



1401 H Street, NW, Washington, DC 20005-2148, USA
202/326-5800 www.ici.org

April 18, 2022

By Email

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 205499-1090

Re: *Amendments to Exchange Act Rule 3b-16 Regarding the Definition of “Exchange” and Alternative Trading Systems (ATSS) That Trade U.S. Treasury and Agency Securities, National Market System (“NMS”) Stocks, and Other Securities (File No. S7-02-22)*

Dear Ms. Countryman:

The Investment Company Institute¹ is writing to respond to the Securities and Exchange Commission’s (“Commission”) proposal to, among other things, amend Rule 3b-16 under the Securities Exchange Act of 1934 (“Exchange Act”), which defines certain terms used in the statutory definition of “exchange” under Exchange Act Section 3(a)(1), to include systems that offer the use of non-firm trading interest and communication protocols to bring together buyers and sellers of securities (“Proposal”).² If adopted, the Proposal, among other things, would require that a communication protocol system (CPS) register with the Commission as an exchange or, alternatively, register as a broker-dealer and comply with alternative trading systems (ATS) requirements.³

¹ The [Investment Company Institute](https://www.ici.org) (ICI) is the leading association representing regulated investment funds. ICI’s mission is to strengthen the foundation of the asset management industry for the ultimate benefit of the long-term individual investor. Its members include mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and UCITS and similar funds offered to investors in Europe, Asia, and other jurisdictions. Its members manage total assets of \$31.0 trillion in the United States, serving more than 100 million investors, and an additional \$10.0 trillion in assets outside the United States. ICI has offices in Washington, DC, Brussels, London, and Hong Kong and carries out its international work through [ICI Global](https://www.ici.org/global).

² *Amendments to Exchange Act Rule 3b-16 Regarding the Definition of “Exchange” and Alternative Trading Systems (ATSS) That Trade U.S. Treasury and Agency Securities, National Market System (NMS) Stocks, and Other Securities*, Exchange Act Release No. 94062 (Jan. 26, 2022), 87 Fed. Reg. 15496 (Mar. 18, 2022) (“Proposal”).

³ The Proposal also would (i) require ATSS that trade government securities, as defined under Section 3(a)(42) of the Exchange Act, or repurchase and reverse repurchase agreements on government securities (“Government Securities ATSS”) to comply with Regulation ATS; (ii) amend Form ATS-N to apply to Government Securities ATSS and to

As a threshold matter, the Commission has provided an insufficient comment period for a rule proposal of this magnitude and complexity. Significantly expanding the scope of what constitutes an “exchange”—which is only one aspect of the Proposal—will have fundamental implications for trading and market structure across many different asset classes for all market participants, including funds and advisers. The important issues raised by the Proposal warrant the Commission providing more time and opportunity for public comment so that the Commission can obtain critical feedback on how the amended rule would apply and the full scope of issues and concerns it raises, including any unintended consequences. Given the short comment period and the numerous other recent proposals the Commission has issued that have also required our attention, we focus our comments in this letter on one key aspect: the proposed amendments to the “exchange” definition.⁴

While the proposed amendments reflect the Commission’s focus on increasing regulatory consistency of platforms that facilitate electronic trading, they unfortunately risk sweeping in systems that perform what unmistakably is a different function—order and execution management systems (OEMSs) used by investment advisers⁵ and other buy-side market participants. We believe that the Commission did not intend for the “exchange” definition to apply to the individual OEMSs that investment advisers use to manage their portfolio investments on behalf of regulated funds and other clients. Nevertheless, the broad scope of the proposed amendments to Rule 3b-16, as well as certain inconsistent and ambiguous statements in

require additional information disclosures from existing NMS Stock ATSs; and (iii) amend Regulation Systems Compliance and Integrity (Regulation SCI) to apply to certain ATSs that meet certain volume thresholds in US Treasury securities or agency securities. Several of the requirements applicable to Government Securities ATSs were previously proposed in a 2020 Commission release. *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 Electronic Corporate Bond and Municipal Securities Markets*, Exchange Act Release No. 90019, 85 Fed. Reg. 87106 (Dec. 31, 2020). Consistent with our previous comments, we reiterate our general support for applying ATS and SCI regulations to Government Securities ATSs to promote operational transparency, investor protection, fair access, and system security and resiliency. Specifically, we support applying the Regulation ATS fair access rule to interdealer Treasury ATS platforms, which would help to promote more “all-to-all” trading by enhancing the ability of funds to onboard and participate on these platforms. Letter from Sarah A. Bessin, Associate General Counsel and Nhan Nguyen, Counsel, ICI, to Vanessa Countryman, Secretary, Securities and Exchange Commission, (Mar. 1, 2021) (“2021 ICI Letter”), available at <https://www.sec.gov/comments/s7-12-20/s71220-8431900-229619.pdf>.

