September 26, 2016

Mr. Brent Fields
Deputy Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Release No. 34-78309; File No. S7-14-16; Disclosure of Order Handling Information

Dear Mr. Fields,

The Security Traders Association ("STA")[1] appreciates the opportunity to offer comments on the Securities and Exchange Commission ("Commission" or "SEC") proposed rule on Disclosure of Order Handling Information; File No. S7-14-16 (the "Proposal"). The Proposal seeks to amend Rules 600 and 606 of Regulation National Market System ("Regulation NMS") under the Securities Exchange Act of 1934 ("Exchange Act") to require new and additional disclosures by broker-dealers to retail and institutional customers about the routing of their orders. The Proposal would require broker dealers to disclose routing and execution information upon request from its customers and to also make certain reports publically available. In addition to representing the interests of our members on matters relating to the Proposal, STA is also a member of the Financial Information Forum ("FIF"[2]) Rule 605/Rule 606 Working Group and supports many of the recommendations found in their letter.

Executive Summary

STA is supportive of the Proposal however, we would make the following recommendations:

- The enhanced disclosures on payments and fees on retail customer orders should be provided in a more general disclosure format for retail customers to consume.
- The determination of retail customer and institutional customer should be based on a format other than order size.

[1] The STA is a trade organization founded in 1934 for individual professionals in the securities industry and is committed to promoting goodwill and fostering high standards of integrity in accord with the Association's founding principle, Dictum Meum Pactum – "My Word is My Bond"

[2] The Financial Information Forum (FIF) addresses the implementation issues that impact the securities industry across the order lifecycle. FIF provides a collaborative environment for subscribers to make an impact on industry issues affecting operations and technology.

- The Commission should provide clarity on the level of obligation a broker-dealer who provides algorithm trading services will have to a broker-dealer who is using these services in the course of executing orders on behalf of their institutional customers.
- The categorization of algorithms should not be included in the final rulemaking.
- Proposed amendments to Rule 606, which require the public availability of reports, should be limited to non-directed orders.
- Reporting exemptions for brokers and dealers with di minimis amounts of institutional orders or customers should be allowed.

General Remarks:

Regulatory role in creating industry standards

STA generally supports the Proposal as it pertains to the new disclosure requirements by broker-dealers to institutional customers and enhanced disclosures to retail customers. Specific to institutional customers, STA believes the Proposal seeks to address certain informational gaps and inconsistencies which currently exist. The STA applauds the Commission for taking this proactive step and believe statements in the Proposal which describe the current disclosure regime are consistent with views expressed in STA's letter to the Financial Stability Oversight Council, dated March 23, 2015[1] where we stated:

> *The advancement of technology and its ability to capture and record large amounts of data has yielded tremendous benefits to the asset management industry. A manager's ability to measure and monitor factors critical to operating their business has improved since 2008.* However, *it is STA's general view that there is an affordability gap in the technological resources and budgets of large managers compared to small and mid-sized managers (as identified as $10 billion in AUM or less). While STA acknowledges that there will always exist a gap in the resources, it is our view that this gap can and should be narrowed…*
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> *The STA believes benefits can accrue to individual investors when regulators, with industry input, define industry standards in appropriate areas. Having defined regulatory industry standards ensures information is accurate and uniformly available. In addition, such standards foster private market solutions which transcend to lower costs.*

"Customer Experience"

The expression, "customer experience" is a relatively new, but common expression used by and among retail brokerage firms. STA believes this expression deserves explanation because we believe that the primary catalyst for retail customers in determining where to execute their trades is the comprehensive experience they have with their executing broker-dealer, which includes but is not limited to the explicit and implicit costs of executions. The retail brokerage industry is robust and highly competitive. Retail customers have a number of retail brokerage firms to choose from. In addition, service providers to retail brokerage firms compete vigorously

[1] Letter to Financial Stability Oversight Council March 23, 2015

for their order flow. Combining both quantitative and qualitative factors yield benefits to retail customers who care greatly about the quality of their execution. While the Proposal seeks to provide these customers with additional disclosures not afforded them today, it is STA's view that the primary source of information used by retail customers is and will continue to be that obtained through their experiences with the broker executing their trade.

