



**“Market Structure and the Retail Investor”
SEC Chair Gensler Remarks Before the Piper Sandler Global Exchange Conference
June 8, 2022**

Summary of Prepared Remarks and Conference Q&As

On June 8, 2022, SEC Chair Gensler delivered remarks at the Piper Sandler Global Exchange and FinTech Conference, laying out a framework for long-awaited SEC reforms to equity trading and market structure. The speech, entitled “[Market Structure and the Retail Investor](#),” covered a wide variety of topics and was followed by several live Q&As from Rich Repetto at Piper Sandler. A summary of Chair Gensler’s prepared remarks and the Q&As follows below, and a video of the speech can be found [here](#).

Prepared Remarks

Background

Chair Gensler noted that while technology has transformed (and continues to transform) the equity markets, and has led to some beneficial things such as allowing retail investors greater access to the markets, this “technological transformation” also has led to challenges, including market segmentation, concentration, and potential inefficiencies.

Chair Gensler focused on what he sees as the lack of a level playing field among different parts of the market - specifically wholesalers, dark pools, and lit exchanges – and concerns around markets that have become “increasingly hidden from view” and the routing of the majority of retail marketable orders “to a small, concentrated group of wholesalers that pay for this retail market order flow.” He noted that “[i]t’s not clear, with such market segmentation and concentration, and with an uneven playing field, that our current national market system is as fair and competitive as possible for investors.”

With that said, Chair Gensler stated that he has asked SEC staff to “take a holistic, cross-market view of how we could update our rules and drive greater efficiencies in our equity markets, particularly for retail investors.” Chair Gensler then broke down the issues he would like to see addressed across six areas:

- Minimum Pricing Increment
- National Best Bid and Offer
- Disclosure of Order Execution Quality
- Best Execution
- Order-by-Order Competition
- Payment for Order Flow, Exchange Rebates, and Related Access Fees

Minimum Pricing Increment (i.e., Tick Sizes)

Chair Gensler noted that tick sizes is one example of the lack of a level playing field among the different trading venues, *i.e.*, investors see prices in lit markets in one-penny increments and wholesalers can fill orders at sub-penny prices and “without open competition.” He stated that given the volume being executed in sub-pennies off-exchange, the constraints of the lit markets “raises real questions about whether this structure is fair and best promotes competition” and, in the live version of the speech asked “why not allow all venues to have equal opportunity to execute at sub-penny increments.”

Chair Gensler stated that he therefore has asked SEC staff to make recommendations for the Commission’s consideration around leveling the playing field with respect to two facets of tick sizes: (1) possibly harmonizing the tick size across different market centers such that all trading occurs in the minimum increment regardless of market center; and (2) possibly shrinking the minimum tick size to better align with off-exchange activity.

National Best Bid and Offer (NBBO)

Chair Gensler asked staff to consider three issues related to the NBBO; accelerating the first two, according to Chair Gensler, would allow retail investors to better understand prices sooner:

- Accelerate implementation of the new round lot definition (as discussed and adopted in the Market Infrastructure Rule) given the increase in the amount of odd lots in the markets. Chair Gensler stated that retail investors are more likely to buy or sell at odd lot prices, but at the same time are unable to see these prices.
- Accelerate implementation of the piece of the Market Infrastructure Rule that enhances transparency for quotation information around odd lots.
- Consider whether there should be an odd-lot best bid and offer so that investors would know the best price available in the market regardless of share quantity.

Disclosure of Order Execution Quality

Chair Gensler stated that there is a need to enhance retail investors’ ability to compare execution quality by their brokers. He noted that retail investors today cannot compare execution across brokers, such as how much price improvement they provide to their clients, as such brokers are not required to provide these disclosures on monthly Rule 605 reports. Chair Gensler therefore asked SEC staff to make recommendations on how the Commission can update Rule 605 so that investors receive “more useful disclosure about order execution quality” and whether to require that “all reporters provide summary statistics of execution quality, such as the price improvement as a percentage of the spread.”

Best Execution

Chair Gensler stated that he thinks that “investors might benefit if the SEC considered proposing its own best execution rule” and that broker-dealers and investors might benefit from more detail around the procedural standards brokers must meet when handling and executing customer orders. He therefore has asked SEC staff to consider recommending that the SEC propose its own best execution rule for equities, as well as for other securities.

Order-by-Order Competition

Chair Gensler discussed how best to promote as much competition as possible for retail investors on an order-by-order basis. Specifically, he reiterated his comments on the segmentation in the markets and added that “this segmentation means that institutional investors, such as pension funds, don’t get to interact directly with [retail] order flow” and segmentation, which isolates retail market orders, “may not benefit the retail public as much as orders being exposed to order-by-order competition.”

