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VIA ELECTRONIC DELIVERY

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

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

Dear Ms. Countryman:

Two Sigma Securities, LLC ("TSS" or the "Firm")[1] respectfully submits this letter in response to the above-referenced rule proposal ("Proposed Reg Best Ex" or "Proposal")[2] from the U.S. Securities and Exchange Commission ("SEC" or "Commission"). TSS is an active participant in the U.S. equity markets, and through our wholesale market making business, we work with broker-dealers receiving orders from retail investors to deliver best execution for those clients. Retail investor participation in the stock market is at an all-time high; retail investors receive strong and certain executions at low/no cost, and there are more retail-oriented products and services available than ever before in the history of the U.S. financial markets. These benefits have been made possible by our current market structure and the role that wholesale market makers, such as TSS, play in this market structure.

While the Firm supports a robust best execution standard, the Proposal is unnecessary for investor protection because both FINRA and the Municipal Securities Rulemaking Board ("MSRB") already have longstanding rules, along with interpretive guidance, identifying standards for a broker-dealer's duty of best execution. But more importantly, we are concerned that the Proposal would not actually achieve best execution for investors; rather, it would likely harm investors, particularly retail investors. The Proposal's requirements will introduce unnecessary redundancy, complexity, confusion, potential information leakage and transaction costs on broker-dealers, which in turn, will interfere with their ability to provide best execution. In making the Proposal, the Commission failed to identify a quantifiable resultant benefit or conduct an adequate cost-benefit analysis, instead alluding to vague "investor protection" benefits and failing to consider the associated costs, such as lost execution quality on an aggregate level and increased commission costs, which will be passed on to retail investors.

[1] TSS is a registered market maker focused on providing liquidity through systematic trading strategies across asset classes. TSS has a strong vested interest in making sure our financial markets are efficient and competitive. Accordingly, TSS is an active member of the Securities Industry and Financial Markets Association ("SIFMA") and the Committee on Capital Markets Regulation ("CCMR"), and we support their letters addressing the full scope of the SEC's four market structure proposals.

[2] Regulation Best Execution, 88 Fed. Reg. 5440 (Jan. 27, 2023) ("Proposal" or "Proposing Release").

We discuss below:

- Why a federal best execution standard that is substantially the same as the two existing rules is unnecessary.
- How the Proposal's prescriptive procedural requirements would harm retail investors, including the possibility of diverting order flow away from wholesalers and to exchanges without any demonstrable evidence that doing so would benefit investors, especially retail investors whom the Proposal intends to protect.
- How the SEC has failed to conduct an adequate cost-benefit analysis, as it is required to do by law.

I. The Proposal Is Unnecessary Because It Would Establish a Duplicative Substantive Best Execution Standard.

The Firm believes that the true and ultimate harm of the Proposal is the negative impact it will have on retail investors as discussed in detail below. However, as a baseline matter, the Proposal is duplicative and unnecessary given the existing FINRA and MSRB rules. Specifically, Rule 1100 of Proposed Reg Best Ex would establish the SEC's best execution standard: requiring a broker-dealer 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."[3] This standard is substantially identical to the standards in current FINRA Rule 5310 and MSRB Rule G-18, which require broker-dealers to "use reasonable diligence to ascertain the best market for the subject security and to buy or sell in [such/that] market so that the resultant price to the customer is as favorable as possible under prevailing market conditions."[4] The best execution standard in Proposed Reg Best Ex not only mirrors the FINRA and MSRB standards, but it also includes the identical factors that broker-dealers must consider under the FINRA and MSRB rules to evaluate their compliance with those best execution standards.

Notably, the Commission does not take the position that customers are not receiving best execution under the current regulatory framework, or that the current regulatory framework is insufficient, thereby necessitating the requirements set forth under the Proposal.[5] To the contrary, the Commission emphasized in the Proposing Release that it "believes the existing regulatory

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[3] *Id*. at 5555.

