

March 28, 2023

BY ELECTRONIC SUBMISSION

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

Re: File No. S7-32-22, RIN 3235-AN24, Regulation Best Execution

Dear Ms. Countryman:

Andreessen Horowitz (“a16z”) appreciates the opportunity to comment on the proposal by the Securities and Exchange Commission (“Commission”)¹ to enhance the existing regulatory framework concerning the duty of best execution for broker-dealers. We are most focused on urging the Commission to clarify that the proposed Regulation Best Execution (“Reg. BestEx”) would not apply to investment advisers. We will also raise considerations regarding the Commission’s proposal, seemingly unsupported by any reliable empirical evidence, to require Reg. BestEx to apply to transactions in crypto asset securities.

As one of Silicon Valley’s leading venture capital firms with over \$35 billion in committed capital, a16z has been investing in crypto since 2013, and today, we manage multiple dedicated crypto/web3 pooled vehicles of over \$7.5 billion of committed capital across this family of funds. AH Capital Management, L.L.C., a registered investment adviser, serves as adviser to our fund family, including our crypto-focused funds. As the earliest and largest investor in many crypto and web3 companies and projects, and as one of the largest investment advisers in the technology space, a16z is well-positioned to evaluate the potential impact of the Reg. BestEx Proposal on investment advisers, and on crypto asset securities markets generally.

¹ Regulation Best Execution, 88 *Fed. Reg.* 5440 (Jan. 27, 2022) (“Reg. BestEx Proposal” or “Proposal”).

As discussed below, we believe that if adopted in its current form, Reg. BestEx could have adverse consequences for investment advisers, and could obscure the Commission's existing guidance on investment advisers' duty of best execution. Separate and apart from this concern, we believe that the Proposal's expansion of Reg. BestEx to crypto asset securities markets risks violating the Administrative Procedure Act because it is premature, due to the lack of support of reliable empirical data and the absence of an appropriate analysis of costs and benefits.

INTRODUCTION AND EXECUTIVE SUMMARY

On December 14, 2022, the Commission proposed a new regulation which would establish a best execution standard for broker-dealers ("Reg. BestEx"). Reg. BestEx would require that in any securities transaction for a customer or a customer of another broker-dealer, a broker-dealer must:

1. Use reasonable diligence to ascertain the best market for the security; and
2. Buy or sell in such market so that the price to the customer is as favorable as possible under prevailing market conditions.

a16z has serious concerns about the Reg. BestEx Proposal, which are summarized here and described in further detail below:

Application of Reg. BestEx to Investment Advisers.

- Reg. BestEx should not apply to investment advisers, because an investment adviser's duty of best execution is significantly different from the duty that Reg. BestEx proposes for brokers. An investment adviser's duty of best execution requires the adviser to seek a suitable broker. Reg. BestEx, by contrast, requires a broker to identify the best market and execute the customer's order in that market at the most favorable price.
- Reg. BestEx is a regulation aimed at brokers. Applying Reg. BestEx to investment advisers effectively ignores the difference between the roles of an investment adviser and a broker-dealer and erodes the discretion investment advisers have enjoyed to execute transactions in accordance with a long-term investment strategy.

- Even if the Commission decides to adopt Reg. Best Ex, it need not apply Reg. BestEx to investment advisers in order for advisory clients to benefit from Reg. BestEx. If the Commission did not apply Reg. BestEx to investment advisers, advisers would, where appropriate, continue to select the most suitable broker in line with their existing duty of care to their advisory clients. The broker selected by the adviser would then execute the order in accordance with Reg. BestEx, thereby ensuring that the adviser client indirectly received the benefits of Reg. BestEx.

Application of Reg. BestEx to Crypto Asset Securities Markets

- The Commission proposes to apply Reg. BestEx to crypto asset securities markets, apparently in the same manner that Reg. BestEx would apply to traditional securities markets. This proposal raises significant concerns under the Administrative Procedure Act because:
 - The Commission has not presented any empirical data to explain why Reg. BestEx should apply to crypto asset securities transactions, despite the potentially significant differences between the crypto asset securities markets and traditional securities markets.
 - In the absence of data, the Commission has not conducted a sufficient evaluation of the costs and benefits of extending Reg. BestEx to crypto asset securities markets.
 - The Commission has not put forth any alternatives to its proposal to apply Reg. BestEx to crypto asset securities transactions.

