

BETTER MARKETS

– FACT SHEET –

What You Need to Know About Citadel's Role in the Robinhood and the GameStop Saga

February 16, 2021

Trading anomalies in GameStop and other so-called “Reddit Rebellion” equities have brought attention to longstanding equity market structure issues. In the course of reporting on these events, the media has identified what may be an unfamiliar financial firm at the center of multiple aspects of the recent trading frenzy: Citadel Enterprise Americas, LLC (“Citadel”)—a global financial group with multiple prominent entities, including a \$33 billion hedge fund group, managed through Citadel Advisors, LLC (“CA”), and a proprietary trader, market-maker, and wholesale broker-dealer, Citadel Securities, LLC (“CS”), that executes much of the retail order flow from Robinhood and other retail broker-dealers.¹

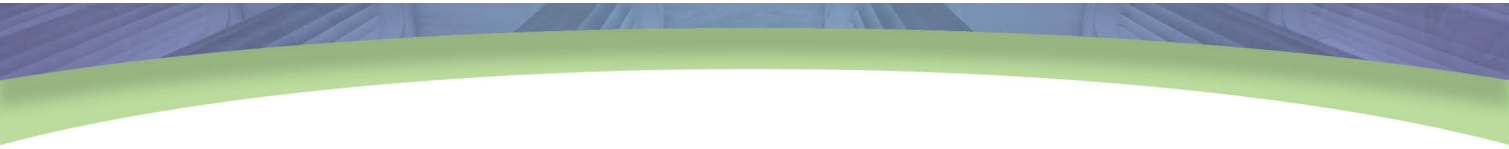
This brief fact sheet is meant to provide a very high-level introduction to Citadel and its multiple roles in the U.S. financial system and the GameStop trading frenzy.

Citadel's most relevant businesses to the GameStop events are its \$33 billion hedge fund group, managed through CA, and its market-maker and wholesale broker-dealer, CS.

Citadel was founded in 1990 by 21-year-old, Kenneth Griffin, and it has since become a prominent player in the global financial system. Its most relevant businesses for present purposes are (1) its [\\$33 billion hedge fund group, managed through CA](#); and (2) [its market-maker and wholesale broker-dealer, CS](#), which executes approximately 26% of U.S. equities volume across 8,900 U.S.-listed equities, executes approximately 47% of all U.S.-listed retail volume, and represents 99% of traded volume in 3,000 U.S.-listed options names. CS is active in every asset class, including commodities and derivatives markets. Citadel's footprint in and importance to the U.S.'s financial markets would be hard to exaggerate. In fact, the Financial Stability Oversight Council should consider designating at least CS as systemically important, given its market presence and the adverse consequences that would accompany any disruption to its trading and related activities.

Citadel's present hegemony among high frequency traders (“HFTs”) is all the more remarkable given the fact that [it nearly failed in the midst of the 2008 financial crisis](#). A little more than a decade later, Citadel is one of the largest and most successful hedge funds, proprietary trading outfits, and wholesale broker-dealers across the financial markets, reportedly earning Griffin, the chief executive officer and chief investment officer, [\\$1.5 billion in 2019](#) alone. In total, Griffin's [net worth is estimated to be \\$21.4 billion](#), reportedly making him the 28th wealthiest person in the United States. The Citadel hedge fund group's flagship Wellington Fund reportedly earned [returns of 24%](#) in 2020, while CS earned [\\$6.7 billion in net trading revenue](#) in 2020.

¹ Citadel's corporate structure, like most financial conglomerates, has evolved over time. Unlike many financial conglomerates, much of Citadel's business structure is not public, so the noted legal entities reflect the best understanding of the current structure that can be gleaned from the available public information.



Citadel was involved in the so-called “Reddit Rebellion” trading frenzy through its role as an executing dealer for Robinhood and its investment in distressed GameStop short seller, Melvin Capital Management.

There has not been any public indication that Citadel was one of the direct short sellers that stood to lose a significant amount of money as a result of the GameStop short squeeze. However, in its now significantly outdated [Form 13F filing](#) for the quarter ending September 30, 2020, Citadel disclosed multiple positions in GameStop, including 111,805 shares and a large but approximately equal position of puts (options that provide a short exposure) and calls (options that provide a long exposure). Large equal puts and calls could indicate that Citadel was positioning itself to profit from GameStop volatility, rather than a specific directional move. It is difficult to know for sure, though, and we can simply say that the reported positions were not solely short in late 2020 based on the dated public disclosures, but that could have changed dramatically since that time.

Nevertheless, as a prominent hedge fund and executing dealer for Robinhood (an executing dealer is just a second broker-dealer brought in by retail brokers to route trades and facilitate trade execution for customers), both Citadel and Griffin found themselves in the middle of the GameStop events and were targets of the so-called “Reddit Rebellion” ostensibly behind the precipitous increase in GameStop’s stock price. One Reddit post’s title—[“Know Thy Enemy: Kenneth C. Griffin, the Barbarian Behind the Gates of the Citadel”](#)—is indicative of Redditors’ feelings and conspiracies about Griffin and Citadel.

