purposes of the Exchange Act, as supported by the discussion below.

Our primary concern is that the proposals neither include any discussion of other risk control alternatives available in the marketplace, like those from HPR or major broker-dealers, nor any analysis of how the proposals would affect competition in this area. In our view, the Exchanges' proposed "no-fee" risk controls are structured to provide the Exchanges (and certain of their users) with unfair and anti-competitive economic and latency advantages over firms like HPR and its customers. Discussion of these considerations is not only important, but is mandated by the Exchange Act and Rule 19b-4 thereunder.

Relatedly, because the proposed risk controls are a commercial offering (albeit largely designed to support regulatory obligations under the Market Access Rule) that directly competes with services provided by brokers or private vendors like HPR, the Exchanges should neither benefit from rule-based limitations on liability nor regulatory immunity. We believe that the Exchanges could not offer the proposed risk controls for free without these benefits, which should be limited to their regulatory activities.

HPR Comments and Concerns Regarding the Proposals

1. The Proposed Risk Controls Will Impose Significant Burdens on Competition

The proposals fail to sufficiently explain the certain anti-competitive effects imposed by the proposed risk controls. **We therefore believe this causes the proposals to be deficient and supports our petition for suspension and disapproval**.

Exchange Action Section 6(b)(8) requires that the rules of an exchange not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act. Item 4 of Form 19b-4 requires the Exchanges to provide their statements on the burden on competition resulting from the proposals. The proposals do purport to address competition. However, we think these aspects of the proposals are mere window dressing, largely make no logical sense in the context of actual competitive effects of the proposals, do not sufficiently satisfy the standards mandated under the Exchange Act, and therefore support our petition for suspension and disapproval.

The proposals include a boilerplate assertion that the Exchanges do not believe that the proposed rule changes will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. However, the Exchanges provide no basis to support this assertion, as they are required to do. In particular, and contrary to the Exchanges' assertions, **we believe the proposals will absolutely impose a significant burden on competition**. Moreover, the proposals will make it commercially impracticable for firms to use

third party offerings like HPR's due to anti-competitive latency features, predatory pricing, and related considerations. The proposals make no mention of these effects on competition.

The Exchanges' inadequate attempts to support their assertions regarding the lack of significant competitive effects consist entirely of several confusing statements seemingly grasping at alleged positive effects the proposed risk controls might have on competition, including:

> the proposal[s] will have a positive effect on competition because, by providing Entering Firms additional means to monitor and control risk, the proposed rule[s] will increase confidence in the proper functioning of the markets.
>
> the proposed additional Pre-Trade Risk Controls will assist Entering Firms in managing their financial exposure which, in turn, could enhance the integrity of trading on the securities markets and help to assure the stability of the financial system. As a result, the level of competition should increase as public confidence in the markets is solidified.

With these conclusory and unsubstantiated statements, the Exchanges are attempting to connect risk considerations, integrity of the markets, and stability of the financial system with an analysis of competition. This is inherently flawed and deficient, primarily because it ignores the fact that a competitive market for risk-related services already exists. Moreover, we fail to see how the proposed risk checks would "solidify public confidence in the markets" and believe that, in fact, the opposite is more likely true. As is further described below, the Exchanges' pre-trade risk check offerings are less understood, less comprehensive, and less tested than other marketplace offerings, such as HPR's. The Exchanges' proposed offerings also introduce new market complexities, considering users need to stitch together multiple unique offerings among different exchanges to satisfy Market Access Rule compliance obligations. It is both possible and likely that certain firms will be incentivized to use such inferior exchange offerings largely due to the anti-competitive economic and latency advantages that are part of the Exchanges' proposed offerings and that are feasible solely due to benefits that result from direct integration into the Exchanges' facilities and their regulatory status. Further, we believe that confidence may be further eroded due to the significant conflict the Exchanges will bear as provider of a service being used to satisfy regulatory obligations while also serving as the regulator responsible for surveilling those very regulatory obligations. The notion that this would increase the level of competition or public confidence in the markets is baseless and inaccurate.

