March 31, 2023

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

Re: Disclosure of Order Execution Information (File No. S7-29-22, RIN 3235-AN22)

Dear Ms. Countryman:

Better Markets[1] appreciates the opportunity to provide comment on the above-captioned proposed amendments to the disclosures required under Rule 605[2] of Regulation NMS for order executions in national market system stocks, which are stocks listed on a national securities exchange. The Commission's proposed rule changes on the Disclosure of Order Execution Information (the "Proposal") was published by the Securities and Exchange Commission ("SEC" or "Commission") in the Federal Register on January 20, 2023 (the "Release").[3]

The simple fact is that in today's securities markets, many investors—especially retail investors—are not getting the best available prices for their orders to buy and sell stock. This state of affairs has arisen from a number of inter-related factors, but prominent among them is a lack of transparency regarding the way orders are routed in today's complex and fragmented markets, where incentives and conflicts of interest between brokers, wholesalers, and other market participants abound. The SEC's Rule 605 on the disclosure of order routing and executions was first implemented over two decades ago to help the public compare and evaluate execution quality among different market centers. But that rule has fallen well behind the dramatic changes in the structure of the markets and the advances in technology that now allow for lightning fast and automated execution of securities trades.

The Proposal will provide sorely needed updates and enhancements to Rule 605 for the benefit of retail investors and the market overall. In short, Better Markets agrees that modernized

---

1 Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

2 17 CFR § 242.605.

3 Disclosure of Order Execution Information, 88 Fed. Reg. 13, 3786 (Jan. 20, 2023).

1825 K Street, NW, Suite 1080, Washington, DC 20006 TELEPHONE (1) 202.618-6464 FAX (1) 202.618.6465 WEBSITE bettermarkets.com

and enhanced execution quality reporting as proposed would improve the public's ability to compare and evaluate execution quality among different market centers and broker-dealers. In short, these reforms will increase transparency of order execution quality, ultimately improve execution quality, and help promote fair competition among market centers and broker-dealers.

BACKGROUND

Over the past two decades, the U.S. Equity markets have increasingly suffered from a long list of unfair trading practices and structural features that have become ingrained in the markets, including conflicts of interest, payments for order flow, minimal order competition, poor execution prices, limited transparency into order routing practices, predatory high-frequency trading, severe trading venue fragmentation, and increased trading on dark markets. Collectively, these practices take billions of dollars out of Americans' pockets every year in incremental losses due to subpar order executions. The market resembles a vast predatory ecosystem underpinning too much of modern finance, including the anti-retail trader and anti-buy side practices enabled by a rigged market structure.

In December 2022, the SEC proposed a set of four related reforms that promise to help solve or at least mitigate some of these harmful market characteristics and practices. They would 1) establish a new SEC "best execution" requirement; 2) require at least some types of orders to be exposed to competition in fair and open auctions before they can be executed internally; 3) expand the monthly reporting on execution quality that firms must make; and 4) reduce the minimum pricing increment at which stocks may be quoted and trade, so that buyers and sellers can get better prices on their trades. In this comment letter we address the third of these reforms, the disclosure of order execution information.

The need for reform has grown steadily over two decades as the markets and trading technologies have changed dramatically since the order execution reporting requirements were first adopted.

- As the Commission observes in the Release, the markets become far more fragmented as market shares of individual national securities exchanges became less concentrated and an increased percentage of order flow moved off-exchange. In 2000, there were nine registered national securities exchanges and one registered national securities association. Order flow was routed to a few, mostly manual trading centers, highly concentrated in the primary listing exchanges. Today, however, trading is highly automated and spread among different types of trading centers: national securities exchanges operating SRO trading facilities, ATSs that trade NMS stocks, exchange market makers, wholesalers, and broker-dealers that execute orders internally by trading as principal or crossing orders as an agent. There are sixteen national securities exchanges, 32 NMS Stock ATSs, and over 230 FINRA members.[4]

- Further, as the Commission notes, there have been significant developments in trading since Rule 605 was adopted. It is now done electronically with automated systems and the

[4] Release at 3791.

speeds have increased exponentially, measured in milli or microseconds, not mere seconds. Furthermore, odd-lots and fractional shares, along with stock prices, have continued to increase over time. Odd-lot quotes in higher-priced stocks continue to offer prices that are frequently better than round lot NBBO. Odd-lot rates have also increased among lower priced stocks. Because current Rule 605 size categories exclude orders smaller than 100 shares, a significant proportion of market activity is not captured under the current reporting regime.[5]