To allay these concerns, a16z urges the Commission to (i) clarify that investment advisers are not subject to Reg. BestEx; and (ii) to not extend Reg. BestEx to the crypto asset securities markets, pending a thorough and detailed collection and study of data relating to the crypto asset securities markets. We stand ready to work with the Commission in the crafting of a suitable best execution standard that reflects the structure and unique characteristics of the crypto asset securities markets. We therefore request the Commission to avoid the automatic extension into crypto asset securities markets of a “one-size-fits all” standard designed for, and drawn from traditional securities transactions.

DISCUSSION

I. REG. BESTEX SHOULD NOT APPLY TO INVESTMENT ADVISERS

The Commission asks: “What effect, if any, would the proposed best execution standard have on investment advisers and their duty to seek best execution?”²

Our response: Reg. BestEx, as proposed, should not apply to investment advisers, and we urge the Commission to clearly state that Reg. BestEx does not apply to investment advisers. Our reasons for this view, which we discuss further here, can be summarized as follows:

- An investment adviser’s duty of best execution is significantly different from a broker-dealer’s duty under Reg. BestEx.
- The Commission does not need to extend Reg. BestEx to investment advisers in order for Reg. BestEx to benefit adviser clients.
- Applying the proposed Reg. BestEx standard to investment advisers will cause significant confusion for investment advisers, making it more difficult for investment advisers to operate.

We discuss each of these reasons further below.

A. An Investment Adviser’s Duty of Best Execution is Significantly Different from a Broker-Dealer’s Duty under Reg. BestEx

As recently as 2019, the Commission has clearly described the scope of an investment adviser’s duty of best execution and when the duty of best execution applies. That duty, as described by the Commission, is substantially different from the duty that Reg. BestEx would impose on a broker-dealer.

² Reg. BestEx, 88 *Fed. Reg.* at 5453.

1. *The Scope of an Investment Adviser's Duty of Best Execution is Well Settled*

As fiduciaries, investment advisers owe their clients a duty of care.³ This duty of care, according to the Commission, includes (i) the duty to provide advice in the best interest of the client, (ii) the duty to seek best execution of a client's transactions; and (iii) the duty to provide advice and monitoring over the course of the relationship.⁴

An investment adviser's duty to seek best execution of its client's transactions applies only where the adviser has the responsibility to select broker-dealers to execute client trades (typically in the case of discretionary accounts).⁵ The Commission states that the duty of best execution requires an adviser to seek to obtain the execution of transactions for each of its clients such that the client's total cost or proceeds in each transaction **are the most favorable under the circumstances**.⁶ (Emphasis ours.) An adviser fulfills this duty by seeking to obtain the execution of securities transactions on behalf of a client with the goal of maximizing value for the client under the particular circumstances occurring at the time of the transaction.⁷

For an investment adviser, maximizing value for a client encompasses more than just minimizing cost. The Commission notes that when seeking best execution, an adviser should consider "the full range and quality of a broker's services in placing brokerage including, among other things, the value of research provided as well as execution capability, commission rate, financial responsibility, and responsiveness to the adviser."⁸ For an adviser, the determinative factor for best execution is not the lowest possible commission

³ Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 *Fed. Reg.* 33,669 at 33,672 (July 12, 2019) ("Standard of Conduct for Investment Advisers").

⁴ *Id.*

⁵ *Id.* at 33,674.

⁶ *Id.* at 33,675.

⁷ *Id.*

⁸ *Id.*

cost, “but whether the transaction represents the best qualitative execution.”⁹ An adviser must also periodically evaluate the execution it receives for its clients.¹⁰

2. *An Investment Adviser’s Duty of Best Execution is Significantly Different from a Broker-Dealer’s Duty Under Reg. BestEx.*

An investment adviser’s duty of best execution is very different from the duty Reg. BestEx would impose on brokers. As the Commission has previously noted,¹¹ the investment adviser’s duty of best execution involves selecting a suitable broker-dealer to execute client trades. In making its choice of a broker-dealer, the investment adviser may consider the range and quality of the broker’s services, but the investment adviser is not itself tasked with executing the client order.¹² By contrast, Reg. BestEx would require an executing broker to choose the best market, and to then execute the transaction at the most favorable price under prevailing market conditions. The investment adviser’s duty is to delegate execution to the broker who can ensure best execution. The executing broker’s duty under Reg. BestEx is to ensure best execution.