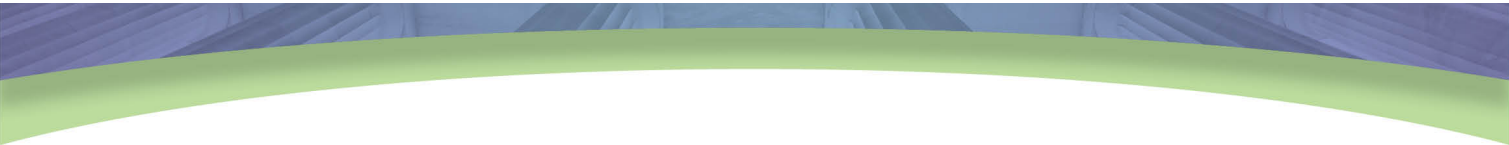
In short, Citadel has emerged alongside Reddit, GameStop, Robinhood, and others as one of the primary characters (or depending on your point of view, villains) in the ongoing saga. At the same time, its multiple roles illuminate some of the more pernicious aspects of financial system and reveal why many (not just conspiratorial Redditors) view the stock market as an essentially rigged game.

A. Citadel was reportedly the single largest payer of payment for order flow to Robinhood and other retail broker-dealers.

Citadel Execution Services is a business unit of CS that facilitates order routing and trade execution for retail broker-dealers, including Robinhood. Like nearly all retail broker-dealers, Robinhood continues to receive significant revenue from CS in the form of payment for order flow (“PFOF”). PFOF is a “rebate” generated on preferential order routing and execution by a select group of executing dealers. We have a [fact sheet on PFOF](#) and full consideration of disruptive and distortive effects of PFOF is beyond this brief fact sheet. However, in essence, PFOF creates conflicts of interest between (1) a retail broker-dealer’s duty to seek the “best execution” available for customer orders and (2) its duty to maximize its own profits for shareholders and/or owners through PFOF revenues generated by preferentially routing transactions to select HFTs. The result is harm to individual investors and markets, as reflected by Citadel’s legal troubles relating to [order routing](#) and [trading ahead](#) (and also the recent [SEC enforcement action against Robinhood](#)). CS is reportedly [the single largest payer of PFOF](#) in the industry.

A significant portion of [\\$687 million dollars](#) in PFOF Robinhood reportedly received in 2020 alone comes from Citadel. Robinhood’s [Form 606 filings](#) demonstrate that its customer orders are most frequently routed to Citadel (In fact, something like half of Robinhood’s customer orders were run through CS in 4Q 2020, with variation by order type, securities class, and month). Given these numbers, it is all but certain that CS generated at least tens of millions in PFOF rebates for Robinhood in 2020.

The PFOF arrangement between CS and Robinhood became salient when Robinhood determined to temporarily suspend purchases of a number of volatile securities, including GameStop, on January 28, 2021.



This led to public outcry and allegations that Robinhood abruptly instituted a trading halt on purchases to stymie retail demand for GameStop and thereby to protect short sellers in the markets, including hedge funds that were then being “squeezed” (i.e., forced to exit short positions at significant losses while GameStop was climbing, thereby requiring close-out purchases that pushed GameStop prices up further).

One of those hedge fund short sellers happened to be Melvin Capital Management (“Melvin Capital”), a hedge fund that was hemorrhaging money due short selling losses and that had just announced a [\\$2 billion bailout directly from Citadel](#) on January 25, 2021.

B. Some have engaged in unsubstantiated speculation that Citadel, Robinhood’s largest generator of payment for order flow, improperly influenced Robinhood’s trading halt determination to benefit an investment in a short selling hedge fund.

By all accounts, Melvin Capital was financially crushed by the so-called “Reddit Rebellion” in GameStop. Indeed, when the dust started to settle in February 2021, Melvin Capital was viewed as one of the primary losers in the GameStop short squeeze, reportedly suffering [losses of approximately 53% in January 2021](#) alone. Those losses necessitated an emergency \$2.75 billion investment from Citadel and another hedge fund, which led to, or reinforced, the perception later in the same week that Citadel had used its PFOF leverage to encourage Robinhood to institute a trading halt as a further bailout measure for Melvin Capital.

Citadel has categorically denied these allegations, stating that it was [“not involved in, or responsible for, any retail broker’s decision to stop trading in any way.”](#) It is unclear whether that statement applies to all Citadel entities, though CS issued its own statement that it had [“not instructed or otherwise caused any brokerage firm to stop, suspend, or limit trading or otherwise refuse to do business.”](#) Both statements are plausible. However, the credibility of each statement was undoubtedly complicated by the less credible, if not equivocal, statements made by Robinhood in explaining its trading halt. For example, apparently as or shortly before he sought a \$3.4 billion capital infusion of his own, Robinhood’s chief executive officer stated on CNBC that “[t]here was no liquidity problem” on account of clearinghouse margin calls, that Robinhood draws down its credit lines “all the time,” and that the firm’s [trading halts were being done “preemptively” and “proactively.”](#) Yet, Robinhood’s CEO suggested during the same interview that its trading halts were motivated by the substantial deposits due to clearinghouses on account of market volatility and its customers’ concentrated positions, as well as unspecified impacts on its net capital position.

Without regard to unsubstantiated and unequivocally denied allegations, the appearance of impropriety due to Citadel’s multiple functions in our markets is inescapable and partly a function of the unmitigated conflicts of interest that continue to unnecessarily plague our financial system and equity market structure. Most of all, these events demonstrate all too clearly the dangerous ongoing financial entanglements of retail broker-dealers, market-maker HFTs, hedge funds, and other actors within our financial system. The lack of transparency only compounds those problems.

Conclusion

The GameStop frenzy has demonstrated the fragility of the securities markets and once again exposed the pernicious financial eco-system that surrounds broking, market-making, trading, lending, and other Wall Street activities. That fragility is only exacerbated by the existence of probably currently indispensable market-makers, like Citadel, that operate in multiple capacities simultaneously and continue to present clear but unmitigated conflicts of interest in their performance of critical market functions.



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