The proposals also fail to discuss how the Exchanges are able to provide the proposed risk checks for free, particularly whether such a discount would be feasible if it were not for the economic advantages provided by exchange rule-based limitations on liability or purported regulatory immunity in the case of a flawed deployment or malfunction. We understand that the Exchanges intend to fully benefit from their rule-based limitations on liability and perhaps even purported regulatory immunity, despite that the proposed services will directly compete with similar non-exchange commercial offerings. We suspect that such services could not be offered for free were it not for the fact that they bear little economic risk in the event of a failure of their pre-trade controls. Further, the Exchanges do not address whether significant competitive forces constrain their ability or charge a fee for the risk controls. Conversely, the Exchanges do not address how

not charging for the proposed risk controls would impose significant anti-competitive forces that would constrain others, like HPR, from charging for similar services.

Similarly, the proposals do not discuss the Exchanges' costs to develop the proposed risk checks—i.e., are they so negligible that a zero fee is consistent with the Exchange Act? The proposals also do not address whether the Exchanges are able to upsell market data and other synergistic products as they form and solidify direct relationships with non-member users of the proposed risk controls (versus those users consuming risk controls provided by member firms or vendors, including HPR's products).

We believe that the points raised above, individually and in the aggregate, objectively show that the Exchanges have failed to explain how the proposed risk controls will not impose a significant burden on competition and, therefore, that the Commission should suspend and disapprove the proposals.

2. The Exchanges Failed to Sufficiently Describe Latency, Lack of Novelty of the Controls, and Related Considerations

The proposals note that use of the proposed pre-trade risk controls would be optional. However, and importantly, "all orders on the Exchange[s] would pass through these risk checks." The proposals further state that a firm "that does not choose to set limits pursuant to the new proposed pre-trade risk controls would not achieve any latency advantage with respect to its trading activity on the Exchange." Finally, the proposals note that "the Exchange[s] expect[] that any latency added by the pre-trade risk controls would be *de minimis* (emphasis added)." Several flaws exist with the proposals in this regard.

Unlevel Playing Field; Anti-Competitive Offering

First, the Exchanges do not explain how they will eliminate latency advantages as between firms that choose to use the proposed risk controls and those that do not. We believe the Exchanges have architected the proposed risk controls to give themselves an unfair and anti-competitive latency advantage over non-exchange offerings provided by broker-dealers or vendors such as HPR. Instead of eliminating a latency advantage between users and non-users of the Exchanges' services, the proposed risk controls would ensure an unfair latency advantage for users of the Exchanges' services in contrast to those firms that use another, non-exchange service – not because the Exchanges' services are better or faster, but because the Exchanges impose a "latency tax" on non-users of the Exchanges' services.

To illustrate, non-exchange providers of low latency pre-trade risk controls (and their customers) incur a small latency cost (latency cost A). Exchanges (and their customers) would also incur a small latency cost for their low latency pre-trade risk checks (latency cost B). If non-exchange providers (and their customers) incur both latency cost A and latency cost B, regardless of whether they want or need the Exchange-offered controls, then non-exchange providers (and their customers) are put at a distinct latency disadvantage versus the Exchanges and their customers that only incur latency cost B. The Exchanges should not be permitted to subject all customers to latency cost B, specifically those customers that opt out of the Exchanges' proposed risk controls

and have otherwise (including in a more robust and comprehensive manner) managed their regulatory obligations, including under the Market Access Rule.

No Substantiation of "De Minimis" Latency Claims

Second, the Exchanges do not explain what they consider "de minimis" latency added by the proposed risk controls. The Commission knows all too well that speed and latency, measured in nanoseconds (i.e., increments of one-billionth of one second), are among the most critical considerations for many institutional market participants. In reality, HPR as well as certain broker-dealers have made significant technology investments to compete at a nanosecond level with pre-trade risk checks. It is critical that the Exchanges clearly describe how they intend to compete in the space of low-latency pre-trade risk checks and to ensure that they are doing so on a level playing field with other providers of such services. The Commission also previously thought this issue was so critical that in 2016 it issued an interpretation (the "de minimis interpretation") of what "immediate" means in the context of Regulation NMS as "not precluding a de minimis intentional delay—i.e., a delay so short as to not frustrate the purposes of Rule 611 by impairing fair and efficient access to an exchange's quotations."[4]

We suggest that the Commission should view the proposed risk controls as an intentional access delay. However, in contrast to the intentional access delay offered by another exchange addressed by the Commission, which is administered evenly to all its members with no differentiation of services provided, in this case, the Exchanges will mandate that all trading interest pass through the proposed controls, resulting in latency even for those firms who choose not to avail themselves of the controls. This is an uneven and unfair application of an intentional access delay and puts those users who have chosen to use a pre-trade risk check service elsewhere at a disadvantage to those who use the Exchanges' pre-trade risk checks. This application creates an unfair burden on competition that is inconsistent with the Exchange Act.[5]