⁹ *Id.* Although the Commission does not expressly say so, it likely follows that there may be circumstances where an investment adviser managing discretionary accounts might conclude that it is more effective to execute a transaction itself, rather than to engage a broker-dealer. For example, in the crypto asset markets, the Commission notes that “there are currently no special purpose broker-dealers authorized to maintain custody of crypto asset securities.” (88 *Fed. Reg.* at 5448.) In such crypto asset markets, for example, investment advisers might conclude that a transaction that involves custodying client crypto assets cannot be delegated to a broker-dealer, because no broker-dealer exists with suitable custodial authority over crypto assets. The Commission has also previously found it a violation of the antifraud provisions of the securities laws to interpose an unnecessary party in a transaction, resulting in payment to the interposed party, and an additional cost to the fiduciary account. *See Delaware Management Co.*, 43 SEC 392 (1967) (interpositioning broker between adviser and market maker caused adviser to pay unnecessary brokerage costs and violated the adviser’s duty of best execution). This suggests that there may be situations where an investment adviser’s delegation of a transaction for execution to a broker might be unnecessary and a violation of the securities laws.

¹⁰ Standard of Conduct for Investment Advisers, 84 *Fed. Reg.* at 33,675.

¹¹ *Id.*

¹² We note, of course, that “dual hatted” investment advisers who are also broker-dealers might execute, as brokers, transactions for their own advisory clients, but this is an exception.

The investment adviser is therefore required to evaluate brokers and brokerage services – using factors such as the value of research provided by the broker, the broker’s execution capability, responsiveness, commissions charged and financial responsibility. The investment adviser is also required to periodically evaluate whether the chosen broker is providing best execution for adviser clients — for example, when brokerage and/or fee arrangements are changed.¹³ Reg. BestEx, on the other hand, would require brokers to evaluate markets – using factors such as best displayed prices, opportunities for price improvement, the trading characteristics of the security, the size of the order, the likelihood of execution, and the accessibility of the market.

B. The Commission Does Not Need to Extend Reg. BestEx to Investment Advisers in Order for Reg. BestEx to Benefit Adviser Clients

Even if the Commission decides to adopt Reg. Best Ex, it does not need to extend Reg. BestEx to investment advisers in order for adviser clients to benefit from Reg. BestEx.

When we ask the Commission to not extend Reg. BestEx to investment advisers, we mean that the Commission should not require investment advisers, even those with discretionary accounts, to use reasonable diligence to ascertain the best market for the security, and buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. We think the standard of conduct for investment advisers that the Commission described in 2019 would permit an investment adviser to delegate this proposed duty to a broker-dealer. Such delegation, as we explain below, provides sufficient protection to investment adviser clients.¹⁴

If the Commission adopts Reg. BestEx, but clearly states that Reg. BestEx does not apply to investment advisers, advisers will continue to follow the Commission’s existing interpretation of their duty of best execution. Under this existing interpretation, if a

¹³ See, e.g., the Commission’s recent order in *Huntleigh Advisors Inc.*, (Feb. 27, 2023), finding, among other things, a violation of the duty of best execution by an adviser who failed to assess whether clients were receiving best execution from an affiliated broker-dealer in light of changes to transaction fees, and changes in clearing brokerage fees.

¹⁴ This would not apply to “dual hatted” investment advisers, who may be subject to Reg. BestEx, but only in their broker-dealer role.

transaction requires the use of a broker, an adviser must select the most suitable broker for each client so as to maximize value for the client under the particular circumstances occurring at the time of the transaction. The broker selected by the adviser will, however, be bound by Reg. BestEx, and must then use reasonable diligence to ascertain the best market for the security, and buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions.

In other words, even if the Commission adopts Reg. BestEx but decides that it does not apply to investment advisers, the net effect for adviser clients will generally be the same. The brokers that execute transactions for adviser clients will be bound by Reg. BestEx, even though advisers will not be bound by Reg. BestEx. In each brokered transaction entered into by an adviser, therefore, the Commission will thus secure the benefits of Reg. BestEx for adviser clients indirectly – clients will receive execution from brokers selected by the investment adviser and these brokers will, in turn, comply with Reg. BestEx in executing adviser client transactions.