- The participation of retail investors has increased significantly over the past twenty years. As discussed in the Release, financial inducements to attract order flow from broker-dealers that receive retail investor orders, *i.e.*, "payment for order flow" ("PFOF"),[6] have become more prevalent. Such inducements may be significant sources of revenue, and they create significant conflicts of interest. Broker-dealers that primarily service the accounts of retail investors often route the marketable orders of retail investors in NMS stocks to wholesalers. Wholesalers may provide different execution quality to different broker-dealers.[7]

As a result of this evolution, the current reporting requirements regarding execution quality have become outdated. They simply do not capture enough information about how orders are routed and executed in today's modern markets. They, therefore, do not adequately serve or advance the overarching policy goals that Congress sought to archive when it provided for a "national market system":

> "The national market system objectives of Section 11A of the Exchange Act include the economically efficient executions of securities transactions; fair competition among brokers and dealers, among exchange markets, and between exchange markets and markets other than exchange markets; the availability of information on securities quotations and transactions; and the practicability of brokers executing investor orders in the best market."[8]

Among the most significant gaps in the current Rule 605 reporting regime is the exclusion of broker-dealers, orders made by smart order routers that may not be located within a market center, the granularity of the information in terms of the information required and the applicable timing increments, the dichotomy between reporting order sizes based on number of shares versus odd lots, and the potential non-reporting of fractional share orders. The Proposal is a generally well-crafted solution that will assist in closing these gaps and ultimately help ensure that our securities markets are more fair to retail investors, competitive for market participants, efficient, and transparent.

---

5 Release at 3792.

6 *See* Better Markets "Fact Sheet: A Real Robin Hood On Wall Street Markets: Democratizing Equity Markets Without Exploitation" for a review of the harms associated with PFOF.

7 Release at 3791 n.

8 Release at 3787.

OVERVIEW OF PROPOSAL

The Proposal would increase transparency by ensuring that additional information is disclosed on a monthly basis about how investor orders are actually executed in the markets. Specifically, the proposed amendments would:

- Expand the scope of entities subject to Rule 605 by requiring broker-dealers with more than 100,000 accounts,[9] single dealer platforms, and entities that would operate qualified auctions under a related rule proposal to make available to the public monthly execution quality reports.

- (i) expand the definition of "covered order" to include certain orders submitted outside of regular trading hours, certain orders submitted with stop prices, and non-exempt short sale orders; (ii) modify the categorization of order sizes to be reported to base them on round lots for greater content clarity, and include additional order size categories for fractional share, odd-lot, and larger-sized orders; and (iii) create a new order type category for marketable immediate-or-cancel orders and replace three existing categories of non-marketable order types with three new categories of order types).

- Amend the content of the reports required under Rule 605 to (i) revise time-to-execution categories in favor of average time to execution, the median time to execution, and 99th percentile time to execution statistics, each as measured in increments of a millisecond or finer; (ii) require new realized spread statistics; and (iii) require new statistical measures of execution quality that could be used to evaluate price and size improvement for all order types and additional price improvement statistics for market and marketable order types.

- Enhance the accessibility of the required reports by requiring all entities subject to Rule 605 to make a summary report available that would be formatted in the most recent versions of the XML and PDF formats as published on the SEC's website.

Overall, the Disclosure of Order Execution Information proposal would expand the quantity and quality of disclosure pursuant to Rule 605, thus increasing the ability of investors and other market participants to compare and evaluate execution quality, as measured by several factors, including price and speed.

COMMENTS

I. EXPANDING THE SCOPE OF ENTITIES SUBJECT TO RULE 605, AS PROPOSED, IS NECESSARY AND APPROPRIATE.

Current Rule 605 requires "market centers" to provide monthly reports concerning the execution quality for covered orders in NMS stocks. Reg NMS defines a "market center" as any

9 As Table 13 at 3887 of the Release shows, approximately 85 broker-dealers introduce or carry more than 100,000 customer accounts and these broker-dealers together handle over 98.5% of customer accounts.

exchange market maker, over-the-counter ("OTC") market maker, alternative trading system ("ATS"), national securities exchange, or national securities association.

The proposed amendments would expand the scope of entities subject to Rule 605 by requiring broker-dealers with more than 100,000 accounts, single dealer platforms ("SDP"), ATSs,[10] and entities that would operate qualified auctions – being proposed separately under the Order Competition Rule to make available to the public monthly execution quality reports.