[4] FINRA Rule 5310(a); MSRB Rule G-18(a). *See id.* at 5441, n.3 (noting that "proposed best execution standard is consistent with the best execution standards set forth in FINRA and MSRB rules").

[5] Indeed, FINRA and the MSRB seem well positioned to adopt, implement, and enforce their rules governing best execution and have published online numerous guidance documents over the years. *See generally* FINRA, *5310. Best Execution and Interpositioning*, *available at* https://www.finra.org/rules-guidance/rulebooks/finra-rules/5310#notices; MSRB, *Rule G-18 Best Execution*, *available at* https://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-18.

framework concerning the duty of best execution has helped broker-dealers fulfill their duty to their customers."[6]

To the extent the Commission is concerned that the FINRA and MSRB best execution standards are not currently being met, the Commission does not need to adopt a duplicative rule. Rather, the SEC has the authority to see that the FINRA and MSRB rules are adequately enforced. Specifically, the SEC has oversight responsibility over self-regulatory organizations, like FINRA and the MSRB, and can exercise its oversight to the extent the Commission believes that FINRA and the MSRB are not ensuring that customers are receiving best execution under their respective rules.

II. The Proposal's Unduly Prescriptive Procedural Requirements Required to Demonstrate Compliance with the Proposal's Best Execution Standard Would Harm Retail Investors.

Today, wholesale market makers, such as TSS, provide significant and unique benefits to retail investors that other market participants, such as exchanges and ATSs, do not provide. While not altering the substantive best execution standard, the Proposal would create unduly prescriptive procedural and documentation requirements to demonstrate compliance with the SEC's best execution standard, particularly when it comes to so-called "conflicted transactions." For conflicted transactions, broker-dealers must, in effect, apply an ill-defined "better than best execution" standard, which requires them to identify, collect data about, and consider not only various material potential liquidity sources but also *immaterial* liquidity sources to comply with additional onerous and impractical documentation requirements. The Proposal defines a "conflicted transaction" to include any transaction executed on a riskless principal or principal basis. The definition also covers any transaction where there is payment for order flow ("PFOF") or routing to or from an affiliate. As a result, this broad definition would cover almost every transaction executed by a wholesale market maker.

The additional procedural and documentation requirements create an unworkable standard for order handling that would make wholesale market making exceptionally difficult. These requirements do not resolve the alleged conflict but do increase the burdens and costs associated with a broker-dealer's compliance with its duty of best execution. In this way, the Proposal will diminish the effectiveness of current market structure, which consists of well-established and compliance-focused execution protocols that achieve a positive overall retail execution experience today and will lead to worse execution quality for retail investors. The SEC expressly acknowledges that its new conflicted transaction requirements are so onerous that some broker-dealers will stop engaging in conflicted transactions altogether, which, as noted above, for wholesale market makers, is almost every transaction.[7] Retail investors will bear the

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[6] Proposing Release at 5441.

[7] *See id.* at 5524 ("The Commission preliminarily believes this is likely to reduce the share of retail customer order flow that is internalized because some broker-dealers that currently receive PFOF are likely to stop receiving it to become de-conflicted, and some broker-dealers that pay PFOF will internalize fewer of the orders they receive to comply with the proposal.").

consequences, which the Commission identifies as including "costs… in the form of higher commissions or reduced services."[8]

We discuss below the significant benefits that wholesalers provide today and how changes to the current execution protocols as a result of this Proposal will have deleterious impacts on the current positive retail client execution experience, thereby depriving retail investors of the superior execution quality and lower transactions costs they currently receive.

A. Wholesale Market Makers Provide Significant Benefits to Retail Investors That Are Not Available from Exchanges or ATSs.

