August 30, 2021

Via Electronic Submission

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Request for Exemptive Relief Pursuant to Rule 612(c) of Regulation NMS to Permit a Minimum Increment of $0.005 in "Tick Constrained" NMS Stocks

Dear Ms. Countryman:

MEMX LLC ("MEMX") respectfully requests that the U.S. Securities and Exchange Commission ("Commission") exercise its exemptive authority under Rule 612(c) of Regulation NMS to permit market participants to display, rank, and accept bids or offers, orders, and indications of interest in an increment of half of one cent ($0.005) in "tick constrained" NMS stocks that trade with an average quoted spread of 1.1 cents or less.[1] As explained herein, Rule 612 of Regulation NMS (the "Sub-Penny Rule"), which imposes a minimum increment of one cent on thousands of equity securities with different trading characteristics has resulted in artificially wide quotes in a number of actively-traded, often low-priced, securities. Quoting in these securities is limited not by supply and demand, but rather by outdated regulatory constraints, harming public price discovery and increasing transaction costs paid by investors. The requested exemption would allow market participants, including national securities exchanges, national securities associations, alternative trading systems, vendors, and brokers or dealers, to implement a more appropriate

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1 Today, orders are also permitted to be priced at the midpoint of the national best bid and offer ("NBBO"). We ask that the Commission continue to permit this practice and allow orders to be priced at the NBBO midpoint in an increment of $0.0025 for any NMS stock that is quoted in a $0.005 increment consistent with the requested exemption.

trading increment in securities where the current increment is demonstrably too wide and imposes unnecessary costs on investors that rely on the U.S. equity markets for their investing needs.

Background

The Sub-Penny Rule prohibits national securities exchanges, national securities associations, alternative trading systems, vendors, and brokers or dealers from displaying, ranking, or accepting from any person a bid or offer, an order, or an indication of interest in any NMS stock priced in an increment smaller than $0.01 if that bid or offer, order, or indication of interest is priced equal to or greater than $1.00 per share.[2] Rule 612(c) further gives the SEC authority to grant exemptions from the requirements of the Sub-Penny Rule if doing so is the public interest and consistent with the protection of investors.[3] Specifically, Rule 612(c) provides that the Commission may exempt from these requirements "any person, security, quotation, or order, or any class or classes of persons, securities, quotations, or orders, if the Commission determines that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors."[4] In fact, following the adoption of Regulation NMS the Commission has previously granted an exemption from Rule 612 in several instances where such exemption was necessary and appropriate in the public interest.[5] MEMX believes that an exemption is similarly necessary and appropriate for quoting in tick constrained NMS stocks given the harmful economic

2 17 CFR § 242.612(a).

3 17 CFR § 242.612(c).

4 Id.

5 See, e.g., Securities Exchange Act Release Nos. 67347 (July 3, 2012), 77 FR 40673 (July 10, 2012) (SR-NYSE-2011-55; SR-NYSEAmex-2011-84) (approving retail liquidity programs for both NYSE and NYSE Amex on a pilot basis and granting a limited exemption to the Sub-Penny Rule); 85160 (February 15, 2019), 84 FR 5754 (February 22, 2019) (SR-NYSE-2018-28) (approving the NYSE retail liquidity program on a permanent basis and granting a limited exemption to the Sub-Penny Rule).

impact of the current minimum increment on displayed spreads in almost one thousand equity securities that together account for 47% of volume, 28% of trades, and 25% of notional value executed in the U.S. equity markets.

Request for Exemptive Relief

As discussed, MEMX respectfully requests that the Commission exercise its exemptive authority pursuant to Rule 612(c) to permit any national securities exchange, national securities association, alternative trading system, vendor, and broker or dealer[6] to display, rank, and accept bids and offers, orders, or indications of interest in tick constrained NMS stocks in an increment of $0.005 if that bid or offer, order, or indication of interest is priced equal to or greater than $1.00 per share.[7] The requested exemption would apply to NMS stocks that traded with an average quoted spreads of 1.1 cents or less during the prior calendar month.[8] As described in the following section, MEMX also requests that as a condition of such relief the Commission require that any national securities exchange, national securities association, or other trading center subject to Rule 610(c) limit access fees under that rule to $0.0015 for tick constrained NMS stocks.

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6 The requested exemption would apply to any trading center subject to the Sub-Penny Rule. However, each trading center would have to determine whether they would choose to offer a $0.005 increment to their customers. As a practical matter, MEMX believes that the majority of trading centers would choose to implement this smaller increment in order to be able to offer improved executions to customers trading on their venue.