Based on this view, we think the proposals are deficient on their face, as they do not fully describe expected added latencies to both users and non-users or the application of the access delay—neither in the proposed rule text itself nor in the purpose section, statutory basis section, burden on competition section, nor any other section of the Exchanges' Forms 19b-4 filed with the Commission. This supports our opinion that the Commission should suspend and disapprove the proposals. We submit that the Exchanges' proposals have neither undergone a "process through which [they] publicly propose[d] their rule changes" nor have the proposals been "scrutinized on an individual basis through that process."[6]

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[4] See Exchange Act Release No. 78102 (June 17, 2016), 81 FR 40785 (June 23, 2016) (File No. S7-03-16) (Commission Interpretation Regarding Automated Quotations Under Regulation NMS), available at https://www.sec.gov/rules/interp/2016/34-78102.pdf.

[5] As noted in the Commission de minimis interpretation, "this interpretation does not address whether any particular access delay is unfairly discriminatory, an inappropriate or unnecessary burden on competition, or otherwise inconsistent with the Act" further adding "that the evaluation of any proposed access delay would involve additional considerations." Id. at 40789.

[6] Id. at 40790. As noted in the Commission de minimis interpretation, "this interpretation does not obviate the requirement of individualized review of proposed access delays, including de minimis delays, for consistency with the Exchange Act and Regulation NMS. Any exchange seeking to impose an access delay must reflect that in its rules,

The Commission knows that "unquestioning reliance" on the Exchanges' representations in the proposals is not sufficient to support a finding that the proposals are consistent with the Exchange Act."[7] Notwithstanding our view that such an uneven application of an intentional access delay is inconsistent with fairness provisions under the Act as noted above, the Exchanges should certainly not be permitted to proceed with any such access delay without Commission approval after thoroughly describing details like the ensuing latency via a proposed rule change filed pursuant to Exchange Act Section 19(b)(2) that is published for notice and comment. Filing these proposals for immediate effectiveness pursuant to Section 19(b)(3)(A) is improper.

No Corroboration of "Substantially Identical" Claims

Third, the Exchanges assert that the proposed risk checks are not novel. In support of this, the Exchanges claim that they are substantively identical to risk settings available on other equities exchanges and that market participants are already familiar with the protections the proposed risk controls afford. However, the Exchanges make no effort to corroborate what they mean by "substantively identical" or to compare and contrast the offerings on those other markets with the risk checks described in the proposals, including the application of other intentional access delays. Even if identical, the conclusory manner of these assertions by the Exchanges is not sufficient to comply with the requirements of the Exchange Act and Rule 19b-4, as we noted above related to "unquestioning reliance." Further, the risk checks currently offered by other markets cited by the Exchanges have evolved incrementally in ways that may have occurred outside of the rule filing process without Commission review or public comment and may, at this point, warrant further Commission review to determine if similar issues and concerns are present.

The Exchanges' members, their competitors, firms like HPR, the general public, and the Commission itself are unable to sufficiently analyze the effects of the proposed risk controls based on the sparce information in the proposals or, for other exchanges, in their published rules and related marketing materials. Without more detail and substantiation, the Exchanges have failed to provide sufficient information to support their statements and, therefore, the Commission should suspend and disapprove the proposals.

3. The Proposals Do Not Address Elements Required for Fee Filings or Related Commission Staff Guidance

On their face, the proposals do not establish or change a due, fee, or other charge. We do not dispute that. However, it is indisputable that the proposed risk checks are a service provided by the Exchanges, which the Exchanges may, at their discretion, decide to charge for at any point in the future. Had the Exchanges proposed to charge for the proposed risk controls, the filings would have needed to address several other considerations, including explaining how those proposed fees

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which are required to be filed with the Commission as part of the exchange application or as an individual proposed rule change. This interpretation does not alter the requirement that any exchange access delay must be fully described in a written rule of the exchange, which in turn must be filed with the Commission and published for notice and comment, nor does it obviate the need for a proposed rule change that would impose an access delay otherwise to comply with the Act and the regulations thereunder applicable to the exchange." Id.