TSS operates a wholesale market making business, regularly committing capital to execute retail orders consistently and efficiently. As a "wholesaler," TSS receives and executes retail investor orders routed to it from other broker-dealers. In furtherance of its duty of best execution owed to its customers, TSS seeks to execute those orders on the best terms reasonably available by "internalizing" them (i.e., acting as principal), routing them for execution to other venues, or a combination of the two. TSS leverages its willingness to commit capital as well as its sophisticated order routing logic and low-latency connections to numerous market centers to achieve quality executions for customer orders. Internalization is a key component of TSS's ability to deliver benefits to retail investors. Due to its ability to internalize orders and commit its own capital, TSS provides the following benefits to retail investors that an exchange or ATS do not:

- Consistent price improvement;
- Consistent size improvement;
- Rapid execution of orders;
- Consistent execution of orders for both liquid and illiquid securities; and
- Service models that provide expedient issue resolution if an order is erroneously entered or there is a trading error.

TSS frequently provides "price improvement" to marketable retail orders by internalizing them at prices better than the national best bid or offer ("NBBO")—this means that a retail investor receives a better price than the NBBO at the time they submitted the order. On average, TSS provides more price improvement more often than exchanges, as evidenced by the below table which shows that TSS's price improvement percentage is better than all identified exchanges by many multiples and more than ten times better than most major exchanges. TSS's effective/quoted percentage is also significantly better than the exchanges. The lower the effective/quoted percentage, the better the execution quality and, as a result, effective/quoted percentage is often used by regulatory agencies to assess best execution in the context of both examinations and enforcement actions.

[8] *Id*. at 5483.

Quality of Execution Statistics (Market Orders and Marketable Limit Orders)
(April-December 2022)[9]

Market Center	Improved %	Effective / Quoted %
NYSE AMERICAN	2.96	105.27
NYSE ARCA	3.74	101.93
NYSE	4.31	98.51
NASDAQ	5.59	97.44
BATS	9.88	91.91
IEX	11.58	88.64
TWO SIGMA SECURITIES	**61.54**	**69.69**

In addition, TSS frequently provides "size improvement" by internalizing orders at a share quantity that is greater than the size displayed at the NBBO. This results in the retail investor getting an overall better price for their order than they otherwise may receive by routing directly to another market center that may be executing through several price levels of quotes. Beyond that, by internalizing orders, TSS can provide consistently faster executions than other market centers. For example, from April through December 2022, TSS had an average order time to execution of 7.8 milliseconds for market and marketable limit orders sized from 1-9,999 shares in the S&P 500 Index. Because TSS can internalize orders, and because of our robust technological infrastructure, TSS is able to provide executions for orders routed to it, often with fill rates superior to many other market centers.

Even when TSS utilizes other market centers, it attains strong, consistent execution quality. When routing orders to other venues, TSS leverages sophisticated decision-making algorithms and routing technology to maximize execution quality; in this way, TSS seeks to optimize execution quality in terms of price, speed, and certainty of execution, among other factors. TSS also can break up larger orders and internalize or route child orders to other market centers both simultaneously and/or sequentially. This process seeks to optimize executions by breaking up larger orders into more manageable segments to efficiently achieve better overall execution quality for the order.

Notably, the Commission admits in the Proposing Release, as well as in the Order Competition Rule proposing release, that wholesalers, such as TSS, perform better than exchanges in all metrics that the industry uses to measure execution quality for retail orders:

> [W]holesalers appear to compare favorably to exchanges in the execution quality of orders routed to them, suggesting that execution quality could be another key factor in the decision of retail brokers to route to wholesalers. In particular, *marketable orders routed to wholesalers appear to have higher fill rates, lower effective spreads, and lower E/Q ratios. These orders are also more likely to receive price improvement and, conditional on receiving price improvement,*

[9] Figures in the table were calculated based on data from publicly available Rule 605 reports and reflect the volume-weighted averages across all reported Rule 605 order size categories.