Thus, a clarification from the Commission that investment advisers are not bound by Reg. BestEx will allow investment advisers to continue to follow the existing and clear Commission guidance on best execution, without depriving adviser clients of the benefits of Reg. BestEx. This is an outcome that recognizes advisers' reliance on settled and stable Commission interpretations, while ensuring adviser clients receive the intended benefits of the proposed regulation.

C. Applying the Proposed Reg. BestEx Standard to Investment Advisers Will Cause Significant Confusion for Investment Advisers, and Make it More Difficult for Investment Advisers to Operate.

If the Commission were to take the position that investment advisers are subject to Reg. BestEx, the effect will be the overt supplanting of many decades of Commission guidance,¹⁵ and ensuing confusion in the investment adviser community as to the scope of an adviser's duty of best execution.

¹⁵ See, e.g., Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, 71 *Fed. Reg.* 41,977 at 41,978 (July 24, 2006) (stating that investment advisers have "best execution obligations"); Amendments to Form ADV, Investment Advisers Act Release No.

The Commission's existing guidance preserves significantly more discretion for advisers in the exercise of their best execution obligations, than Reg. BestEx does for brokers. Reg. BestEx would require a broker to execute the transaction so that the price to the customer is as favorable as possible under prevailing market conditions. Investment advisers, by contrast, must obtain the execution of transactions so that the client's total cost or proceeds in each transaction are the most favorable under the circumstances.

This difference is not merely semantic. The Commission has recognized that investment advisers have a qualitatively different relationship with clients, compared to broker-dealers. As the Commission notes, "Investment advisers and broker-dealers have different types of relationships with investors, offer different services, and have different compensation models. This variety is important because it presents investors with choices regarding the types of relationships they can have, the services they can receive, and how they can pay for those services."¹⁶ The Commission has also noted that "[b]roker-dealers typically provide transaction-specific recommendations and receive compensation on a transaction-by-transaction basis (such as commissions)" while "[i]nvestment advisers, on the other hand, typically provide ongoing, regular advice and services in the context of broad investment portfolio management, and are compensated based on the value of assets under management..., a fixed fee or other arrangement ..."¹⁷

The Commission has contrasted the "continuous advisory services" received from an investment adviser against the "episodic recommendations from a broker-dealer."¹⁸ For adviser clients who receive these "continuous advisory services," particular transactions may be part of an overall investment strategy, and their execution should be evaluated in the context of that strategy. By contrast, Reg. BestEx focuses on the identification of the best market and the best price, and makes no provision for any broader strategy that an adviser may be trying to implement on behalf of its client. Requiring an investment adviser to

3060, 75 *Fed. Reg.* 49,233 at 49,243 (Aug. 12, 2010) (discussing an adviser's best execution obligations in the context of directed brokerage arrangements); Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 *Fed. Reg.* 33,669 at 33,672 (July 12, 2019).

¹⁶ Standard of Conduct for Investment Advisers, 84 *Fed. Reg.* 33,670.

¹⁷ Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 *Fed. Reg.* 3318 at 3319 (July 12, 2019) ("Reg. BI").

¹⁸ Reg BI, 84 *Fed. Reg.* at 3319.

implement Reg. BestEx may therefore have the unintended effect of unduly narrowing the discretion traditionally available to investment advisers. This, in turn, could lead investment advisers to constantly second-guess investment strategies to ensure that these do not fall afoul of Reg. BestEx, even if such strategies are otherwise in the best interest of the client. The result would likely be significant uncertainty and confusion for investment advisers, sub-optimal advice and planning for adviser clients, and the distortions caused by applying, in the advisory context, a regulation intended for a fundamentally different type of relationship.

The difficulties we describe above, which would arise from the extension of Reg. BestEx to investment advisers, are very significant and would likely affect investment advisers generally. However, the Commission can address these difficulties through a simple clarification that Reg. BestEx does not apply to investment advisers (except where dual registered investment advisers operate in their capacity as broker-dealers).

For investment advisers and broker-dealers who operate in the crypto asset securities markets, however, proposed Reg. BestEx raises even greater challenges. These challenges raise very substantial concerns under the Administrative Procedure Act, and stem from the Commission's proposal, which was unsupported by data, to require Reg. BestEx to apply to transactions in crypto asset securities. We examine these challenges and concerns below.