[7] See, e.g., Susquehanna Int'l Group LLP, et al., v. SEC; 866 F.3d 442 (D.C. Cir. 2017).

are (i) reasonable, (ii) equitably allocated, (iii) not unfairly discriminatory, and (iv) not an undue burden on competition.[8]

Exchange Act Section 19(b)(3)(A)(ii) provides that, notwithstanding the provisions of Exchange Act Section 19(b)(2), "a proposed rule change shall take effect upon filing with the Commission if designated by the self-regulatory organization as establishing or changing a due, fee, or other charge imposed by the self-regulatory organization *on any person*, whether or not the person is a member of the self-regulatory organization (emphasis added)." Meanwhile, Rule 19b-4(f)(2) refers to immediate effectiveness for fees applicable "only to a member."

According to prior Commission staff guidance,[9] "fee filings" are proposed rule changes relating to fees, including, but not limited to, transaction fees, proprietary market data fees, and connectivity and access fees. Connectivity and access fees refer to fees charged by a self-regulatory organization ("SRO") that permit a member or non-member to access an SRO's proprietary market data or its trading and execution systems, including, without limitation, fees for network services, physical ports, and logical ports. The staff guidance indicates that the term "fees" refers "broadly to all pricing determinations set forth on an SRO's fee schedule, including charges assessed, waivers thereof or discounts thereto, and rebates or credits offered."

Simply put, the Exchanges propose to offer a service to compete with services in which others have invested significant financial resources to develop, and for which others charge a fee, and the Exchanges further propose to use their unique regulatory position to undercut the market by offering the services for free, at least initially. We think it is reasonable to take the view that the proposed zero-fee risk controls effectively constitute a fee waiver or discount currently set at zero. We believe footnote 9 of the Commission staff guidance provides support for this view:

> Note that a proposal establishing a new service, program or trading rule cannot be designated as a fee filing under Rule 19b-4(f)(2) solely because it also includes a fee component. *See* Exchange Act Rule 19b-4(f)(2). Such a filing would be rejected by the staff as improperly designated/filed. The provisions of the proposal apart from the fee would have to be separately filed under Section 19(b)(2) or under another provision of Rule 19b-4, including 19b-4(f)(6), if applicable. *However, if a proposal filed under Section 19(b)(2) or another provision of Rule 19b-4 includes a fee component, this guidance will apply to the fee component* (emphasis added).

The staff guidance clearly contemplates filings submitted other than pursuant to Rule 19b-4(f)(2) that include "a fee component" and that the staff guidance "will apply to the fee component." We believe that the Commission should consider a pricing-for-services determination that results in a zero fee in the same light as it considers any non-zero fee for a set of services – especially for services that are already offered in the marketplace as fee-based services. In this regard, the proposals do not address at all (or insufficiently address) whether the proposed risk controls are (i) reasonable, (ii) equitably allocated, (iii) not unfairly discriminatory, and (iv) not an undue burden

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[8] See Exchange Act Sections 6(b)(4), (5), and (8).

[9] *Staff Guidance on SRO Rule Filings Relating to Fees*, SEC, (May 21, 2019), *available at* https://www.sec.gov/tm/staff-guidance-sro-rule-filings-fees.

on competition. In this circumstance, we believe that the zero fee *does* cause a significant and undue burden on competition, especially in light of the significant costs associated with building, marketing, testing, and deploying products of this nature. HPR, for example, has spent tens of millions of dollars building pre-trade products that are better, more reliable, and more sophisticated at managing for latency. A free version of such product appears to be akin to classic "dumping" by a large and powerful player that is uniquely positioned to eliminate competitors.[10] Once competitors charging fees have been eliminated, the remaining party is left with excessive market power due to the absence of substitutes. In the history of economic competition, this type of behavior has never resulted in improved services, lower costs, and better competition over the long term. Instead, the typical result is inferior services, increased costs, and less or no competition in the marketplace. Accordingly, we believe the Commission should suspend and disapprove the proposals.

4. The Exchanges Failed to Discuss Their Limits on Liability and Conflicting Roles in the Context of the Proposals and the Market Access Rule

The proposals are clearly designed to assist the Exchanges' members and, indirectly, non-member customers in satisfying compliance with the Market Access Rule. To the contrary, however, the proposals note that the proposed risk controls "are meant to supplement, and not replace, [members'] own internal systems, monitoring, and procedures related to risk management and are not designed for compliance with Rule 15c3-5 under the Exchange Act." The proposals also note that:

> the [Exchanges do] not guarantee that [the proposed risk controls] will be sufficiently comprehensive to meet all of [a member's] needs, the controls are not designed to be the sole means of risk management, and using these controls will not necessarily meet [a member's] obligations required by [the Exchanges'] or federal rules (including, without limitation, the [Market Access Rule]). Use of the Exchange's [proposed risk controls] will not automatically constitute compliance with Exchange or federal rules and responsibility for compliance with all Exchange and SEC rules remains with the [member].