Better Markets supports this expansion of entities subject to Rule 605 disclosures as it will help the public compare and evaluate execution quality among different market centers and broker-dealers and thereby increase transparency of order execution quality, increase the information available to investors, and help promote competition among market centers and broker-dealers. Indeed, as the Commission notes, the Proposal will benefit not only retail investors but institutional investors as well.[11] While institutional investors currently have access to alternative sources of execution quality information through Rule 606(b)(3) reports and transaction cost analysis, that information is limited to execution quality obtained from broker-dealers with which the institution investor currently does business. As Rule 605 reports are public, expanding the class of entities making disclosure will allow institutional investors to compare the execution quality of broker-dealers and market centers with which they do not currently do business.

Better Markets does believe that it would be useful for customers of certain broker-dealers to be able to review Rule 605 reports specific to those broker-dealers instead of relying on execution quality statistics reported by the market centers to which the broker-dealers route orders because Better Markets agrees that market centers may provide different execution quality to orders based on the routing broker-dealer based on PFOF arrangements.[12] Expansion of Rule 605 reports would thus allow broker-dealer customers to view the material aspects of their firm's PFOF arrangements.[13] Furthermore, broker-dealer specific Rule 605 reports will shed far more light on the order execution quality that retail investors are receiving than the current two-step Rule 605/Rule 606 process that obscures actual order execution quality data on an individual-broker dealer and individual customer basis.[14]

---

10 The Proposal suggests, and Better Markets agrees, that requiring SDPs and ATSs to produce Rule 605 reports independently from their broker-dealers operations would increase transparency by allowing market participants to distinguish such activity from more traditional broker-dealer activity. Release at 3803.

11 Release at 3831, n.507.

12 Release at 3800, q.1. Better Markets also believes that broker-dealers that are also market centers should be required to separately report their market center functions for all cover orders. (*See* Release at 3800, q.2).

13 Release at 3796, n.153.

14 Better Markets also agrees with Professors Christopher Schwarz, Brad Barber, Xing Huang, Philippe Jorion, and Terrance Odean, who have conducted empirical research in this field, that broker-dealers with multiple account types, and varying account fee structures, should have to file separate Rule 605 disclosures for each account type to reflect the observation that execution quality differs across platforms with different commission and PFOF structures. (*See* Comment Letter of Professors Christopher Schwarz, Brad Barber, Xing Huang, Philippe Jorion, and Terrance Odean, dated February 7, 2023).

II. THE DEFINITION OF "COVERED ORDER" SHOULD BE FURTHER EXPANDED, THE CATEGORIZATION OF ORDER SIZES SHOULD BE BASED ON ROUND LOTS, AND THE ORDER TYPE CATEGORIES SHOULD BE REORGANIZED, AS PROPOSED.

Currently, Rule 605 reports organize disclosed order execution information for an individual security based on one of five order types and one of four order sizes. The Proposal would significantly modify this by requiring more detailed quality statistics regarding price and size.

Specifically, the proposed amendments would expand the definition of "covered order" to include (i) non-marketable limit orders ("NMLOs") received outside regular trading hours or while a national best bid and offer ("NBBO") is not being disseminated, if they became executable during (and were not executed outside of) regular trading hours;[15] (ii) executable orders with stop prices; and (iii) non-exempt short-sale orders unless a price test restriction is in effect for the security. This expanded definition of "covered order" would allow for more robust and useful disclosure to market participants. However, we believe that the Commission should further expand the definition of "covered order" to include securities whose quote is disseminated via the Securities Information Processor, which includes any fund security ("ETF") listed on an SEC registered exchange, ATS, or SDP.

The Proposal would also modify the categorization of order sizes to be reported so that they are based on round lots[16] instead of number of shares for greater content clarity, and include additional order size categories for fractional share, odd-lot, and larger-sized orders. The new order size categories would be (i) less than one share;[17] (ii) odd-lot;[18] (iii) one round lot to less than five round lots;[19] (iv) five round lots to less than twenty round lots; (v) twenty round lots to less than fifty round lots; (vi) fifty round lots to less than one hundred round lots; and (vii) one hundred round lots or more. Better Markets agrees that basing the order size categories on round lots not only harmonizes Rule 605 disclosure consistent with the 2020 rule amendments that established a price-based definition of "round lot" but also better enables Rule 605 reports to group orders in a way that provides useful order execution information.