II. THE COMMISSION'S PROPOSAL TO APPLY REG. BESTEX TO THE CRYPTO ASSET SECURITIES MARKETS RAISES SIGNIFICANT CONCERNS UNDER THE ADMINISTRATIVE PROCEDURE ACT

The Commission's proposal to apply Reg. BestEx to transactions in crypto asset securities would create great confusion for broker-dealers and other market participants operating in the crypto asset securities markets and the broader markets for crypto assets generally. The Commission has preliminarily proposed to apply Reg. BestEx to crypto asset securities markets in exactly the form it would apply to traditional securities markets, and appears to have done so even in the absence of any convincing and reliable empirical data on order handling in crypto asset securities markets. In fact, the Commission freely admits that it is not certain as to the nature or extent of the crypto asset securities markets, or even

the extent to which they are regulated by the Commission. This absence of data makes it very difficult for the Commission to consider how this decision might affect the nascent and growing crypto asset securities markets, and it is therefore unsurprising that the Commission seems to have not at all considered the impact of extending Reg. BestEx to crypto asset securities markets. If the Commission, with its considerable staff and resources, finds it difficult to assess the crypto asset securities markets, it seems wholly unfair to require broker-dealers to evaluate those markets.

Under the circumstances, we urge the Commission to study the crypto asset securities markets in significantly more detail before deciding whether Reg. BestEx should apply to crypto asset securities transactions. If after such study the Commission does decide to apply Reg. BestEx to the crypto asset securities markets, it should repropose Reg. BestEx specifically in the context of crypto asset securities markets, and clearly consider the costs and benefits of its decision. These steps would permit stakeholders to engage in a meaningful discussion with the Commission regarding the implications of Reg. BestEx for the crypto asset securities markets. We are concerned that the Commission's failure to take these steps, and a decision to reflexively apply Reg. BestEx in an unnuanced manner to the crypto asset securities markets without sufficient data or appropriately considering alternatives, may render Reg. BestEx vulnerable to challenge under the Administrative Procedure Act.

A. The Commission Does Not Have Sufficient Empirical Data to Explain its Proposal to Apply Reg. BestEx to Crypto Asset Securities Transactions

Under the Administrative Procedure Act, the Commission must “articulate a satisfactory explanation for its action including a rational connection between the facts found and the choices made.”¹⁹ In the Reg. BestEx Proposal, the Commission articulates a choice — to apply Reg. BestEx to crypto asset securities transactions — but fails to find or discuss any material facts about the crypto asset securities markets that satisfactorily explain its choice. Indeed, at various points in the Reg. BestEx Proposal, the Commission admits that it:

¹⁹ *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (DC Cir. 2011); *Motor Vehicle Mfrs. Ass’n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

- “lacks data on broker-dealer routing behavior, the frequency of crypto asset securities trading in both non-conflicted and conflicted transactions, and many details of trading protocols and crypto asset securities trading platforms”;²⁰
- “does not have data on the prevalence of introducing brokers in the crypto asset securities market”;²¹
- finds it difficult to determine the costs of compliance for broker-dealers in crypto asset securities because “it lacks data and other information on existing broker-dealers and their practices in the crypto asset securities market”;²² and
- is either unable to quantify certain economic effects, or is required to make certain assumptions that may make the quantification of effects unreliable.²³

The Commission appears to take the view that because the duty of best execution is of fundamental importance, a customer transacting in crypto asset securities should receive the protections afforded by Reg. BestEx. We do not disagree that the duty of best execution is important, and that crypto asset securities customers should be protected, but it does not follow that crypto asset securities customers must be protected in exactly the same way as customers for traditional securities. The Commission itself makes a clear acknowledgment that crypto asset securities markets are unique, and are not comparable to markets for other asset classes.²⁴

B. The Commission Recognizes but Disregards the Unique Characteristics of the Crypto Asset Securities Markets

The Commission notes several features that make the crypto asset securities markets unique, but does not appear to consider these in its proposal to apply Reg. BestEx to crypto

²⁰ See Reg. BestEx Proposal, 88 *Fed. Reg.* at 5528.

²¹ *Id.* at 5529, n. 569.

²² *Id.* at 5532.

²³ *Id.* at 5483.

²⁴ *Id.* at 5529, n.566, noting that “no exact comparison to any other asset market is likely with crypto asset securities.”

asset securities transactions. Although the Commission appears to recognize that these features are relevant and important to a developed understanding the crypto asset securities markets, there appears to be no discussion, even on a hypothetical basis, of how these features would or should affect any decision to apply Reg. BestEx to the crypto asset securities markets.