We would agree that the Exchanges' pre-trade risk controls, on their own, are unlikely to meet all of a broker-dealers' Market Access Rule compliance obligations. To meet their best execution obligations and to comply with the Order Protection Rule, for example, broker-dealers must route to multiple venues, not solely to one exchange. A broker-dealer would likely need to stitch together multiple exchange pre-trade risk offerings and manage risk centrally in this manner. While complex, cumbersome, and less comprehensive than all-inclusive offerings such as HPR's, it is highly likely that each of the Exchanges' offerings could become integral component parts of a broker-dealer's overall Market Access Rule compliance and could be held up as largely satisfying a broker-dealer's specific set of Market Access Rule obligations at each Exchange separately.

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[10] See supra notes 17 and 18, referring to a comparable pre-trade risk control from a competing exchange that will similarly be offered at zero cost and will, in that exchange's own words, "[r]educe the use of outside vendors."

This raises at least two important questions and considerations that the Exchanges did not address in the proposals, further supporting our petition for suspension and disapproval.

Conflicted Role as Both Regulator and Commercial Provider

First, in the event of a failure of risk controls, the Exchanges have not addressed whether and how they will account for and manage their conflicted roles as a regulator of users of the proposed risk controls, on the one hand, and a commercial provider of risk-based tools integral to exchange members' regulatory obligations, economic interests, and competitive positions, on the other hand. This is a fundamental and material conflict that could affect how the Exchanges implement their regulatory obligations and enforcement capabilities and responsibilities. In this regard, various rules of the Exchanges require that members establish and maintain systems to supervise the activities of their associated persons and the operations of their business, including that such systems be reasonably designed to ensure compliance with applicable federal securities laws and regulations and the Exchanges' rules.[11] The Exchanges have brought enforcement actions against their members for failing to comply with the Market Access Rule, consistent with their obligations as SROs.[12] The proposals note that "[r]responsibility for compliance with all Exchange and SEC rules remains with the [firm]." Nevertheless, would the use of the proposed Exchange risk controls factor into the Exchanges' analysis of whether a firm maintained reasonably designed erroneous order and credit controls? If not, how would the Exchanges ensure equal consideration for firms who use the proposed exchange risk controls compared to those who use other competing commercial products? Would the type of investigation, disciplinary action, and the amount of any eventual fines be linked in any way to use of the proposed Exchange risk controls? Likewise, would or should the Commission consider whether risk controls were provided by an SRO or non-SRO in determining whether to bring an enforcement action against a firm that used the proposed Exchange risk controls, but eventually submitted erroneous orders or orders that exceeded pre-set capital limits, for example?

Exchange Limitation on Liability; Regulatory Immunity

Second, we question whether and to what extent the Exchanges' rules limiting their liability to members and their broader claims of regulatory immunity would be applicable to future instances of malfunction of the proposed Exchange risk controls or to the Exchange's implementation of their regulatory obligations as SROs. In this regard, and for example, NYSE American Rule 13.2E broadly disclaims liability associated therewith for any loss, expense, damages or claims that arise out of the use or enjoyment of the facilities or services afforded by the exchange, any interruption in or failure or unavailability of any such facilities or services, or any action taken or omitted to be taken in respect to the business of the exchange except to the extent such loss, expense, damages or claims are attributable to the willful misconduct, gross negligence, bad faith or fraudulent or criminal acts of the exchange or its officers. The other Exchanges maintain similar rules. For

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[11] See, e.g., NYSE Arca Rule 11.18(b).

