

# DOJ Antitrust Division Cautions SEC on Proposed Equity Market Restructuring

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On April 11, 2023, the Antitrust Division of the United States Department of Justice (the “DOJ”) [issued](#) a public comment on four proposed rules promulgated by the United States Securities and Exchange Commission (“the SEC”). The four proposed rules target national market system (“NMS”) stocks by (1) expanding disclosures of order execution information (“Rule 605 Proposal”);<sup>[1]</sup> (2) amending minimum pricing increments, access fees, and transparency requirements (“Regulation NMS Proposal”);<sup>[2]</sup> (3) enhancing competition for certain orders (“Order Competition Proposal”);<sup>[3]</sup> and (4) establishing a duty of best execution for certain market participants (“Best Execution Proposal”).<sup>[4]</sup> The DOJ’s comment warns the SEC of the possible negative interactions between the four proposed rules and the antitrust dangers of issuing the rules all at once.

## The Proposed Rules

### A. The Rule 605 Proposal

For background, Rule 605 requires certain entities to make available monthly public reports describing the execution quality of their NMS stocks. The SEC [proposes](#) to expand the list of entities subject to Rule 605 to include (1) broker-dealers who introduce or carry 100,000 or more customer accounts; (2) single-dealer platforms; and (3) entities that would operate proposed qualified auctions. The SEC also seeks to update the scope and content of the monthly reports by (1) expanding the definition of “covered order” to include certain additional orders and order types; (2) modifying the existing order size categories to base them on round lots rather than number of shares, and including additional order size categories for fractional share, odd-lot, and larger-sized orders; and (3) creating a new order type category for marketable immediate-or-cancel orders, and replacing three existing categories of nonmarketable order types with three new categories of order types. The monthly reports would also need to include (1) average time to execution, median time to execution, and 99th percentile time to execution statistics; (2) realized spread statistics that would be required to be calculated after both 15 seconds and one minute; and (3) new statistical measures of execution quality.

### B. The Regulation NMS Proposal

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The SEC [proposes](#) to amend the minimum pricing increments (also known as tick sizes), currently at \$.001, to smaller sub-penny increments that are determined by liquidity and price competition. The SEC also seeks to lower the fee cap that trading centers can charge for executing orders against certain types of quotations and require national securities exchanges to make the amounts of all fees and rebates determinable at the time of execution. The proposal updates the definition of “round lots” and “odd lots”, which are ways to categorize quantities of stocks when quoting prices.

### **C. The Order Competition Proposal**

This [proposal](#) designates certain NMS stock orders by individual investors as “segmented orders” that must be subject to a competitive auction process before the orders can be executed. Currently, retail brokers send more than 90% of marketable orders to wholesalers. These wholesalers typically execute these orders internally without providing any opportunity for competition with other market participants. By requiring an open and fair marketplace for these kinds of stock orders, the SEC claims that it seeks to promote competition and enhance transparency.

### **D. Best Execution Proposal**

This [proposal](#) establishes a best execution standard for brokers, dealers, government securities brokers, government securities dealers, and municipal securities dealers. This duty requires a broker-dealer to execute customers’ trades at the most favorable terms reasonably available under the circumstances. Broker-dealers are required to establish, maintain, and enforce written policies and procedures reasonably designed to comply with the best execution standard. They are also required to generally consider including the level of competition of a market as an element of its best execution policies and procedures.

## **The DOJ’s Concerns**

The DOJ applauded the efforts of the SEC to promote competition by promulgating the four proposed rules. The comment noted that the Order Competition Proposal promotes transparency and competition, and smaller minimum increments allow exchanges to compete more effectively for order flow. However, the DOJ urged the SEC to consider ways that these rules could interact with one another. As an example, DOJ hypothesized that tick-size reductions could move stock orders from wholesalers to exchanges, which would then reduce the number of orders that are subject to auctions under the Order Competition Rule. Because the Best Execution Proposal requires broker-dealers to consider the level of competition as an element of its policies, broker-dealers will have to take into account auctions conducted pursuant to the Order Competition Rule and consider the competitive dynamics of those auctions compared to other ways to execute clients’ orders.

In President Biden’s [Executive Order](#) on Competition, all agencies are called to coordinate with one another to adopt procompetitive regulations under the “whole-of-government” approach. This includes sharing an agency’s respective expertise with other agencies to improve government efficiency and promote competition. The DOJ cited this approach as justification for issuing the public comment.

## **Takeaways**

The DOJ’s public comment on the SEC’s proposed rules for equity markets show its commitment to competition advocacy and ensuring all federal agencies consider competition within their jurisdictions.

The DOJ's public comments seem to suggest a lack of pre-issuance coordination between SEC and DOJ. Under Biden's "whole of-government" approach to promoting competition and improving efficiency, we would have expected DOJ's input before the SEC published its proposed rules. It will be interesting to see if the SEC responds to the DOJ, makes substantive changes in its final rule, or strengthens coordination with the DOJ in future rulemaking proceedings.

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## FOOTNOTES

[1] Disclosure of Order Execution Information, 88 Fed. Reg. 3786 (Jan. 20, 2023) ("Rule 605 Proposal").

[2] Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, 87 Fed. Reg. 80,266 (Dec. 29, 2022) ("Regulation NMS Proposal").

[3] Order Competition Rule, 88 Fed. Reg. 128 (Jan. 3, 2023) ("Order Competition Rule Proposal").

[4] Regulation Best Execution, 88 Fed. Reg. 5440 (Jan. 27, 2023) ("Regulation Best Execution Proposal").

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