⁴ Given the limited opportunity to provide fulsome feedback on the Proposal, we urge the Commission and its staff to provide further guidance or no-action relief as necessary to address issues that may arise under any final rule. With the benefit of a longer comment period, we would have also provided comments on the numerous proposed changes to Form ATS-N, including amendments to Form ATS-N that would apply to both NMS Stock ATSs and Government Securities ATSs, as well as amendments to the Regulation ATS fair access rule.

⁵ For purposes of this letter, the term “investment adviser” refers to one or more affiliated investment advisers within an investment management complex.

the Proposal, could lead to adverse outcomes for funds and their advisers if the Commission were to conclude otherwise.

To avoid any such adverse outcomes, which we discuss below, we request that the Commission confirm that an OEMS is not a CPS and otherwise would not meet the definition of “exchange” based on amended Rule 3b-16(a). Specifically, the Commission should confirm that the following attributes or functions of an OEMS would not cause the OEMS to be deemed a CPS or otherwise meet the definition of “exchange” because of the proposed amendments to the rule:

- Facilitating communication of trading interest by serving as a conduit to connected “trading venues,”⁶ *i.e.*, providing a communications link and conveying trading instructions to a trading venue via an OEMS.
- Importing and displaying data fields or information from connected trading venues, *e.g.*, those that facilitate submitting requests-for-quotes (RFQs) or receipt of indications of interest (IOIs), based on the methods, rules, or protocols set forth by those venues.
- Applying “communication protocols” that are established by a connected trading venue.
- Organizing, presenting, or otherwise displaying trading interest (whether firm or non-firm) that is available at a connected trading venue, but is not available on or through the OEMS itself.
- Facilitating internal cross-trading among clients (including funds) by an investment adviser or its affiliates, consistent with the adviser’s fiduciary duty and applicable statutes (*e.g.*, the Investment Advisers Act of 1940 (“Advisers Act”) and the Investment Company Act of 1940 (“Investment Company Act”)), rules (*e.g.*, Rule 17a-7 under the Investment Company Act), and Commission and staff guidance and relief.

Confirming that these typical OEMS attributes or functions would not cause an OEMS to be deemed a CPS or otherwise meet the definition of an “exchange” is necessary to avoid critical disruptions to the ability of funds and their advisers to utilize OEMSs to centrally manage their portfolio holdings and carry out related investment activities across multiple asset classes and product types. Applying Rule 3b-16 to an OEMS would unnecessarily disrupt the continued growth of fixed income electronic trading, which has helped to improve trading and operational efficiencies for funds, promote pre-trade price transparency, and enhance overall market liquidity, all of which have improved execution and lowered costs for investors. The

⁶ For purposes of this letter, the term “trading venue” includes a similar scope of entities as the Commission specifies in the Proposal. As proposed, a “trading venue” would mean a national securities exchange or national securities association that operates a self-regulatory organization trading facility, an ATS, an exchange market maker, an over-the-counter market maker, a futures or options market, or any other broker- or dealer-operated platform or system for executing trading interest internally by trading as principal or crossing orders as agent. *See* Proposal at 15540 (proposed definition of “trading venue” in revisions to Form ATS-N). *See also id.* at 15514 (noting that “trading venues” includes exchanges, ATSs, and single-dealer broker platforms).

consequences of disrupting this growth would include not only higher compliance burdens and costs for OEMSs and their users, but also likely less innovation in OEMS solutions. Further, we believe that subjecting OEMSs to ATS and broker-dealer regulations⁷ would not advance the Commission's goal of improving competition and leveling the playing field between trading venues, but instead would impose duplicative regulatory requirements on multiple entities without a corresponding regulatory benefit.

For similar reasons, we also request that the Commission confirm that a system or portal that an ETF sponsor uses to facilitate ETF primary market operations (*i.e.*, creation and redemption of ETF shares) is not a CPS and otherwise does not meet the definition of "exchange" based on Rule 3b-16(a), as proposed to be amended. Similar to an OEMS, we believe that the Commission did not intend for the exchange definition to apply to an ETF sponsor's system or portal. Applying the ATS and broker-dealer regulatory frameworks to ETF systems or portals would impose unnecessary additional costs and burdens to the ETF creation and redemption process, lead to unintended consequences, and would not further the Commission's regulatory objectives.

I. Background

ICI's members include US registered investment companies ("registered funds"), such as mutual funds, exchange-traded funds (ETFs), unit investment trusts (UITs), and closed-end funds, that are regulated under the Investment Company Act of 1940 ("Investment Company Act"), and non-US regulated funds⁸ (together with registered funds, "regulated funds" or "funds"), along with the advisers to these regulated funds. Advisers and regulated funds are significant participants in the US and global securities markets across equities, fixed income, and other asset classes.⁹ Well-calibrated regulation is critical to promoting the integrity and quality of these markets for advisers, funds, and the millions of investors who use advisers and funds to achieve their most important personal financial goals.