Disclosure and Transparency

STA believes there are tremendous benefits to institutional and retail customers when transparency achieved through accurate and uniform disclosures is provided in the context of what the customer needs and is looking for. However, STA believes that when levels of disclosures are voluminous and contain elements of subjectivity, it can become difficult for customers to find the transparency they are looking for, namely actionable data to enable a thoughtful choice. STA generally supports the new and standardized reporting elements for institutional order handling described in the Proposal and believes they will close what we perceive as an affordability gap between order routing information that large institutional customers can obtain versus small- to mid-size institutional customers with fewer resources. However, STA has reservations if the proposed enhanced reporting requirements by broker-dealers to retail customers, which require the disclosure of net aggregate amounts of any payments for order flow received, payments from any profit-sharing relationship received, transaction fees paid, and transaction rebates received by a broker-dealer from certain venues, will contribute favorably to transparency for retail customers due to the voluminous amounts of information they will produce.

STA recognizes such disclosures enable investors to recognize conflicts of interests; however, we believe that investors would be better served with a less voluminous and complex means of obtaining this information, such as a general disclosure of such arrangements. Should the Commission deem it necessary to have this information disclosed, STA would recommend that as part of its final rulemaking the Commission include a review of the level of inquiries by retail customers and a commitment to cease this particular regulatory disclosure requirement should the levels of inquiries be de minimis. STA believes that twelve (12) months is a reasonable period of time to determine if there are sufficient benefits, as measured by the levels of inquiries, compared to costs of maintaining this reporting regime. Information on 606 Order Routing Disclosure is readily attainable today as many retail and full service brokerage firms who offer a self-directed platform are able to this track activity.

Defining Retail and Institutional

The Proposal separates disclosure on order routing and execution based on customer type (either retail or institutional) and uses criteria based on trade size to determine one customer type over the other. Some market participants disagree with this approach of customer segregation and recommend the Commission should instead focus on the methods of handling specific orders. Some of these participants recommend using a format based on held vs not-held orders to efficiently segregate order flow so as to provide routing disclosure information in the context of what institutional and retail investors are seeking.

At this time, STA does not have a formal recommendation on which format or which approach - customer type or specific order type - would be the most efficient means to achieve the goals of the proposal. However, STA makes the following statements:

- STA recognizes that regardless of which approach or format the Commission uses to segregate order flow, there will be some level of duplication or shortfall in capturing routing and execution data from retail and institutional customers. STA recommends the Commission, with industry input, choose an approach and format which presents the most de minimis level of duplication and shortfall in data.
- STA believes that the vast majority of orders entered by institutional customers are with not-held instructions and the vast majority of orders entered by retail customers are entered with held instructions.
- The Commission should not use a format based on order size for determining retail or institutional clients, be it the one defined in the Proposal or any other order size levels. STA agrees with remarks in FIF's letter that doing so will, *"…cause investors to receive incomplete information: 1) many orders submitted by retail investors will exceed $200,000, and therefore be omitted from the "retail" report, yet appear on the "institutional" report; and, 2) because many institutions split their orders into smaller pieces (less than $200,000) before submitting to multiple broker-dealers, they will be omitted them the institutional report and be included instead on retail reports.*
- If it is deemed necessary at all to distinguish between retail and institutional customers, STA recommends that for retail customers the Commission should either adopt or modify FINRA's Rule 4512(c) as the single definition across regulators.
- STA understands there is a desire for institutional customers to use a Large Trader ID ("LTID") under Rule 13h-1. STA is concerned this approach would result in considerable overlap with the number of customers who meet the definition of retail customer under FINRA Rule 4512(c) who also have a LTID.

Customer-specific report on institutional order handling

The Proposal would require a broker-dealer to provide its institutional and retail customers upon request a report on the broker-dealer's handling of their orders. Today, many small- to mid-size broker-dealers use trading algorithms provided by other broker-dealers to execute orders on behalf of institutional customers. In a majority of these situations, the institutional customer also has a direct trading relationship with the broker-dealer who provides the trading algorithm. The Proposal is unclear whether the broker-dealer who provides the algorithm trading services would be required to provide a routing and execution report to the broker-dealer who is executing of behalf of the institutional customer. STA respectfully asks that the Commission provide clarity on the level of obligation a broker-dealer who provides algorithm trading services will have to the broker-dealer who is using these services in the course of executing orders on behalf of their institutional customers.