1. *The Commission Appears to Ignore the Potentially Lower Degree of Broker Participation in Crypto Asset Securities Markets*

The Commission notes that a significant degree of the volume in major centralized crypto asset securities markets appears to come directly from retail customers.²⁵ The Commission also notes that there are no special purpose broker-dealers currently registered with the Commission²⁶ — these are the only broker-dealers currently permitted by the Commission to custody crypto asset securities.

The importance of the possibility that broker-dealers may play a much less critical role in the crypto asset securities markets cannot be overstated. Reg. BestEx is intended to regulate the conduct of broker-dealers, and executing brokers, in particular. The Commission admits that there is significant direct retail participation in crypto asset securities markets, and that it is unaware of the degree of broker-dealer participation in these markets — but it does not then explain why Reg. BestEx should presumptively apply to a market where the degree of broker-dealer involvement is questionable, and where the degree of executing broker participation may be very low.

The significant restrictions that currently apply to broker-dealers dealing in crypto asset securities would likely make it less convenient for advisers to use broker-dealers to effect crypto asset transactions. Put differently, using a broker-dealer may, in certain types of crypto transactions, unnecessarily complicate and increase the cost of execution of the transaction.²⁷ If a thorough study of the crypto asset securities markets shows significantly

²⁵ *Id.* at 5518.

²⁶ *Id.* at 5448.

²⁷ *See* n. 9, *supra*, noting that “investment advisers might conclude that a transaction that involves custodial client crypto assets cannot be delegated to a broker-dealer, because no broker-dealer exists with suitable custodial authority over crypto assets.”

lower rates of executing broker-dealer involvement in the crypto asset securities markets, the Commission's proposal to apply Reg. BestEx to crypto asset securities markets will lack a firm empirical foundation. Such Commission action, apparently taken on the basis of insufficient empirical data is arbitrary, capricious and in violation of the Administrative Procedure Act.²⁸

2. *The Commission Appears to Ignore the Significant Uncertainty Around the Character of Crypto Assets and the Extent of Crypto Asset Securities Markets*

The Commission acknowledges that many crypto asset markets may be operating in violation of the federal securities laws, but does not discuss how this would affect the concept of the "best market" under proposed Reg. BestEx. Nor does the Commission provide a clear framing for which crypto asset markets should be subject to Reg. BestEx, and how broker-dealers should evaluate crypto asset markets.

The Commission claims that many crypto asset markets are trading securities, in violation of the federal securities laws.²⁹ It also claims that there are many crypto asset markets that are not domiciled in the U.S. but are open to participation by U.S. investors.³⁰ If these claims by the Commission regarding the crypto asset markets are accurate, then it would likely be very difficult for broker-dealers to comply with Reg. BestEx, as there would be considerable confusion regarding what the best markets for a crypto asset should be. Should a broker-dealer seek execution on the best regulated crypto asset securities market? Or should a broker-dealer seek execution on the best crypto asset market, irrespective of its regulatory status? Should a broker-dealer, seeking to identify the best market, consider only the universe of U.S. domiciled crypto asset markets? Or should a broker-dealer consider all crypto asset markets, irrespective of location?

²⁸ *Business Roundtable*, 647 F.3d at 1148.

²⁹ Reg. BestEx Proposal, 88 *Fed. Reg.* at 5448. ("[O]nly a small portion of crypto asset security trading activity is occurring within entities that are registered with the Commission and any of the [Self Regulatory Organizations].")

³⁰ *Id.* at 292, n. 517. ("Some platforms that purport to be located outside of US nevertheless seek to cater to US customers, among other ways, by complying with certain requirements set by the CFTC and FinCEN.")

These questions are not incidental or marginal – they are central to the operation of Reg. BestEx in the crypto asset securities markets. The Commission implicitly acknowledges the existence of these questions, but it disregards them by simply proposing that Reg. BestEx should apply to crypto asset securities markets, without any discussion of the difficulties this regulatory choice will likely pose for broker-dealers. If the Commission, with its abundant resources, cannot satisfactorily determine the parameters within which Reg. BestEx should operate in the crypto asset securities markets, broker-dealers cannot be reasonably expected to make such determinations.