7 Rule 612(b) establishes a smaller minimum increment of $0.0001 for bids or offers, orders, or indications of interest priced less than $1.00 per share. 17 CFR § 242.612(b). Therefore, MEMX's requested exemption would be limited to quoting at or above $1.00.

8 When the Commission's market data infrastructure rule is implemented, round lot sizes would similarly be adjusted on a monthly basis. See Securities Exchange Act Release No. 90610 (December 9, 2020), 86 FR 18596 (April 9, 2021). Following a similar schedule for the requested tick size exemption could minimize complexity around such changes.

When the Commission adopted the Sub-Penny Rule, it acknowledged the possibility that the "balance of costs and benefits" [9] that animated this regulation "could shift in a limited number of cases or as the markets continues to evolve."[10] The Commission also further discussed the circumstances under which it may be appropriate for it to provide relief pursuant to Rule 612(c), noting that the following considerations would be relevant to its analysis under that rule: (1) whether the security "always trades with a penny spread and there is tremendous liquidity available on both sides of the market;"[11] (2) "[w]hether the NMS stock is an ETF or other derivative that can readily be converted into its underlying securities or vice versa, in which case the true value of the security as derived from its underlying components might be at a sub-penny increment;"[12] (3) "[l]arge volume of sub-penny executions in that security due to price improvement;"[13] and (4) "[l]ow price of the security."[14] A recent analysis of these factors conducted by MEMX shows that exemptive relief is warranted to remedy the impact of tick constraints on trading in NMS stocks.[15]

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9 See Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37553 (June 29, 2005) ("Regulation NMS Adopting Release").

10 Id.

11 Id at 37554.

12 Id.

13 Id. This exemption request and supporting material do not include an analysis of this factor as trades in sub-penny increments are likely to be indicative of retail internalization as opposed to market participants seeking to trade within a tick constrained spread.

14 Id.

15 See *Tick Constrained Securities, Why GE's Basis Point Spread was Four Times Higher Before its Reverse Split and What We Should Do About It*, Adrian Griffiths, MEMX ("MEMX White Paper").

As detailed in the attached white paper,[16] which we incorporate herein by reference,[17] the factors listed by the Commission in the Regulation NMS adopting release weigh in favor of granting a targeted exemption pursuant to Rule 612(c) for tick constrained NMS stocks. Specifically, the following factors, each of which were discussed by the Commission when it adopted the Sub-Penny Rule, weigh heavily in favor of granting such exemptive relief: (1) almost one thousand NMS stocks accounting for nearly half of all volume and about a quarter of all trades and notional value traded on a daily basis are tick constrained, meaning that they consistently trade with a penny spread; (2) such tick constrained NMS stocks trade with "tremendous"[18] liquidity at the NBBO as quoting activity is forced to cluster at the minimum increment instead of more aggressive prices that would offer improved economics to investors;[19] and (3) tick constraints occur frequently and are most impactful in (A) low-priced NMS stocks where a one cent spread is more economically significant in relation the price of the security,[20] and (B) ETPs whose prices

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16 Id.

17 A detailed analysis of available data and other factual support for our request for exemptive relief is provided in the attached white paper. Id.

18 See supra note 11 and accompanying text.

19 Tick constrained NMS stocks frequently trade with notional at the NBBO that is many times what we observe in other NMS stocks with similar levels of trading activity. See MEMX White Paper, supra note 15. For example, on the day before its reverse split, GE, which was then still a tick constrained stock, traded with more than $1.4 million notional at the NBBO, ranking it above nine of the ten most actively traded symbols that day by notional value executed despite the fact that GE traded only a fraction of the trading activity seen in those much more active names. Id.

20 Although there are tick constrained NMS stocks across the price spectrum, two-thirds (66%) of tick constrained NMS stocks trade between $1 and $20 per share, and these securities have the worst basis point spreads. Id.

can be appropriately derived from their underlying constituents.[21] Ultimately, tick constraints reduce market quality in a large segment of the market for U.S. equity securities, impede the public price discovery process, and cost investors money in the form of increased transaction costs.