> *receive greater price improvement when routed to wholesalers as compared to exchanges.*[10]

Despite the apparent benefits that the Commission has acknowledged wholesalers provide to retail investors, the SEC would disrupt current execution protocols and standards to the detriment of retail investors.

B. Making It Harder to Internalize Orders Harms Retail Investors.

The new procedural and documentation requirements for conflicted transactions inject complexity and ambiguity into the obligations of firms engaging in such transactions. While Proposed Reg Best Ex would establish the same substantive standard as the existing FINRA and MSRB standards, the prescriptive procedural and documentation requirements, particularly when paired with the proposed Order Competition Rule, would all but require broker-dealers (1) to route orders as agent to qualifying exchanges or ATSs, or (2) to engage in unnecessary, inefficient, and costly exercises that do not benefit retail investors to demonstrate that they have satisfied the SEC's standard. In making this policy choice, the Commission provides little consideration to the benefits wholesalers provide and that retail investors stand to lose.

As described above, the benefits that wholesalers provide include their ability to internalize customer orders to provide the end client with consistent, high-quality executions. The Proposal would make it much more costly to internalize orders by requiring, in effect, that a wholesaler complies with the "better than best execution" standard for conflicted transactions whenever the wholesaler seeks to internalize an order. The ambiguous requirement to access material potential liquidity sources as well as immaterial sources in search of better-priced liquidity will likely result in information leakage and untimely executions where the market moves against the order. By making it more costly for wholesalers due to the information leakage associated with seeking liquidity from so many sources, wholesalers will not have the same incentive to provide the execution quality benefits they currently provide to retail investors, including price and size improvement.

Many retail brokers receive PFOF from wholesalers for their retail order flow, which enables those retail brokers to subsidize retail investor trading in the form of low or zero commission trading, and to provide lower margin rates and other economic benefits to investors. Faced with the onerous procedural and documentation requirements that would be required for engaging in a "conflicted transaction," retail brokers may avoid sending orders to wholesalers altogether.

Thus, the Proposal inevitably will lead to several outcomes—all of which are harmful to retail investors: (1) fewer retail orders will receive capital commitment from wholesalers; (2) retail orders will receive less price and size improvement; and (3) retail brokers will need to determine the impact of the Proposal on any PFOF models, possibly introducing new or additional commissions or fees for and reducing services available to retail investors. Retail investors, who are the ultimate beneficiaries of the benefits wholesalers provide, will be made to bear new costs

[10] Proposing Release at 5496 (emphasis added).

in the form of worse execution quality—i.e., less price and size improvement, more price slippage, less certain executions, and slower execution times due to less frequent internalization—and increased fees for services currently being subsidized.

These costs borne by retail investors will be compounded by the Commission's other proposed rules that would significantly alter today's existing market structure. For example, the proposed Order Competition Rule would force most retail orders onto exchange "qualified auctions" before they could be internalized by a wholesaler. Like the requirements for conflicted transactions, this requirement will further challenge current execution protocols that ultimately benefit retail investors.

If more order flow is directed to exchanges as a result of this Proposal and the Commission's other proposed rules, then that consequence would not be without technology-related execution risks. As demonstrated by the Nasdaq issues during the Facebook initial public offering in May 2012, and more recently, with the NYSE exchange system failure in January 2023, these systems can and do fail.[11] However, in those cases, the total loss for investors was subject to the exchanges' limited liability thresholds. As a result, investors are often left to absorb these losses when exchanges experience systems failures. In addition to Proposed Reg Best Ex, the SEC's proposed Order Competition Rule would drive more and more order flow onto exchanges, and the tick sizes, access fees, and transparency of better priced orders proposal that would reduce tick sizes and accelerate implementation of parts of the SEC's market data infrastructure rules would substantially increase message and data traffic, increasing investors' reliance on the operation of these systems while simultaneously increasing the strain on those systems.[12] In the event of a more widespread exchange system failure in the future, investors would experience a more disparate, negative impact as a result of more order volume being routed to exchanges. However, given the limited liability protections applicable to many exchanges,[13] the potential recovery for any harm suffered by investors would be significantly limited.