Investment advisers utilize OEMSs to carry out investment activities on behalf of funds and other clients. An OEMS, which can either be developed internally for proprietary use or provided by a third-party vendor, typically offers a range of customizable tools, functions, and services

⁷ We agree with the Commission's expectation that many CPSs would choose to comply with the conditions of the Regulation exemption from the exchange definition, which would require registering as a broker-dealer. Proposal at 15502 n.75.

⁸ "Non-US regulated funds" refers to funds that are organized or formed outside the United States and are substantively regulated to make them eligible for sale to retail investors, such as funds domiciled in the European Union and qualified under the UCITS Directive (EU Directive 2009/65/EC, as amended), Canadian investment funds subject to National Instrument 81-102, and investment funds subject to the Hong Kong Code on Unit Trusts and Mutual Funds.

⁹ At year-end 2020, funds held (i) 30 percent of US-issued equities outstanding; 15 percent of the US Treasury and government agency securities outstanding; (ii) 23 percent of bonds issued by both US corporate issuers and foreign bonds held by US residents; and (iii) 29 percent of municipal securities outstanding. ICI, Investment Company Institute Factbook at 46 (2021), available at www.icifactbook.org.

that a single end-user (e.g., an investment adviser) can customize to manage holdings across multiple asset classes and products based its own needs. Increased electronic trading in recent years has led to more innovative OEMS product offerings that promote greater market participation in traditionally less liquid markets. An OEMS allows a user to perform a broad range of complex functions across the entire investment process, including investment data research and analysis, identification of liquidity in different marketplaces, monitoring of real-time market conditions, order instruction routing to different trading venues, and post-trade processing and execution analysis. This has allowed advisers to manage investments more efficiently, enhance fund pricing practices, and reduce overall transaction costs and trading frictions, thereby enhancing the ability to attain best execution on behalf of funds and their investors. While a user could pursue each of these functions individually, an OEMS greatly increases investment and trading efficiency by allowing the user to perform these interrelated activities in an integrated and less costly manner.

II. The Commission Should Confirm That an OEMS is not a CPS or Exchange Based on Amended Rule 3b-16

We request the Commission to confirm that an OEMS, which facilitates investment management activities as described above, would not be deemed a CPS or otherwise an “exchange” under amended Rule 3b-16 based on the attributes or functions described further below. As proposed to be amended, Rule 3b-16(a) provides that an exchange:

- (i) *brings together buyers and sellers* of securities using trading interest; *and*
- (ii) makes available established, non-discretionary methods (whether by providing a trading facility or *communication protocols*, or by *setting rules*) under which buyers and sellers can interact and agree to the terms of a trade.¹⁰

While we believe that the Commission did not intend for the amended definition to apply to an OEMS, it has not clearly articulated whether it believes that such a system would meet these criteria, including whether it would constitute a “communication protocol system.”¹¹ The

¹⁰ Proposed Rule 3b-16(a) (emphasis added).

¹¹ The Commission neither clearly defines CPS nor provides parameters for what is or is not a communication “protocol,” apart from stating that a CPS would include a system that offers both “[structured] protocols and the use of non-firm trading interest to bring together buyers and sellers of securities,” Proposal at 15497 n.5, and providing a handful of non-dispositive examples. *Id.* at 15507. *See also id.* at 15500 (stating that “protocols” allow market participants to communicate with each other and negotiate a price or size of a trade). In fact, the Commission invites the broadest possible interpretation of its meaning and reinforces this approach with its own statement that it would take an “expansive view of what would constitute ‘communication protocols.’” *Id.* at 15507. As a result, we are concerned that many traditional activities not commonly understood by market participants to be activities performed by an exchange would need to be re-evaluated in light of amended Rule 3b-16. While we explain below why an OEMS itself does not provide “communication protocols,” *see infra* Section II.C, we request that the Commission provide greater clarity regarding the scope of this term.

Proposal is unclear regarding the Commission's views. When discussing a negotiation system, for example, the Commission states that "[a] system may 'scrape' or obtain the symbol of trading interest that a participant is seeking from the participant's *order management or execution management system* and use that to alert other participants on its system about potential contra-side interest in seeking to initiate a negotiation."¹² The Commission's statements regarding a negotiation system interacting with an OEMS suggests that the Commission views an OEMS as separate and distinct from a CPS and not engaged in activity subject to proposed Rule 3b-16. Other statements in the Proposal, however, appear to contradict this. In particular, the Commission states that "market participants can use [CPSs] to post and see non-firm trading interest on several trading venues simultaneously, thereby increasing their ability to find a counterparty and reduce search costs."¹³

As we explain further below, an OEMS is an investment management tool used by market participants that neither creates a marketplace nor performs functions in a manner that are commonly attributed to an exchange. The core functions of an OEMS, which include acting as a conduit to trading venues, providing users with the ability to view liquidity on those venues, and facilitating communication to those venues in accordance with each venue's methods, rules, or protocols, do not meet the key criteria in amended Rule 3b-16(a). We also explain—and seek confirmation from the Commission—that an OEMS function that facilitates internal cross trades between funds or other client accounts managed by an investment adviser or its affiliates does not constitute a "marketplace" that would be subject to ATS or exchange regulation.