Moreover, as required by Rule 612(c), granting the requested exemption would be in the public interest and consistent with the protection of investors. Trade commissions and other explicit costs of trading have gone down significantly in the decade and a half since Regulation NMS was first implemented. However, minimizing the implicit costs of trading, *e.g.*, spread costs, remains important to investors seeking best execution. When the Commission adopted Regulation NMS it recognized the importance of reducing such costs, noting that "[t]he transaction costs associated with the prices at which [investor] orders are executed represent a continual drain on their long-term savings"[22] and that "[m]inimizing these investors costs to the greatest extent possible is the hallmark of efficient markets, which is a primary objective of the NMS."[23] Today, the Sub-Penny Rule itself imposes significant costs on investors by keeping spreads artificially wide. Allowing these securities to instead trade with a $0.005 increment would reduce transaction costs and facilitate more robust price discovery by enabling liquidity providers to post more aggressive quotations within the current penny spread seen in these tick constrained NMS stocks. Further, given the significant amount of trading that occurs in these securities, the potential savings are likely substantial and would meaningfully improve the experience of the investing public.

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21 MEMX's data shows that more than half of equity ETPs and the vast majority of fixed income, commodity, and other ETPs trading at least 100 million notional each day are tick constrained. Id.

22 Regulation NMS Adopting Release, *supra* note , at 37498.

23 Id.

Finally, such exemptive relief could be granted without jeopardizing the objectives of the Sub-Penny Rule as the Commission's rationale for imposing restrictions on sub-penny quoting do not apply to tick constrained NMS stocks. The Sub-Penny Rule was primarily designed "to limit the ability of a market participant to gain execution priority over a competing limit order by stepping ahead by an economically insignificant amount."[24] This concern is not relevant to tick constrained NMS stocks, which are instead characterized by the opposite problem – *i.e.*, a complete lack of price competition. When a security trades with a consistent penny spread, market participants that may be willing to improve displayed prices and contribute to public price discovery are unable to do so for any amount, regardless of how economically significant. Indeed, evidence of the impact of a uniform one cent minimum increment for all NMS stocks quoted at or above $1.00 shows that what is "economically significant" varies based on factors such as the price of the security that are not taken into account under the current regulatory structure. Rather than facilitating "stepping ahead,"[25] allowing a smaller increment in tick constrained securities would instead promote beneficial price competition that is currently hindered by regulation.

Conditions for Exemptive Relief

Rule 612(c) also provides that the Commission may choose to exercise its authority to grant exemptions "either unconditionally or on specified terms and conditions."[26] MEMX respectfully requests that the Commission condition any relief granted pursuant to this request on any national securities exchange, national securities association, or other trading center subject to Rule 610(c) limiting access fees under that rule to $0.0015 in any tick constrained NMS stocks trading in

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24 Id at 37551.

25 Id.

26 17 CFR § 242.612(c).

$0.005 increments. The minimum increment established pursuant to the Sub-Penny Rule is intimately tied to the access fee cap pursuant to Rule 610(c), which generally imposes a maximum access fee of $0.003 per share if the price of a protected quotation or other quotation of a trading center subject to the rule is $1.00 or more. While the current access fee cap continues to be appropriate for NMS stocks trading with a one cent minimum increment, a lower fee cap may be necessary in connection with an exemption that permits certain NMS stocks to trade in $0.005 increments, as any fee charged to access quotations in such securities would make up a commensurately larger proportion of the spread. Reducing the access fee cap as a condition of any relief granted pursuant to Rule 612(c) would prevent market distortions that may occur in situations where access fees are allowed to exceed half of the minimum trading increment – *i.e.*, by limiting situations where an exchange quoting at the best price may not actually provide the best "all-in" economics when accounting for both fees paid and rebates provided by different venues.[27] In addition, it would further reduce transaction costs for investors in securities that are likely to be quoted efficiently without additional economic incentives for adding liquidity.[28]

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Accordingly, for the reasons discussed in this request for exemptive relief and the attached white paper on tick size reform, MEMX respectfully request that the Commission exercise its exemptive authority pursuant to Rule 612(c) to permit a minimum increment of $0.005 for tick constrained NMS stocks, subject to the conditions described herein.

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27 Although the access fee cap pursuant to Rule 610(c) does not explicitly limit rebates provided by trading centers, it imposes a practical limitation on rebates as the amount that can be recouped by the trading center is limited by the access fee that it can charge.

28 Based on our estimate of average take fees charged by different exchanges, potential savings may be as much as $879 million annually if each exchange with a take fee of more than $0.0015 were to reduce the take fee to this level in tick constrained securities.

Sincerely,

/s/ Adrian Griffiths

Adrian Griffiths
Head of Market Structure