[12] See, e.g., In re: SpeedRoute, LLC; NYCEARCA Letter of Acceptance, Waiver, and Consent (Dec. 30, 2021), available at https://www.nyse.com/publicdocs/nyse/markets/nyse-arca/disciplinary-actions/2021/SpeedRoute%20AWC%20Fully%20Executed%2012.30.21.pdf.

decades, exchange-based limitations of liability rules have been, and continue to be, a source of contention between SROs and their members.[13] Separately, exchanges (generally) have made claims of immunity in litigation due to their SRO status and quasi-governmental activity despite also engaging in non-regulatory commercial activity. Exchanges should not be able to rely on their liability limiting rules or regulatory immunity when engaging in non-regulatory commercial endeavors such as these proposed risk controls, especially when they are competing with non-exchange commercial offerings like HPR's. The SEC's views in a prior amicus brief appear to support our view:[14]

> The Commission believes that absolute immunity is properly afforded to the exchanges when they are engaged in their traditional self-regulatory functions—in other words, when the exchanges are acting as regulators of their members. Immune activities include the core adjudicatory and prosecutorial functions that have traditionally been accorded absolute immunity, as well as other functions that materially relate to an exchange's regulation of its members. For example, an exchange should be immune when it disciplines its members for misconduct or suspends from trading by its members a security listed on its market. But the Commission believes that immunity *does not properly extend to functions performed by an exchange itself in the operation of its own market, or to the sale of products and services arising out of those functions* (emphasis added)

To take an opposite view would erode the core principles of competition and fair play. We take this view even when the Exchanges propose to offer the controls for a zero fee. This will be especially true when the Exchanges eventually decide to charge a fee other than zero for these offerings, likely after their anti-competitive effect on the marketplace has eradicated any competition.

The Exchanges' proposals implicate the need for careful and deep consideration in these areas, which we think can only be accomplished through the course of a "regular" rule filing that is published for full notice and comment and in a way that requires the Exchanges themselves to proffer their related views. We are particularly interested in how the Exchanges would deal with a scenario in which a user was to allege that the Exchange risk controls caused or contributed to a regulatory violation or caused or contributed to activity on the Exchanges that resulted in a substantial commercial loss. Would the Exchanges insist on staying within their rule-based liability limits, even if the customer's losses greatly exceeded those amounts? Would the Exchanges claim regulatory immunity and on what basis if a related legal claim linked the Exchanges' controls to the Exchanges' very own technical failure (and possibly the Exchanges' imposition of a regulatory fine as SRO)? If the Exchanges claim regulatory immunity, would that

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[13] See, e.g., Exchange Act Release No. 93484 (Oct. 29, 2021), 86 FR 60933 (Nov. 4, 2021) (File No. 4-698).

[14] See Brief of the Securities and Exchange Commission, Amicus Curiae, City of Providence, Rhode Island, Employees' Retirement System of the Government of the Virgin Islands, Plumbers and Pipefitters National Pension fund, State-Boston Retirement System v. BATS Global Markets, Inc., Chicago Stock Exchange Inc., Direct Edge ECN, LLC, NYSE Arca, Inc., NASDAQ OMX BX Inc., New York Stock Exchange LLC, The NASDAQ Stock Market, LLC, No. 15-3057 (November 28, 2016), available at https://www.sec.gov/litigation/briefs/2016/providence-bats-global-markets-1116.pdf.

be appropriate under the circumstances?[15] And, could the Exchanges make financial concessions to members if the proposed risk controls were even a partial source of a member's failure to satisfy the Market Access Rule? Would any such concessions be made only with respect to commercial losses or also with respect to regulatory penalties?

Each of these questions and considerations warrant discussion in the proposals and, without being addressed therein, should lead to their suspension and disapproval by the Commission. These questions and considerations also factor into the competition discussion above, including because non-SROs typically are not in a position to completely disclaim any liability to their users, whether directly or indirectly, commercial or regulatory in nature, or otherwise. As one former SEC Commissioner stated, "[i]t's hard to imagine many businesses that we'd want to hold accountable more than our stock exchanges, where millions of Americans' retirement and education savings are invested each day. Yet when they are sued, stock exchanges assert that they are immune from liability on the theory that they are acting as regulators rather than profit-makers."[16] We strongly believe that it is critical for the protection of the markets and to ensure competition between market participants that the Exchanges and the Commission address how and to what extent the proposed risk controls would be viewed with respect to the Exchanges' liability-limiting rules or regulatory immunity under the Exchange Act.

Conclusion

We appreciate the opportunity to comment on the proposals and share our belief that the proposals are deficient and that the Commission should suspend and disapprove them.