A. Serving as a Conduit to Trading Venues

An OEMS does not "bring together" trading interest to create a marketplace of buyers and sellers because it enables a single end-user, *i.e.*, the investment adviser, to connect with and view trading interest that is available on different trading venues.¹⁴ When an OEMS user seeks to

¹² See Proposal at 15501 (emphasis added). Further, the Commission suggests that it is maintaining its long-held interpretation that certain types of order management and execution systems are not included in definition of an exchange. The Commission's 1998 Regulation ATS rule release specifically excluded from the interpretation of "exchange" several types of activities that could be considered traditional brokerage activities, including internal broker-dealer order management and execution systems. *Regulation of Exchanges and Alternative Trading Systems*, Exchange Act Release No. 34-40760 (Dec. 8, 1998), 63 Fed. Reg. 70844, 70852 (Dec. 22, 1998) ("Regulation ATS Adopting Release"). In the Proposal, the Commission suggests that it is not changing the scope of this existing interpretation. See Proposal at 15502 n.72.

¹³ See *id.* at 15502.

¹⁴ The Proposal is further ambiguous regarding the scope of amended Rule 3b-16 by reiterating that the Commission "w[ould] attribute the activities of a trading facility to a system if that facility is offered by the system directly or indirectly (such as where a system arranges for a third party or parties to offer the trading facility)." Proposal at 15506 (quoting the Regulation ATS Adopting Release). This suggests a scenario where one party is acting in the same manner on behalf of the other simply based on a technological connection. We are concerned that, if read broadly, this approach could lead to unintended consequences. For example, as described above, an OEMS typically replicates key data fields mandated by the trading venues to which it connects; and enables connectivity to those

interact with that trading interest, the OEMS simply acts as a communication pipeline for an adviser acting on behalf of funds and other clients. As the pipeline, the OEMS enables an adviser to transmit its instructions, including an agreement to trade, to a connected trading venue.¹⁵ While an OEMS enables users to connect to multiple external sources of liquidity, the OEMS simply allows a user to view external sources of liquidity on different trading venues and efficiently access those venues where the liquidity exists. Importantly, the actual matching of the orders or agreement to trade occurs on or through those regulated venues, not on or through the OEMS.¹⁶

B. Importing and Displaying Data Fields and Rules Set by Trading Venues

Importing and displaying parameters and fields set by connected trading venues or otherwise facilitating interaction of trading interest pursuant to trading venues' methods and/or associated rules should not cause an OEMS to be a CPS or an exchange. A typical OEMS used by an investment adviser does not "set rules" or offer "established methods."¹⁷ Rather, an OEMS merely imports the parameters and fields established by trading venues to which the OEMS user is connected into the interface presented and/or customized to the OEMS user. While the OEMS may allow the user to submit RFQs or responses to IOIs to the destination trading venue, including a communication that may signal the user's agreement to the terms of a trade, such communications or interactions are enabled strictly based on the functionality offered and supported by that connected venue and its rules or methods.

The Commission has previously indicated its support for a distinction between setting rules and importing rules set by a trading venue. In the 1998 Regulation ATS Adopting Release, the Commission stated that "rules that merely supply the means of communication within a system (for example, software or hardware tools that subscribers may use in accessing the system)" would not satisfy the "establishing non-discretionary methods" element of Rule 3b-16.¹⁸ This is precisely the functionality that an OEMS provides to a user and, thus, the Commission should reaffirm this guidance and confirm its applicability to OEMSs.

trading venues and submission of trading instructions. The Commission should clarify that mere connectivity to a trading venue and replication of the venue's data fields, without more, does not constitute indirect offering of the trading facility.

¹⁵ An OEMS does not provide access to systems or regulated trading venues with which an investment adviser (or in the case of sponsored access, the firm's broker) does not otherwise have an established relationship.

¹⁶ The Commission has previously stated that a system can constitute an exchange if buyers and sellers agree to the terms of the trade on the system. *See* Regulation ATS Adopting Release at 70852 (stating that "whether or not the actual execution of the order takes place on the system is not a determining factor of whether the system falls under Rule 3b-16"). We emphasize that such agreement and subsequent execution occur on or through the connected trading venue, pursuant to that trading venue's rules and/or protocols.

¹⁷ *See, e.g.*, Proposal at 15506-07.

¹⁸ Regulation ATS Adopting Release at 70851.