C. The Proposal Would Establish Impractical or Impossible Procedural Requirements for Demonstrating Compliance with the Best Execution Standard.

Given the lack of complete and contemporaneous data available to wholesalers at the time they make internalization and other execution decisions, a broker-dealer's satisfaction of Proposed Reg Best Ex's requirements when internalizing is impractical, if not impossible. Further, it is foreseeable that examination and enforcement staff with access to more complete data through the

[11] *See* Nathaniel Popper, *Nasdaq Is Fined $10 Million Over Mishandled Facebook Public Offering*, N.Y. TIMES (May 29, 2013), https://archive.nytimes.com/dealbook.nytimes.com/2013/05/29/nasdaq-to-pay-10-million-fine-over-facebook-i-p-o/; *see also* John McCrank et al., *NYSE Glitch Leads to Busted Trades, Prompts Investigation*, REUTERS (Jan. 24, 2023), https://www.reuters.com/markets/us/some-nyse-listed-stocks-briefly-halted-trading-after-market-open-2023-01-24/.

[12] *See* Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, 87 Fed. Reg. 80266 (Dec. 29, 2022); *see also* Order Competition Rule, 88 Fed. Reg. 128 (Jan. 3, 2023).

[13] For example, NYSE Rule 18 which governs the process for compensation claims for member organizations for NYSE system failures.

Consolidated Audit Trail ("CAT") and the benefit of hindsight could unjustifiably penalize wholesalers for decisions made using the data available to them at the time.

In particular, the Proposing Release could be read to suggest that, in order to meet the SEC's best execution standard, broker-dealers must seek to execute orders at or better than the midpoint price of the NBBO. For example, the Proposing Release states:

> If wholesalers do not have a practice of routinely seeking and accessing midpoint liquidity as appropriate, the retail broker-dealer's policies and procedures could address how it takes that into account when assessing whether a wholesaler is the best market for customer orders.[14]

Going one step further, the Commission seems to suggest that internalized executions not at the midpoint may not be consistent with the Proposal's best execution standard. In this regard, the Commission writes:

> While a retail broker-dealer's decision to route orders to a wholesaler that provides price improvement may indeed be consistent with its duty of best execution in many cases, the Commission believes that customers would benefit from robust considerations by retail broker-dealers regarding, for example, the possibility of available liquidity priced at the midpoint of the NBBO at other markets.[15]

While the Firm currently does look to source midpoint liquidity, there are several problems with making midpoint price the *de facto* standard for best execution: (1) market participants do not have access to market data identifying the location of all available midpoint liquidity (whereas the SEC has a universal *ex post facto* view of midpoint liquidity through CAT against which market participants can be evaluated in hindsight); and (2) this standard favors "over"-routing to seek potential midpoint liquidity at various market centers which will result in delayed executions and could result in worse-priced executions (which the SEC has acknowledged).[16] Broker-dealers seeking midpoint liquidity at other market centers will be "flashing" those orders to the market, which does not guarantee liquidity and instead gives market participants an opportunity to step ahead of those orders (which the SEC has also acknowledged).[17] In addition, a wholesaler would be less likely to provide price improvement to orders that remain at least partially unfilled after routing because such an order would be considered "toxic"—i.e., it would be an order that has been displayed to other market participants and other market participants have declined to fill it. Once an order becomes toxic (over exposed), there is less incentive for a wholesaler to provide price improvement.

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[14] Proposing Release at 5460, n. 159.
[15] *Id.* at 5445.
[16] *See id*. at 5534.
[17] SEC, Press Release, *SEC Proposes Flash Order Ban* (Sept. 17, 2009), https://www.sec.gov/news/press/2009/2009-201.htm ("Flash orders may create a two-tiered market by allowing only selected participants to access information about the best available prices for listed securities . . . . These flash orders provide a momentary head-start in the trading arena that can produce inequities in the markets and create disincentives to display quotes.").