Finally, the proposed amendments would create a new order type category for marketable immediate-or-cancel orders and replace three existing categories of non-marketable order types with three new categories of order types, thus replacing the five current order type categories:

(i) Market;
(ii) Marketable limit;
(iii) Inside-the-Quote Limit;

---

15 Orders received in a prior month, but which remained open, would also need to be included in Rule 605 reports. Release at 3805.

16 In 2020, the Commission adopted rule amendments that established a price-based definition of "round lot."

17 These order sizes are not currently reflected in a Rule 605 report.

18 These order sizes are not currently reflected in a Rule 605 report.

19 The prior Rule 605 report order size categories were (i) 100 to 499 shares; (ii) 500 to 1999 shares; (iii) 2000 to 4999 shares; (iv) and 5000 shares or more.

(iv) At-the-Quote Limit; and
(v) Near-the-Quote Limit.

with six new order type categories that are better designed to capture useful order execution information:

(i) Market;
(ii) Marketable Immediate or Cancel;
(iii) Marketable Limit;
(iv) Beyond-the-Midpoint Limit;
(v) Executable NMLO; and
(vi) Executable Stop.

This too is a beneficial change to Rule 605.

III. AS PROPOSED, THE CONTENT OF THE RULE 605 REPORTS SHOULD BE REVISED TO BETTER DISCLOSE SPEAD AND PRICE INFORMATION TO INVESTORS

The Proposal would amend the content of the reports required under Rule 605 for all order types by:

(i) eliminating the current "time-to-execution" buckets and instead require the reporting of share-weighted average time to execution for non-marketable order types (in addition to reporting of this metric for marketable order types, as is currently required), as well as statistics regarding the distribution of execution times within each order type (*i.e.*, the share-weighted median and 99th percentile time-to-execution);

(ii) requiring new average realized spread statistics for 15 second and one minute realized spreads instead of five minutes after execution spreads as currently required;

(iii) reporting of average effective spreads and, for certain orders (*i.e.*, executable NMLOs, beyond-the-midpoint-limit orders, and executable stop orders), calculation of this metric from the time the order becomes executable;

(iv) reporting of average realized spread and average effective spread as percentages, in addition to reporting in dollar amounts, as is currently required;

(v) calculating a statistic for average effective over quoted spread (“E/Q”), expressed as a percentage, which would represent how much price improvement an order received;

(vi) adding a benchmark metric that would, in combination with information about execution sizes, indicate the level of size improvement (*i.e.*, whether orders received an execution greater than the displayed size at the quote);

(v) reporting of riskless principal orders as executed at another venue, rather than as executed at the market center, broker, or dealer that, to fulfill the customer order, submits a principal order to an away market center.

The Proposal would also require certain additional information for market, marketable limit, marketable IOC, and beyond-the-midpoint limit orders. Specifically, the Proposal would first add a definition for "best available displayed price" and two new terms related to this definition. The Proposal would also add to Rule 605(a)(1)(ii) additional price improvement statistics specifically related to the best available displayed price, which the Commission states, and Better Markets agrees, would allow market participants to evaluate how well market centers and broker-dealers perform in executing covered orders relative to the best available displayed price.

Finally, the Proposal would require additional information for executable NMLOs, executable stop orders, and beyond-the-midpoint limit orders. In particular, the Commission would require reporting of the: (i) number of orders that received either a complete or a partial fill; and (ii) the cumulative number of shares executed regular way at prices that could have filled the order while it was in force, as reported pursuant to an effective transaction reporting plan or NMS plan.

Collectively, these amendments would provide more meaningful information about the distribution of execution times within each order type. For example, requiring timestamp information in granular millisecond increments would allow for meaningful points of comparison between market centers and/or broker-dealers for data that uses timestamp information and time-to-execution statistics.[20] The new 15 second and one minute realized spreads better capture the reality of today's fast-paced market transactions and align well with the available academic literature indicating that realized spreads are likely to be most impacted during the first 15 seconds for large, highly liquid stocks, and one minute for smaller, more thinly traded stocks.[21] Percentage-based spread measurers would provide additional information at the individual stock level where there is a significant price change during a month.[22] And requiring a separate field for E/Q allows market participants to compare price improvement statistics across securities as well as across market centers and broker-dealers.[23]

IV. <u>IN ADDITION TO AMENDEDING RULE 605 REPORTS TO ENHANCE THEIR CONTENT AND ACCESSIBILITY, THE COMMISSION MUST ENSURE THAT RULE 605 REPORTS ARE ACURATE AND EASY TO READ</u>

The proposed amendments would enhance the content and accessibility of the required reports by requiring all entities subject to Rule 605 to make a summary report available that would be formatted in the most recent versions of the XML and PDF formats as published on the SEC's website.