Assigning categories to algorithms

STA believes that disclosure of information produced from assigning categories to algorithms is unnecessary and will result in institutional customers capturing information they do not find useful. Institutional customers are focused on the performance of algorithms as measured by actual trading activity rather than how the algorithm is categorized.

Additionally, STA is concerned that there will be an element of subjectivity by broker-dealers categorizing algorithms, which may result in conflicting information. The Commission recognizes this in the Proposal, when it states:

> *However, the Commission preliminarily believes that the potential inconsistencies of categorization would only occur at the margins among order routing strategies, where characteristics of the strategy could be viewed differently by different broker-dealers.*

STA believes the inconsistencies will occur more often than described in the Proposal. Broker-dealers who outsource algorithm trading services regularly customize a trading strategy for a single institutional customer or a group of institutional customers by mixing or combining the trading strategies offered by a single or multiple provider(s). This customization and mixing process will increase the level of inconsistencies across broker-dealers because a customized strategy may have components described as passive, neutral and aggressive in the Proposal included in one strategy. STA therefore recommends not requiring categorization of algorithms in the final rulemaking.

Directed and Non-Directed Orders

Currently, Rule 606 of Regulation NMS limits the required public disclosure of a broker-dealer's order routing information to non-directed orders in NMS securities that are in amounts less than (i) $200,000 for NMS stocks, and (ii) $50,000 for option contracts. To facilitate enhanced transparency, the Proposal seeks to amend Rule 606 to include institutional orders. The Proposal does not articulate whether the amended public disclosure will be limited to only non-directed orders, or will include directed and non-directed orders. As stated in the Proposal:

> *(c) Quarterly report on institutional order handling. A broker or dealer that receives institutional orders shall make publicly available a report that aggregates the information required by paragraphs (b)(3) of this section, whether or not requested by a customer, on its handling of <u>all institutional orders</u> for all customers for each calendar quarter by calendar month within one month after the end of the quarter.*

STA seeks clarity on the Commission's intent and recommends that public disclosure on institutional orders be limited to non-directed orders. Institutional customers seek transparency on order routing and execution in those situations where the broker-dealer exercises discretion. Segregating non-directed orders from all orders produces a more qualitative level transparency that institutional customers seek. STA would encourage the Commission to follow the approach it has taken in Rule 606(a) and exempt directed orders from public reporting as the broker-dealer has no discretion related to those orders and their inclusion in a public report could distort the statistics the Commission is seeking to make publicly available.

Di minimis exemptions

STA recommends that exemptions to Rule 606 reporting be granted to broker-dealers with either a de minimis amount of institutional customers or a di minimis amount of institutional activity as measured by executed shares as a percentage of all executed shares. (See STA's responses to questions 75 and 76 in the Appendix.)

Conclusion

The STA appreciates the opportunity to comment on the Proposal. We acknowledge and thank the Commission and all the staff responsible for designing the requirements for the worthy policy goal which the Proposal seeks to address. We look forward to working with the Commission on the final design and implementation of the Proposal.

James Toes

John Russell	**James Toes**
Chairman of the Board	**President & CEO**

Appendix:

Question #10
Instead of defining institutional order, do commenters believe that there are alternative approaches that the Commission should consider in structuring order handling disclosures for large orders? If so, please explain the approach in detail, including the benefits and costs of the approach.

Response:
STA recognizes that regardless of which approach or format the Commission uses to segregate order flow, there will be some levels of duplication or shortfalls in capturing routing data from retail and institutional customers. STA would recommend that the Commission identify other approaches and formats and then, with industry input choose the approach and corresponding format which presents the most de minimis levels of duplication and of shortfalls in capturing data.

Question #31
Do commenters believe that disclosure of order routing strategies categorized by passive, neutral, and aggressive would be useful? Should any of these proposed categories be modified or deleted? Are there other categories of strategies that would be more meaningful? Please explain and provide data to support your arguments.