The Proposal requires that broker-dealers have policies and procedures "to address how it will assess potential midpoint executions, including to the extent additional midpoint liquidity emerges."[18] In connection with establishing this requirement, the Commission asserts that:

> between 46% and 73% of retail marketable order shares are internalized by a wholesaler at a price worse than the NBBO midpoint.[19]
>
> [for] stocks priced higher than $30, it appears that for between 60–93% of the shares executed by the wholesaler in a principal capacity at a price less favorable than the NBBO midpoint there was midpoint liquidity that was available on exchanges and ATSs at the time the wholesaler executed the order.[20]

However, market participants have no way to obtain real-time information about "available" (i.e., definitively capable of being executed against), sources of midpoint liquidity. Midpoint liquidity is not displayed on a market center's order book or through NMS core data or otherwise through proprietary exchange data feeds. As a result, there is a greater risk associated with routing specifically for midpoint liquidity in terms of speed and certainty of execution, and often in terms of price slippage during order handling. In pointing to substantial "available" midpoint liquidity, the Commission fails to consider the substantial uncertainty inherent in routing for such liquidity.

As noted above, by the time a broker-dealer pings various market centers for midpoint liquidity, it is very feasible that the midpoint price would no longer be the same as when the broker-dealer's search began and may in fact have moved against the customer due to information leakage to other sophisticated market participants. The SEC confirms this risk in the Proposing Release, stating: "[p]inging for midpoint liquidity at multiple venues could increase the risk of information leakage or that prices may move, possibly resulting in some market participants canceling midpoint orders they posted."[21] The Commission also fails to consider that numerous sources of that supposed "available" liquidity do not permit wholesalers to route to them (e.g., venues with order size stipulations) and that connecting to significantly more market centers may be cost-prohibitive, particularly for smaller-sized broker-dealers.

The Commission's emphasis on midpoint liquidity creates a presumption that executions not at or better than the midpoint price are somehow subpar and suggests that such executions will be heavily scrutinized absent having routed for midpoint liquidity to numerous, or perhaps all, potential market centers. The Commission's examinations and enforcement staff will have the ability to compare firms' order handling and prices achieved with prices present in CAT data,

[18] Proposing Release at 5460.
[19] *Id*. at 5445, n.52.
[20] *Id*. at 5445. The Commission uses CAT data to establish these data points in support of the Proposal yet has refused to allow market participants access to this data so that they can perform their own evaluations of the Commission's justification of the Proposal despite a recent FOIA request to obtain this information. Further, the Commission did not take various factors into consideration, such as the tiering and minimum size execution requirements. For example, many resting midpoint institutional orders have a minimum size that would rule out most retail orders.
[21] *Id*. at 5502, n.429.

which provides a more comprehensive view of the market and is not available to market participants contemporaneous with order execution.

For the reasons set forth above, the Proposal's impact would greatly disrupt the current transparent order handling and execution protocols. A consequence may be that more retail order flow will be directed to a small handful of exchanges and ATSs, which are not responsible for guaranteeing best execution, and as a result, investors would receive worse and less certain executions and pay higher transactions costs, including higher commissions and exchange fees.

III. The SEC Failed to Justify the Need for Regulatory Action or Conduct an Adequate Cost-Benefit Analysis.

Section 3(f) of the Securities Exchange Act of 1934 requires the SEC to "consider or determine whether an action is necessary or appropriate in the public interest" and "in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation." The Proposal does not satisfy these objectives. Relatedly, the Commission is required to justify the costs imposed by any rulemaking by weighing them against the corresponding benefits—which the Commission has not done. To the contrary, the Proposal would impose a federal best execution standard with costly requirements for demonstrating compliance that has no known benefit and instead, as described above, has the potential to cause significant harm to retail investors.