C. An OEMS Does Not Impose Its Own Communication “Protocols”

Facilitating connectivity and/or communications based on structured “protocols” set forth by connected trading venues should not cause an OEMS to be a CPS or an exchange. While an OEMS provides connectivity to trading venues, it does not itself set the protocols for trading on or through a trading venue—any such protocols typically are established by the particular trading venue to which the OEMS connects. For example, an OEMS does not impose its own structured protocols on users that circumscribe user communications, such as minimum content for messages sent or received, prescribed time periods for responding, limits on the number of messages that can be sent, or the types of securities about which a user can communicate.¹⁹

Based on these characteristics, OEMSs are “systems that provide general connectivity for persons to communicate without protocols, such as utilities or electronic web chat providers, that would not fall within the definition of exchange.”²⁰ The Commission should confirm that an OEMS that merely facilitates communications without imposing its own protocols would not be deemed a CPS or meet the amended definition of an exchange.²¹

D. Organizing, Presenting, or Displaying Trading Interest from Trading Venues

We disagree with the Commission’s view that a functionality that merely “organiz[es] the presentation of trading interest” would be a CPS. Among its functions, an OEMS enables a user to import and access information and data about real-time market conditions and available trading interest from connected trading venues. The OEMS does not provide any substantive enrichment of this content—the OEMS simply aggregates and presents the same information and data that a user could otherwise access, organize, and analyze on its own were it to connect to each trading venue separately.²² However, it would be significantly less efficient for funds and

¹⁹ See Proposal at 15507 (specifying the types of communication protocols that a CPS subject to Rule 3b-16(a)(2) may offer). As discussed above, we recommend that the Commission clarify the scope of what would constitute a “communication protocol.” See *supra* note 11. The Commission also should distinguish an OEMS from an “RFQ system.” The former typically does not establish messaging protocols or facilitate interactions of buyers and sellers on a shared system or platform, whereas the latter typically does feature communication protocols and utilize a single shared platform and, in the Commission’s view, constitutes a CPS and would be subject to amended Rule 3b-16. Proposal at 15500.

²⁰ See *id.* at 15502.

²¹ We note that an OEMS may provide a template for its user to communicate non-firm trading interest in a security to a broker-dealer platform or system via standard FIX messaging. In our view, the OEMS’s template, which allows the user to identify the security and either quantity, direction, or price, also does not constitute a “protocol.” In our view, the OEMS itself is not “setting the minimum criteria for what a message might contain,” see Proposal at 15507, but rather is facilitating communications consistent with the independently established FIX protocol, which is a series of standard messaging specifications adopted by market participants in the early 1990s to facilitate trade communications. See FIX Trading Community, *What is FIX?*, <https://www.fixtrading.org/what-is-fix/>.

²² As we noted above, advisers can otherwise access and view all of the information and data independent of the OEMS, such as through a direct feed to a trading venue or via an API.

advisers to view market activity in this manner. The mere consolidation of market data from other marketplaces is well outside the scope of functions commonly understood to be those performed by an exchange.

Further, this function is clearly distinguishable from the other examples of CPS protocols that the Commission has provided, which include protocols that (i) set minimum criteria for what messages must contain; (ii) set time periods under which buyers and sellers must respond to messages; (iii) restrict the number of persons to whom a message can be sent; (iv) limit the types of securities about which buyers and sellers can communicate; or (v) set minimums on the size of the trading interest to be negotiated.²³ Unlike an OEMS functionality that merely aggregates and displays trading interest from other trading venues for its user, these examples are trading venue protocols that govern the interaction of trading interest that can facilitate an agreement to trade. In contrast, a OEMS function that organizes, presents, or displays trading interest does not establish such parameters.

E. Facilitating Internal Cross Trades

We specifically request that the Commission clarify that an OEMS does not create a “marketplace”—and thus would not be an exchange based on amended Rule 3b-16—where it is used by an investment adviser or its affiliates to perform internal cross trades on behalf of funds and other clients.²⁴ Advisers and certain of their clients (*e.g.*, funds) or affiliates may facilitate or engage in cross trades to reduce transaction costs and increase portfolio management efficiency.²⁵ This type of transaction activity is analogous to internal portfolio ledger activity within a single firm and, importantly, does not involve using the OEMS to locate, communicate, or interact with trading interest on other trading venues. We do not perceive any regulatory benefit to applying an ATS or broker-dealer regulatory framework to this internalized trading activity, which is independently regulated. In particular, the costs of doing so, which would include broker-dealer registration and ongoing compliance with ATS and broker-dealer requirements, would frustrate advisers’ ability to seek best execution on behalf of their clients

²³ See Proposal at 15507.