3. *Identifying the Relevant Crypto Asset Securities Markets Will Continue to be Difficult and Contested, Until There is Clearer Guidance Around Which Crypto Assets are Securities*

The Commission’s difficulty in identifying the scope of the crypto asset securities markets is, as we note above, likely to be shared by broker-dealers. More fundamentally, however, this difficulty in identifying the relevant crypto asset securities markets is a direct consequence of disagreements among many market participants regarding the security status of specific crypto assets. We recognize the valuable guidance provided by the Commission and its staff regarding which crypto assets are investment contracts,³¹ but we also recognize that such guidance has not definitively settled debates regarding the status of individual crypto assets.

We do not disagree that investors in crypto asset securities are entitled to statutory and other safeguards. We recognize, however, that there continue to be profound disagreements in good faith, even among federal regulators,³² as to the character of many specific crypto assets. While these disagreements persist, and until greater regulatory clarity

³¹ See, e.g., Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81207 (July 25, 2017). See Framework for “Investment Contract” Analysis of Digital Assets, available at <https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets>.

³² Nikhilesh De, CFTC Should Be Crypto’s ‘Primary Cop,’ Acting Chairman Says, Coindesk, Oct. 27, 21, available at <https://www.coindesk.com/policy/2021/10/27/cftc-should-be-cryptos-primary-cop-acting-chair-says/>, noting that “The regulator pointed to the size of the crypto market, noting the overall market capitalization is about \$2.7 trillion now, and ‘nearly 60% were commodities.’”

is available, it would be unfair to require brokers to definitively determine which specific crypto assets are securities, particularly where issuers of such assets take a different view. In other contexts, the securities laws permit a broker-dealer seeking to trade an asset to rely on an issuer's disclosure of information regarding that asset.³³ We see no reason why the crypto asset markets should be an exception from that rule.

C. The Commission Does Not — and Cannot, Without Further Data Collection — Evaluate the Cost and Benefits of Applying Reg. BestEx to Crypto Asset Securities Transactions

The Exchange Act requires the Commission, in its rulemaking, to “consider the effect of a new rule upon ‘efficiency, competition, and capital formation.’”³⁴ The Commission must “apprise itself — and hence the public and Congress — of the economic consequences of a proposed regulation.”³⁵

The absence of data leaves the Commission effectively unable to weigh the costs and benefits of its proposal to extend Reg. BestEx to crypto asset securities markets. The Commission recognizes this, noting that “the Commission does not have, and in certain cases does not believe it can reasonably obtain, data that may inform the Commission on certain economic effects”.³⁶ The Commission even goes on to add that its “inability to quantify certain costs, benefits, and effects does not imply that the Commission believes such costs, benefits, or effects are less significant.”³⁷ The Commission's open admission that it lacks significant information will likely lead reasonable observers to question whether the proposal to apply Reg. BestEx to crypto asset securities transactions is premature or ill-advised.

We recognize the difficulties associated with the collection of information relating to crypto asset securities markets, and we appreciate the Commission's request to commenters to provide relevant data and information to assist in quantifying the economic consequences

³³ See, e.g., Exchange Act Rule 15c2-11(b).

³⁴ 15 U.S.C. § 78c(f).

³⁵ *Chamber of Commerce v. SEC*, 412 F.3d 133, 144 (D.C. Cir. 2005).

³⁶ Reg. BestEx Proposal, 88 *Fed. Reg.* at 5483.

³⁷ *Id.*

of proposed Reg. BestEx. However, this data collection and analysis effort should be done separately from, and in advance of a proposed rulemaking, not as part of a proposed rule's public comment process where the Commission might seek to finalize aspects of a proposal which lacked reliable data itself and where the public, in providing such data to the Commission, cannot holistically engage that data. We cannot agree that Reg. BestEx should apply to crypto asset securities transactions until the Commission is able to collect sufficient reliable data and present it to the public for meaningful engagement. In the words of the D.C. Circuit Court of Appeals, "Uncertainty may limit what the Commission can do, but it does not excuse the Commission from its statutory obligation to do what it can to apprise itself — and hence the public and the Congress — of the economic consequences of a proposed regulation before it decides whether to adopt the measure."³⁸

Accordingly, we would suggest that the Commission take the time required to study the crypto asset securities markets, and evaluate the costs and benefits of applying Reg. BestEx to these markets. Until such time as the Commission can carry out the required study and cost-benefit analysis, we would urge the Commission to clarify that Reg. BestEx does not apply to crypto asset securities transactions.