As one Commissioner observed, "the Commission itself is not confident [the Proposal] will help brokers achieve even better—much less best—execution."[22] Nor could it be. The Proposing Release contains no quantitative data demonstrating that the Proposal's requirements would improve the execution quality received by retail investors. The Commission claims that it cannot do the required analysis because it "lacks detailed data on broker-dealers' current order handling practices and documentation practices that would allow it to predict the extent of changes as a result of this proposal."[23] Specifically, the SEC states it lacks (1) data regarding whether and to what extent broker-dealers already document order handling for fixed income and other non-NMS securities asset classes; (2) information about what information broker-dealers evaluate in making routing decisions; and (3) how specific customer and order characteristics affect order handling.[24] The SEC's concession that it has not conducted the required economic analysis to satisfy its basic rulemaking obligation should render the Proposal presumptively invalid as a statutory matter. Moreover, the SEC's claim that it cannot meet its basic rulemaking obligation because it "lacks the information necessary" is not reasonable. The SEC has the responsibility, authority, and ability to collect the information it says it lacks if it wants to proceed with rulemaking.

To the extent the Commission addresses the potential benefits of the new procedural requirements in the Proposing Release, the Commission acknowledges that they may be *de*

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[22] Comm'r Hester M. Peirce, *Is This the Best Execution We Can Get?* (Dec. 14, 2022), https://www.sec.gov/news/statement/peirce-best-execution-20221214.

[23] Proposing Release at 5523; *see also id.* at n.535 ("Commission lacks quantifiable data that summarizes how order handling data are currently documented . . ..").

[24] See *id*.

minimis. For example, the SEC notes its belief that at least some broker-dealers already consider the required information,[25] *in which case there would be minimal, if any, benefits* to implementing Proposed Reg Best Ex. With regard to the substantial documentation requirements, the SEC expressly acknowledges in the Proposing Release that any potential benefits "may be small."[26]

At the same time that the SEC fails to quantify any benefits, it also fails to reasonably consider the costs associated with the Proposal. As explained above, we are concerned that the increased costs to broker-dealers will result in higher costs passed on to and a diminished execution quality experience for investors, particularly retail investors. In fact, the Commission notes that such requirements may result in "higher barriers to entry and potential exit of small broker-dealers," contrary to the Commission's mandate to enhance competition.[27]

In addition, the SEC fails to sufficiently consider the costs associated with overlapping and duplicative regulation. While the SEC's proposed best execution standard is substantially identical to the best execution standards set forth in FINRA and MSRB rules, the Commission has not considered the costs imposed on broker-dealers to comply with three separate best execution rules and potential differences in interpretation by the SEC, on the one hand, and FINRA and the MSRB, on the other. FINRA and the MSRB have indicated that they would harmonize their best execution rules with the Commission's best execution rule; however, harmonization will not eliminate the potential for interpretive differences as to the three rules among the regulators.

For all of these reasons, the Commission has not demonstrated that the Proposal is necessary or appropriate.

IV. <u>Conclusion</u>

We appreciate the need for a robust best execution standard, but Proposed Reg Best Ex, despite its name, would not achieve best execution. The current FINRA and MSRB frameworks are both appropriate and sufficient for achieving this goal and in fact have effectively produced strong execution quality and low transaction costs for investors. Proposed Reg Best Ex, on the other hand, would introduce significant new costs and worsen execution quality without generating corresponding benefits for investors. Therefore, the SEC should not adopt the Proposed Reg Best Ex but rather, should rely on the existing FINRA and MSRB rules, along with the accompanying guidance, that they have approved.

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[25] *Id*. at 5534.

[26] *Id*. at 5525.

[27] *Id*. at 5523.

We would welcome the opportunity to discuss this letter and engage in further dialogue with the Commission on these topics.

Respectfully submitted,

Sandip Khosla

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Sandip Khosla, Esq.
General Counsel