²⁴ In certain circumstances, an investment adviser will facilitate internal cross trading among its clients (including funds), consistent with its fiduciary duty and applicable statutes (*e.g.*, the Advisers Act and Investment Company Act), rules (*e.g.*, Rule 17a-7 under the Investment Company Act), and Commission and staff guidance and relief.

²⁵ See ICI, *Rule 17a-7 at the Crossroads: The Right Path Forward* (Apr. 2021), available at <https://www.sec.gov/file/investment-company-institute.pdf>; ICI, *Rule 17a-7 at the Crossroads: Supplemental Information on Equity Cross Trading* (Oct. 2021), available at https://www.ici.org/system/files/2021-10/21_ppr_rule17a7_supplement.pdf.

and would not be justified to address any regulatory shortcoming or gap with respect to investor protection or market oversight.²⁶

III. Applying Amended Rule 3b-16 to an OEMS Would Not Benefit Investors

As stated above, we firmly believe the Commission did not intend for OEMSs to be subject to Rule 3b-16, as proposed to be amended.²⁷ As discussed below, including OEMSs within the scope of the rule would be detrimental to advisers, funds, and investors. The use of sophisticated OEMSs reflect the growth of electronic trading in the corporate bond and municipal markets, which has led to greater trading and operational efficiencies for funds (*e.g.*, lower search costs).²⁸ By facilitating the ability to efficiently connect to multiple trading venues and identify different pools of liquidity, we believe that OEMSs have also helped to promote greater pre-trade price transparency and overall market liquidity. These benefits have led to improved execution and lower costs for investors. Subjecting these systems to ATS and broker-dealer regulatory frameworks would undermine these benefits, impose significant costs without commensurate benefit, and likely lead to less future innovation among OEMS solutions. Further, regulating an OEMS as a broker-dealer and an ATSS would fail to achieve the Commission's goal of promoting more fair competition between trading venues and create inconsistent and duplicative regulations.

A. Applying Amended Rule 3b-16 to an OEMS Would Impose Significant Costs with No Benefit

If the Commission does not confirm that OEMSs are outside the scope of proposed Rule 3b-16, then there is a significant risk that OEMS providers may conclude that they that they need to register as broker-dealers and comply with the Regulation ATS framework. If they were to do so, these providers would be subject to higher operational, technological and compliance costs—costs that inevitably would be passed along to OEMS users—including advisers and their clients, funds, and other investors through higher trading costs. Further, a lack of regulatory certainty

²⁶ In addition, these costs are not addressed in the Economic Analysis section of the Proposal, which the Commission would be obligated to consider if amended Rule 3b-16 applied to OEMS functions that facilitate cross-trading activity. *See infra*.

²⁷ The Economic Analysis and Paperwork Reduction Act sections of the Proposal provide support for this view, as they contain no discussion of these systems, the effects on competition, or the costs or other burdens that OEMSs would incur. Under the Administrative Procedure Act, if the Commission intended proposed Rule 3b-16 to apply to OEMSs, it must address the potential effects of the Proposal on these systems. *See, e.g.*, 5 U.S.C. § 553 (requiring adequate notice and a meaningful opportunity to comment); 15 U.S.C. 78c(f) (requiring the SEC to consider whether the action will promote efficiency, competition, and capital formation); 15 U.S.C. 78w(a)(2) (requiring the SEC to consider, among other matters, the impact that any such rule would have on competition and not to adopt any rule that would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act); and 44 U.S.C. § 3507 (requiring a discussion of the full burden of complying with the proposed rule).

²⁸ 2021 ICI Letter at 6.

could cause investment advisers that develop and operate their own individual OEMSs solely for internal use to conclude that they themselves may also be subject to broker-dealer registration requirements and Regulation ATS, resulting in unnecessary regulatory costs that similarly would result in higher trading costs for their clients, including funds and investors. In either case, applying the ATS and broker-dealer frameworks would yield no meaningful benefits to market participants or investors in the form of enhanced market liquidity, greater market transparency and efficiency, or increased investor protection. Instead, it would likely lead to less pre-trade price transparency and overall market liquidity.

B. Applying Amended Rule 3b-16 to an OEMS Could Inhibit Further Innovation

Instead of providing any meaningful benefit, applying the ATS and broker-dealer framework to OEMSs would lead to a loss of trading and market efficiency benefits for advisers and create barriers to further electronic trading. As trading becomes more automated, buy-side participants such as advisers require an integrated technology solution that maximizes both trading efficiency and portfolio management capabilities across a broad range of asset classes and products. Rather than continuing to develop and offer more innovative solutions, however, OEMS providers may focus on mitigating the regulatory burdens if they were required to register as broker-dealers and comply with ATS requirements.²⁹ For example, providers may be incentivized to separate OEMS functionalities or avoid offering certain functions or features to avoid being subject relevant rules.³⁰ Applying the ATS and broker-dealer frameworks to OEMSs also may have a detrimental effect on providers' development of more innovative OEMS solutions to avoid inadvertently triggering a registration obligation, even though such solutions may allow advisers to further enhance their investment capabilities and lower trading costs. As a result, advisers would be forced to either expend additional costs and resources to develop their own proprietary front-end solutions; establish separate connections to multiple trading venues, communication tools, data feeds, and different administrative and processing programs; or even revert to bilateral trading outside of trading venues. Regardless of the ultimate outcome, regulating OEMSs in this manner would only lead to greater inefficiencies without attaining any more meaningful oversight over trading activity.