D. The Commission Did Not Consider Reasonable Alternatives to the Application of Reg. BestEx to Crypto Asset Securities Transactions

The Administrative Procedure Act requires the Commission, in any rulemaking exercise, to consider alternatives to the proposed rule that are neither "frivolous nor out of bounds."³⁹ The Commission is required to address alternative ways of achieving its objectives and to provide adequate reasons for rejecting these alternatives.⁴⁰

It is certainly true that the Commission is not required to consider "every alternative ... conceivable by the mind of man ... regardless of how uncommon or unknown that alternative" may be,⁴¹ but in this case the Commission gives no evidence of having considered any alternatives at all to its proposal to apply Reg. BestEx to the crypto asset

³⁸ *Chamber of Commerce*, 412 F. 3d at 144.

³⁹ *Id.* at 145.

⁴⁰ *Motor Vehicle Mfrs. Ass'n*, 463 U.S. at 51

⁴¹ *Id.* at 51.

securities markets. The Commission has not, for example, considered any alternative formulations of the best execution standard that may be better suited to crypto asset securities markets. The Commission has not considered the application of Reg. BestEx to some clearly-defined geographical or legal subset of the crypto asset securities markets. The Commission has not considered alternative measures to protect retail crypto customers other than the imposition of the Reg. BestEx standard. Not one sentence of the Reg. BestEx Proposal discusses any alternative to the proposed application of Reg. BestEx to crypto asset securities markets.

The Commission could have kept the application of Reg. BestEx in abeyance while it consulted with crypto market participants on how to secure best execution in crypto asset securities markets. It has chosen not to do so, opting instead to propose the application of Reg. BestEx, without any modification or nuance, to the crypto asset securities markets. This decision, without even the barest consideration of any alternatives, raises grave concerns under the Administrative Procedure Act.

E. If the Commission Seeks to Create a Best Execution Standard for the Crypto Asset Securities Markets, it Should Repropose that Portion of the Reg. BestEx Proposal

If the Commission aims to create a best execution standard that is tailored to crypto asset securities transactions, it should propose a new rule for this purpose. That rule should:

- study, in depth, the character and extent of, and degree of broker participation in the crypto asset securities markets,
- consider and account for the unique characteristics of the crypto asset securities markets,
- examine the economic effects of the proposed new best execution standard for crypto asset securities transactions,
- evaluate the costs and benefits of the proposed new best execution standard for crypto asset securities transactions, and
- consider reasonable alternatives to the proposed best execution standard.

Reproposing this particular part of the Reg. BestEx Proposal would permit the Commission to focus on the crypto asset securities markets, with their unique features and challenges, and to engage in greater depth with crypto asset securities market participants.

CONCLUSION

a16z appreciates the opportunity to share its perspective on the Commission's proposed Reg. BestEx. The Reg. BestEx Proposal poses such significant concerns for investment advisers, and for the Commission's existing guidance regarding the duties of investment advisers, that we must respectfully request the Commission to clarify that investment advisers are not within the scope of Reg. BestEx. A clarification to this effect will allow investment advisers to continue with settled execution practices, in reliance on well-established Commission guidance. If no clarification is issued, the Commission may risk confusion among the investment adviser community, to the general detriment of adviser clients and orderly markets.

With respect to the Commission's proposal to apply Reg. BestEx to crypto asset transactions, we ask that the Commission:

- delay its proposal to apply Reg. BestEx to crypto asset securities transactions, and instead engage in a detailed study of the crypto asset securities markets, with a view to collect data on these markets, and brokerage practices therein; and
- following such study, if appropriate, repropose a rule with a best execution standard suitably tailored to the crypto asset securities markets.

We ask that, as part of that reproposal, the Commission issue a detailed cost-benefit analysis evaluating the effects of a best execution standard on the crypto asset securities markets. This cost-benefit analysis is not only required under the Administrative Procedure Act, it would also further the Commission's objectives of investor protection, capital formation and orderly markets.

The crypto asset securities markets continue to be in a nascent state, and the rules, policies and practices of the Commission and other U.S. regulators are critical to their orderly

development. These unique markets demand, and deserve, detailed and rigorous examination by regulators and participants alike. We urge the Commission to evaluate crypto asset securities markets on their own terms and to reject any reflexive extension of regulations from the traditional securities markets. a16z is ready to work with the Commission towards the regulatory regime that crypto markets truly need.

Respectfully submitted,

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