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March 31, 2023

Securities and Exchange Commission
100 F St. NW
Washington, DC 20549-9303
Rule-comments@sec.gov

Re: Regulation Best Execution
File No. S7-32-22

Dear SEC:

¹ All opinions are strictly my own and do not necessarily represent those of Georgetown University or anyone else. I am very grateful to Georgetown University for financial support. Over the years I have served as a Visiting Academic Fellow at the NASD (predecessor to FINRA), served on the boards of the EDGX and EDGA stock exchanges, served as Chair of the Nasdaq Economic Advisory Board, and performed consulting work for brokerage firms, stock exchanges, other self-regulatory organizations, market makers, industry associations, and law firms. I am the academic director for the FINRA Certified Regulatory and Compliance Professional (CRCP[®]) program at Georgetown University. I've also visited over 75 stock and derivative exchanges around the world. As a finance professor, I practice what I preach in terms of diversification and own modest and well-diversified holdings in most public companies, including brokers, asset managers, market makers, and exchanges.

Summary

- It is really great that this applies to all transactions, not just “securities”
- Let’s have one rule instead of three.
- Update Regulation Best Interest to cover all things sold by BDs and RIAs
- If done right, this rule eliminates any need for retail auctions.

As part of its market structure armada of four major proposals in December 2022, the SEC has proposed a Best Execution rule at the SEC level. Currently, both FINRA and the MSRB have best execution rules, but there is not yet a rule at the SEC level.

I have covered the FINRA and MSRB best execution rules in my classes for many years. The FINRA and MSRB rules attempt to be the same, but there are subtle differences which can provide a trap for compliance professionals.²

The SEC is proposing a new rule with additional regulatory requirements. Among other things, the proposal requires additional written policies, procedures, and documentation beyond what FINRA and MSRB require. The rule requires additional policies and procedures from firms engaging in “conflicted” transactions. In addition, the rule would cover all transactions, not just securities transactions.

More than price matters.

The rule narrowly defines best execution in terms of the most favorable price. This is not bad for retail customers, but it ignores speed of execution for market orders, and probability of execution for limit orders.

Institutional customers have other considerations as well. For example, an institutional customer may be very concerned about leakage of the information in a

² See <https://www.jdsupra.com/legalnews/new-best-execution-requirement-for-munic-22211/>? For a discussion of some of the differences.

particular trade as well as how long it takes to fill a large order. Furthermore, institutional customers may be very concerned about the customer service that they get from their brokers and trading venues in the event of a trading problem.

“Any transaction” (including crypt assets) is the right way to go. RIGHT ON!

I love the “any transaction” part of the proposed rule. That includes transactions in equities, fixed income, options, commodities, collectibles, and magic crypto-moonbeams. It would be very sad for registered broker-dealers to be held to a high standard when executing equity trades but not trades in other things. Consumers should be able to expect the same quality for all transactions from their brokers, regardless of the type of transaction they are engaging in. RIGHT ON!

“Best available price” should include access fees.

One of the problems with the current NMS framework, is that brokers are not allowed to take exchange access fees into account when routing customer orders. With transparent fees, there is no reason that brokers should not be allowed to take fees into account and route to the best available all-in price. Brokers could choose whether to pass through the exchange fees and rebates or to eat them. The impact on market quality will be visible on the brokers’ newly required Rule 605 reports. However, this choice should be clearly disclosed in their order routing disclosures and marketing material.

The Commission should also apply Regulation Best Interest to all products sold by BDs and RIAs to retail investors.

In the same vein, the Commission should consider updating Regulation Best Interest to also apply to all recommendations made by broker-dealers and advisers. The SEC has explicit authority under Dodd-Frank to regulate all sales practices of broker-dealers and RIAs, not just how they sell securities.

§914(h) of Dodd-Frank reads (**emphasis added**) “
(h) OTHER MATTERS.—The Commission shall—

“(1) facilitate the provision of simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest; and

“(2) examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors.”

Indeed, Congress felt so strongly about this that it inserted the same language both in the Securities Exchange Act and the Investment Advisers Act. Congress didn't even attempt to customize the language to make the Securities Exchange Act amendment refer to brokers and dealers and the Adviser's Act amendment only to RIAs. Instead, both sections refer to brokers, dealers, and investment advisers.

Note that this is in addition to the grant of authority in §914(f) regarding the standard of care for advice supplied to retail investors about securities. This additional authority relates to all sales practices. This authority is NOT limited to securities. As Congress repeated this in Dodd-Frank, let me repeat this again: This authority is NOT limited to securities. Thus, the Commission has explicit and broad rulemaking authority to deal with ALL sales practices of broker dealers and RIAs, not just those having to do with individualized advice to retail investors about securities. In particular, the Commission has authority over the sales practices of everything that broker dealers and RIAs sell, including crazy cryptos and dodgy annuities. The Commission should exercise this authority.

Consumers should be able to expect the same level of duty from financial professionals regardless of whether the product involved is a security, a dodgy annuity, a gold coin, or a crypto beanie baby.

The Commission should consolidate all three rules into one.

Having three different best execution rules will be extremely confusing and difficult to comply with. Please, please, PLEASE have mercy on the compliance professionals who have to deal with all this stuff! As the commission admits in the

proposal, there are subtle differences between these three sets of best execution rules. This will trip up compliance professionals. Even the well-meaning ones who are honestly trying to comply may inadvertently fail to dot some of the required paperwork Is or cross some of the paperwork T's.

I suggest combining the three rules into one SEC rule and rely upon the SROs to enforce them. Rather than having the SROs attempt to adapt their rules to be in conformance, the SROs should scrap their existing rules. Once the new SEC rule is in effect, FINRA should issue a statement reminding members that FINRA Rule 3110 requires supervisory systems to comply with all applicable securities laws and regulations, including Regulation Best Execution.

Economic analysis needs to consider combined impact of proposed rules.

Four major rule proposals were proposed by the Commission on the same day. These undoubtedly interact with each other in hard to determine ways. The economic analysis should consider the combined impact of all of the proposed rules that have been proposed at the same time. In particular, if this rule is done right, then there would be no need for other more prescriptive rules, such as the proposed auctions, to get best execution for customers.

Respectfully submitted,

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