Response:
STA believes that institutional customers are focused on the performance of algorithms as measured by actual trading activity rather than how the algorithm is categorized. Therefore, we do not believe categorizing order routing strategies will be useful.

Question #34
Do commenters believe that customers would have sufficient information to meaningfully compare how their institutional orders were handled by different broker-dealers in light of the fact that each broker-dealer would establish its own categorization of routing strategies?

Response:
STA believes that the subjective nature of broker-dealers assigning categories to their routing strategies will make evaluating and comparing strategy categories across different broker-dealers inefficient.

Question #35
Do commenters agree that potential inconsistencies of categorization will only occur at the margins and grouping order routing strategies by the three broad categories would still allow for meaningful comparison of order handling practices across broker-dealers?

Response
STA believes that inconsistencies will be greater than at the margin. Broker-dealers who outsource algorithm trading services regularly customize a trading strategy for a single institutional customer or a group of institutional customers by mixing or combining the trading strategies offered by a single or multiple provider(s). This customization and mixing process will increase the levels of inconsistencies across broker-dealers because a customized strategy may have passive, neutral and aggressive components included in one strategy.

Question #64
Do commenters believe that disclosing the average net execution rebate or fee for shares of orders providing liquidity at each venue and by order routing strategy would be useful in assessing potential conflicts of interest broker-dealers may face with regard to routing venues and the order routing strategies that use those venues?

Response
STA does not believe the enhanced disclosures on fees and rebates for retail orders will contribute favorably to transparency for retail customers due to the voluminous amounts of information they will produce. STA believes that retail customers would be better served with a less voluminous and complex means of obtaining this information, such as a general disclosure of such arrangements. In addition, metrics do not easily capture some other benefits that retail brokers obtain in the course of serving their customers when routing to certain destinations, such as the liability protection that multiple market participants provide if there is an outage or other market or technological event at one or more other market venues.

Question #75
Do commenters believe that the rule should include a de minimis exemption for broker-dealers that receive, in the aggregate, less than a certain threshold number or dollar value of institutional orders? Why or why not? If so, what would be the appropriate threshold number or dollar value of institutional orders a broker-dealer should need to receive from all customers in the aggregate before it would be required to provide the public order handling reports? Please explain. Separately, are there alternative approaches to reduce the compliance costs on broker-dealers with few institutional customers? Please provide data to support your arguments.

Response
Yes, STA believes that broker-dealers with a di minimis amount of institutional activity, as measured by institutional shares executed as a percentage of all shares executed should be

exempt from reporting institutional orders. Should the Commission decide to identify institutional orders as those orders with not-held instructions, STA would recommend that broker-dealers with a di minimis amount of not-held orders be exempt from reporting. STA believes that a majority of these will exemptions would be for retail brokerage firms. STA does not believe institutional customers find these levels of reporting to be meaningful therefore we recommend an exemption be granted.

Question #76

Regarding broker-dealers with a small number of institutional customers, do commenters believe there is a potential risk of exposing the customer's sensitive, proprietary information in an aggregated report? Should the Commission make any modifications to the proposed disclosures or eliminate any or all of the proposed requirements under certain circumstances? If so, what is the appropriate measure? Please provide support for your argument.

Response

While we appreciate the steps the Commission has taken to attempt to protect customers' proprietary information and trading strategies from being reverse-engineered, STA does not believe any public reporting can be safely made on order routing information when a broker-dealer services so few customers. In November 2010 the Commission adopted Rule 15c3-5, the Market Access Rule, which prohibits broker-dealers from providing unfiltered, or "naked" access, to an exchange or ATS. Since the adoption of Rule 15c3-5, a business model whereby an institutional customer who manages a portfolio based on low latency, quantitative strategies and executes through one broker-dealer developed. The broker-dealer often has some affiliation with the institutional customer and does not maintain many, if any, other institutional customer relationships. Even in the aggregate and on a quarterly basis, the proposed public disclosure could expose the small number of institutional customers each broker-dealer services to the risks associated with the leakage of proprietary information that comes from having sophisticated parties reviewing their aggregated order routing information.

As a result we would encourage the Commission to create a de minimis exception from public reporting for broker-dealers with ten or fewer institutional customers.