In response to suggestions that the current segmentation allows retail investors to receive slightly better prices compared to the NBBO, Chair Gensler stated that “[p]rice improvement without competition, though, isn’t necessarily the best price improvement” and that “[w]holesalers may be saving more than they’re passing along to investors in terms of price improvement.”

Chair Gensler therefore asked SEC staff to make recommendations around how to enhance order-by-order competition, possibly through “open and transparent auctions or other means, unless investors get midpoint or better prices.”

Payment for Order Flow, Exchange Rebates, and Related Access Fees

Chair Gensler stated that “payment for order flow can raise real issues around conflicts of interest” and that exchange rebates also may present conflicts in the routing of customer limit orders. In the context of retail brokers, he noted in the live portion of his speech that “zero commissions does not mean zero costs to the retail public.”

Chair Gensler therefore asked SEC staff to make recommendations around how to mitigate such conflicts including: (1) consideration whether exchange fees (*e.g.*, access fees) and rebates should be more transparent so that investors can understand these amounts at the time of trade execution and (2) how access fees might change in light of a potentially lower minimum tick size, *i.e.*, if the minimum pricing increment is reduced, it may also be appropriate to reduce access fee caps proportionately.

Questions and Answers

There was a brief Q&A session with Chair Gensler at the end of his prepared remarks. For the most part, Chair Gensler reiterated many of the comments made in his prepared remarks and did not add to what had already been stated.

1. **Order-by-Order Competition:** What might order-by-order competition look like under the outlined reforms, and is PFOF prohibited or would it continue to exist?

Chair Gensler did not get into any further specifics on the topic and stated that he did not want to get ahead of his fellow Commissioners or the staff on the issue; he just thought it would be helpful through his speech to put out what the Commission was considering. He reiterated what he asked the staff to look at, particularly how to inject competition regarding retail orders to address the segmentation that now exists. He acknowledged that there is some price improvement provided to retail investors but not as much as people think, that competition can be provided through the auction mechanism, and that we should learn from the options markets what may or may not work in this area.

In terms of PFOF and exchange rebates, he reiterated that they present inherent conflicts of interest and noted that other jurisdictions are considering getting rid of them, so he continues to ask SEC staff what the Commission should do in the area. Chair Gensler added that as the SEC puts this all together, they will put potential reforms out for notice and comment to hear from the public as well.

2. **State of the US Retail Market:** Many regard the US retail market as highly efficient. Is there any data to suggest that the auction process will be better or result in economic benefits that make the process better, does the SEC plan to do any pilot tests, and is the SEC concerned that the reforms can have an impact on the low (or nil) pricing that e-brokers charge?

Chair Gensler stated that the issue around pricing that e-brokers charge is misleading, *i.e.*, there is a cost to retail of the current system, and the cost is that two or three highly concentrated market makers are buying retail order flow. He added that though there might be some price improvement “against a poorly put together measuring rod” (*i.e.*, the NBBO), that does not mean that it is full price improvement or best execution. Chair Gensler also reiterated his comments around the issue of institutional investors not having access to that retail flow and questioned whether this is the best capital markets. Chair Gensler noted that anything that would be proposed would have economic analysis included.

3. **Timeline:** What is the real timeline behind what is being suggested, and would the SEC be open to a roundtable discussion (which the SEC has held in the past)?

Chair Gensler stated that there are lots of ways to get public input, and that the SEC has been seeking input all along. He noted that this is not a proposal - it is the Chair’s speech - and that he is not speaking on behalf of the staff or the Commissioners. Chair Gensler invited public comment on what the SEC will put out for public comment, and encouraged people to continue to engage with the staff and the Commission overall.

4. **Market Infrastructure Rule:** You [Chair Gensler] discussed the Market Infrastructure Rule, and specifically the odd lot portion of the Rule - do you expect to implement this and other parts of the Rule over the next year or so?

Chair Gensler did not directly address the timeline except to note that the Rule was recently upheld by the courts (and litigants still need to decide what to do). He did note that all of this is similar to what he is discussing - the Rule was about competition relating to market data and all the issues he is discussing is about how to use the benefits of competition to drive greater efficiency in our capital markets. Chair Gensler also reiterated comments on the round lot/odd lot issue and noted that it would be through a notice and comment process to see if the SEC should accelerate those portions of the Market Infrastructure Rule.

5. **Auctions:** Would ideas around auctions that were addressed cover, or preclude, large banks that have internalization of orders?

Chair Gensler did not address the question directly except to say that he is not trying to prejudge the staff on where the Commission may come out on everything.