C. Applying Amended Rule 3b-16 to an OEMS Would Not Promote Competition Among Trading Venues

Regulating OEMSs as ATSs or exchanges also would not promote the Commission's goal of increasing competition and leveling the playing field among trading venues. The Commission states in the Proposal that broadening the scope of the exchange definition is intended in part to address a competitive imbalance caused by a disparity in the regulatory status of trading

²⁹ See Proposal at 15633 (similarly acknowledging that amended Rule 3b-16 could act as a "deterrent or a barrier to entry" and cause certain entities to exit the market for trading services.)

³⁰ For example, OEMS providers may separate order execution and order management functions and further scale back functionality in other ways that inhibit functionality for advisers and funds.

venues.³¹ Any such imbalance, however, is not attributable to a difference in the regulatory status of an OEMS versus a trading venue. OEMS users do not consider an OEMS to be an alternative forum for trading in lieu of trading on a regulated venue, but rather as a complementary tool to *facilitate* trading. An OEMS, in fact, *promotes* greater competition by enabling advisers and other users to efficiently connect with more than one trading venue and by augmenting a user's ability to identify liquidity available across multiple venues. Thus, regulating OEMSs as broker-dealers and ATSs would not enhance or meaningfully improve the competitive landscape for trading venues.³²

D. Applying Amended Rule 3b-16 to an OEMS Would Result in Inconsistent and Duplicative Regulation

Applying the ATS and broker-dealer framework to OEMSs would lead to inconsistent regulatory outcomes. First, as we explain above, the investment activities that an adviser can perform via an OEMS (*e.g.*, managing investment holdings, analyzing market data, and transmitting communications to connected trading venues) are activities that advisers can perform directly outside of an OEMS, albeit in a less efficient manner. The regulatory status of such activity should not differ simply because a fund or its adviser is utilizing an OEMS to invest on behalf of funds and other clients with greater efficiency and at lower cost.

Second, regulating OEMSs as ATSs would impose duplicative regulatory obligations on the OEMS and the trading venues to which it connects, with no benefit to the Commission or investors. Where messages transmitted via an OEMS lead to an agreement to a trade, that agreement occurs on or through a connected trading venue that is already regulated as an exchange, an ATS, or in the case of single-dealer systems, as a broker-dealer.³³ No enhancement to investor protection would be gained by subjecting both an OEMS and connected trading venues to a similar set of regulatory requirements. To the contrary, doing so would create regulatory uncertainty regarding which entity has a particular regulatory obligation and could result in unnecessary and confusing duplication. For example, if an OEMS were required to register as an ATS, it is unclear whether the OEMS or the connected trading venue, or both, would bear certain regulatory responsibilities such as FINRA trade reporting. This uncertainty

³¹ Proposal at 15498.

³² Rather than enhance competition, we have concerns that regulating OEMSs as broker-dealers and ATSs could instead further limit competition. For example, trading venues with broker-dealer and ATS status may seek to limit the ability of other ATSs, *i.e.*, OEMSs that provide users with connectivity to multiple other trading venues, to connect to their platforms; such venues may instead require users to connect to their platform on a direct basis. Given the increased costs and inefficiency of this approach, users may be compelled to limit the number of trading venues to which they connect, which would harm competition among venues and impair overall market liquidity.

³³ To the extent that there are trading venues that are currently not subject to regulation, *e.g.*, RFQ systems, we note that such venues would be subject to regulation pursuant to amended Rule 3b-16. *See supra* note 19 (noting the distinction between OEMS systems and RFQ systems based on, among other things, the presence of "communication protocols").

would instead lead to confusion among OEMS providers and users, as well as reporting inconsistencies, which could ultimately impair the quality of market data available to the Commission, FINRA, and other market participants. Further, the Proposal does not consider the costs of imposing duplicative and overlapping requirements if OEMSs were subject to a registration obligation. It is clear, however, that the costs of compliance—borne ultimately by investors in the form of higher trading costs—would far outweigh any potential conceivable benefit.