While we are very concerned about the anti-competitive nature of these offerings, we generally believe exchanges should be able to offer pre-trade risk controls like those described in the proposals. However, exchange-offered pre-trade risk controls should not embed unfair latency advantages and should not benefit from rule-based limitations on liability and regulatory immunity, of which non-exchanges cannot avail themselves. We are also concerned that these exchange-offered risk controls exacerbate an inherent conflict within exchanges in their function as competitive, commercial providers of tools used to meet regulatory obligations and as market regulators, and that this conflict could undermine – not promote – market confidence.

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[15] One court decision noted that "[b]ecause they perform a variety of vital governmental functions, but lack the sovereign immunity that governmental agencies enjoy, SROs are protected by absolute immunity when they perform their statutorily delegated adjudicatory, regulatory, and prosecutorial functions." *Weissman v. Nat'l Ass'n of Sec. Dealers,* 500 F.3d 1293, 1296 (11th Cir. 2007). However, that same decision noted that "entities that enjoy absolute immunity when performing governmental functions cannot claim that immunity when they perform non-governmental functions." Id. That decision went on to say that "[SROs] do not enjoy complete immunity from suits." Id. at 1297. Instead, "[o]nly when an SRO is 'acting under the aegis of the Exchange Act's delegated authority' does it enjoy that privilege. Absolute immunity is not appropriate unless the relevant conduct constitutes a delegated quasi-governmental prosecutorial, regulatory, or disciplinary function." Id.

[16] Robert J. Jackson Jr., *Unfair Exchange: The State of America's Stock Markets* (Sept. 19, 2018), available at https://www.sec.gov/news/speech/jackson-unfair-exchange-state-americas-stock-markets.

Finally, we understand that Nasdaq Stock Market ("Nasdaq") plans to offer comparable pre-trade risk controls.[17] Like the Exchanges, Nasdaq filed its proposal for immediately effectiveness, although Nasdaq has not implemented the pre-trade risk checks and recently filed to delay their implementation.[18] We understand that the Nasdaq offering will be a "zero-latency solution" (i.e., every order that comes into its infrastructure will have the same latency, whether it uses its pre-trade risk checks or not). We have concerns with the Nasdaq controls similar to those expressed above with respect to the Exchanges', including related to their significant anti-competitive effects and failure to sufficiently explain latency considerations. We strongly encourage the Commission to suspend and institute proceedings to determine whether to approve or disapprove Nasdaq's proposal and controls (or take other similar action within the Commission's authority in furtherance of its mission, including to maintain fair, orderly, and efficient markets), consistent with the discussion above related to the Exchanges' controls. The Nasdaq controls (and proposal) raise the same concerns and should be further addressed by Nasdaq in a proposed rule change filed pursuant to Exchange Act Section 19(b)(2) that is published for notice and comment and that provides the Commission with an opportunity to consider the controls before Nasdaq implements them.

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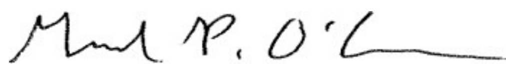
If you have any questions or you would like to discuss these matters further, please contact me at [redacted] or [redacted].

Respectfully submitted,



Gerard P. O'Connor
Vice President and General Counsel
Hyannis Port Research, Inc.

cc: Gary Gensler, U.S. Securities and Exchange Commission, Chairman
Hester M. Peirce, U.S. Securities and Exchange Commission, Commissioner
Caroline A. Crenshaw, U.S. Securities and Exchange Commission, Commissioner
Jaime Lizárraga, U.S. Securities and Exchange Commission, Commissioner
Mark T. Uyeda, U.S. Securities and Exchange Commission, Commissioner
Haoxiang Zhu, U.S. Securities and Exchange Commission, Director, Division of Trading and Markets
David S. Shillman, U.S. Securities and Exchange Commission, Associate Director, Division of Trading and Markets

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[17] See Exchange Act Release No. 95495 (August 12, 2022), 87 FR 50902 (August 18, 2022) (SR-NASDAQ-2022-047). See also Nasdaq Equity Trader Alert #2022-107 (Nasdaq Introduces Equities Risk Checks), available at http://www.nasdaqtrader.com/TraderNews.aspx?id=ETA2022-107. See also Nasdaq Equity Risk Checks (EQRC) Overview, available at https://www.nasdaq.com/docs/EQRC-overview.

[18] See Exchange Act Release No. 96592 (December 29, 2022), 88 FR 892 (Jan. 5, 2023) (SR-NASDAQ-2022-080).