IV. The Commission Should Confirm That an ETF Primary Market System is Not a CPS or Exchange Based on Amended Rule 3b-16

We request that the Commission also confirm that it would not deem a system or portal that an ETF sponsor uses to facilitate ETF primary market transactions (*i.e.*, creations and redemptions of ETF shares) as a CPS or otherwise as an exchange based on amended Rule 3b-16. An ETF sponsor may utilize such a system or portal to enable registered broker-dealers that serve as an ETF's authorized participants (APs) to place automated creation or redemption requests with the fund.³⁴ As part of the creation or redemption process, the sponsor and the APs use systems or portals to communicate with one another about different aspects of an ETF basket, including its component securities and pricing.³⁵ Similar to an OEMS system, this system or portal may facilitate connections to trading venues to facilitate AP functions and provide other related ancillary functions, such as pricing research, in-kind transaction processing and settlement, and portfolio risk analysis. Importantly, an ETF sponsor's system or portal is limited in several important respects: (i) the scope of ETFs involved in the creation or redemption process is confined to those offered by the ETF sponsor; (ii) only registered broker-dealers that have an established agreement with an ETF sponsor's ETF to act as an AP can submit creation or redemption requests to the ETF; and (iii) the system or portal does not directly facilitate secondary market activity in the ETF (*i.e.*, trading of the actual ETF shares among individual investors), nor does it provide access for individual investors that are not registered broker-dealers.

³⁴ For a more detailed explanation of the role of APs in the primary market for ETF shares, see ICI, *Understanding the Regulation of Exchange-Traded Funds Under the Securities Exchange Act of 1934* at 4 (Aug. 2017), available at https://www.ici.org/system/files/attachments/ppr_17_etf_listing_standards.pdf. See also ICI, *The Role and Activities of Authorized Participants of Exchange-Traded Funds* (Mar. 2015), available at https://www.ici.org/pdf/ppr_15_aps_etfs.pdf. For purposes of this discussion, an ETF sponsor, which includes affiliated entities, may use the system or portal to facilitate primary market operations on behalf of different funds in an ETF suite.

³⁵ Fixed income ETFs, for example, may contain such a large number of bonds that precludes an AP from delivering a pro-rata portion of each bond to the ETF sponsor to fulfill an ETF share creation request. In this scenario, an ETF sponsor may use the system or portal to communicate to the AP a targeted subset of bonds that it would likely accept as part of the creation request. The AP may also use the system or portal to propose a subset of bonds, including pricing of those components, to the ETF sponsor for its acceptance.

Similar to an OEMS, we believe that the Commission did not intend for the exchange definition to apply to an ETF sponsor's system or portal and seek clarification that this is not the case. These systems or portals do not create a marketplace for secondary market trading activity and are used by ETF sponsors individually for a specific purpose—to create and redeem their own issued securities. In this respect, we believe that this type of system or portal is similar to a system that allow issuers to sell their own securities to investors, which the Commission proposes to exclude from the scope of Rule 3b-16(a).³⁶ They allow sponsors to efficiently communicate with their APs and reduce operational risks associated with these processes.

Applying the ATS and broker-dealer regulatory frameworks would impose unnecessary additional costs and burdens to this process and lead to unintended consequences. Imposing unnecessary burdens on ETF creations and redemptions, for example, could alter AP behavior and adversely impact secondary market liquidity for ETF investors through wider spreads and higher trading costs. Applying the ATS and broker-dealer frameworks to these systems also would not advance the Commission's goal of enhancing competition among trading venues and likely would impede further innovation in technology solutions for ETFs. Further, we question the necessity or regulatory benefit of layering ATS and broker-dealer regulations on top of the Commission's existing framework for ETFs.³⁷

* * *

We welcome the opportunity to engage with the Commission to develop a carefully crafted regulatory framework that encourages growth and innovation and is appropriately tailored to promote transparency, investor protection, and resiliency. If you have any questions, please contact Sarah Bessin at 202-326-5835 or Nhan Nguyen at 202-326-5810.

Regards,

/s/ Sarah A. Bessin

Sarah A. Bessin

Associate General Counsel

³⁶ The Commission continues to believe that this latter type of system does not bring together multiple buyers and multiple sellers. Proposal at 15506.

³⁷ For example, imposition of both Regulation ATS and recordkeeping and reporting requirements would be duplicative and unnecessary. Rule 6c-11, which establishes Commission oversight over ETF activity, already requires ETFs to, among other things, have written policies and procedures surrounding ETF baskets, 17 C.F.R. 240.6c-11(c)(3), and records detailing the composition of each basket. 17 C.F.R. 240.6c-11(d).

Ms. Vanessa A. Countryman

April 18, 2022

Page 15

/s/ Nhan Nguyen

Nhan Nguyen

Assistant General Counsel

cc: The Honorable Gary Gensler
The Honorable Hester M. Peirce
The Honorable Alison H. Lee
The Honorable Caroline A. Crenshaw

Haoxiang Zhu, Director, Division of Trading and Markets
David Shillman, Associate Director, Division of Trading and Markets
Tyler Raimo, Assistant Director, Division of Trading and Markets

Securities and Exchange Commission