20 Release at 3812.
21 Release at 3815.
22 Release at 3816.
23 Release at 3817.

However, the information contained in required reports is only as good as the quality of information placed in those reports by broker-dealers. As the Commission notes in the Proposal, "Rule 605 and Rule 606 operate together to allow investors to evaluate what happens to their orders after investors submit their orders to a broker-dealer for execution."[24] Therefore, Better Markets strongly advocates that the Commission address the concerns raised by the SEC Division of Examination in its Risk Alert: Observations Related to Regulation NMS Rule 606 Disclosures, dated November 10, 2022 (the "Alert").[25] That Alert found that broker-dealers were not providing the proper information required in their *Rule 606* disclosures, a public report designed to provide better insight into factors that may influence a broker-dealer's order routing decisions so that broker-dealer customers can view the material aspects of their firm's PFOF arrangements. That form also provides disclosures on how the firm routes non-directed orders for execution so that investors can better identify PFOF conflicts of interest.

In particular, the Alert found that broker-dealers (i) had incorrectly identified routing firms as order execution venues; (ii) had published inaccurate amounts of net aggregate rebates received for market orders, marketable limit orders, non-marketable limit orders, and other orders; (iii) had provided general information about, but did not disclose the specific per share PFOF rebates applicable to, different size and order types under PFOF arrangements with non-exchange venues; (iv) did not disclose that they represented to routing or executing brokers that they would provide exclusively retail order flow to the routing broker to receive PFOF under arrangements with routing brokers; (v) did not disclose that the broker-dealer could refuse to route orders to execution venues unless the venues agreed to pay a specified level of PFOF, which the SEC staff alleged could result in decreased price improvement or lower execution quality for customers; (vi) failed to disclose material terms of PFOF agreements including the specific rebate tier applicable to the broker-dealer; and (vii) did not establish adequate written supervisory procedures to ensure the accuracy of their 606 Reports and the disclosures required therein.

These findings with respect to the Rule 606 reports highlight the importance of ensuring that the Rule 605 reports are subject to close scrutiny and where appropriate, enforcement. As with broker-dealer's Rule 606 reports, the usefulness of the information contained in their Rule 605 Reports will be directly correlated to the quality of the information therein.

Finally, Better Markets does not agree with those that would argue that the proposed changes to disclosure of order execution will not benefit retail investors who are unlikely to read the Rule 605 reports.[26] The more thoughtful approach is to recognize that even though a certain percentage of retail investors may not read the Rule 605 reports, they will still benefit indirectly as the enhanced disclosure will promote competition, improve regulatory oversight,

---

24 Release at 3795.

25 *See also*, FINRA, 2022 Report on FINRA's Examination and Risk Monitoring Program: Disclosure of Routing Information, available here.

26 We agree with Healthy Markets Association that improved header data would go a long way to making Rule 605 Reports more readable, particularly for retail investors, and suggest the Commission make this technical enhancement to the Rule 605 NMS Plan.

and facilitate use by third-party researchers and academics, who in turn can extract information from the reports and use it to expose issues and problems with today's order routing and execution practices.[27]

CONCLUSION

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

Stephen Hall

Stephen W. Hall
Legal Director and Securities Specialist

Better Markets, Inc.
1825 K Street, NW
Suite 1080
Washington, DC 20006
(202) 618-6464

[redacted]
http://www.bettermarkets.org/

[27] Release at 3794. With respect to the Commission's approach to economic analysis, Better Markets has long taken the view that the Commission is not obligated to conduct cost-benefit analysis, that its duty is only to "consider" the impact of its proposals on efficiency, competition, and capital formation (the ECCF factors), and that it retains considerable discretion and leeway in doing so. These principles are set forth in a number of our reports, *see, e.g.,* Better Markets, REPORT: THE ONGOING USE AND ABUSE OF COST-BENEFIT ANALYSIS IN FINANCIAL REGULATION (Mar. 23, 2023), https://bettermarkets.org/newsroom/report-the-ongoing-use-and-abuse-of-cost-benefit-analysis-in-financial-regulation/, and we have offered them in our comment letters, including the one submitted today on the SEC's order competition proposal that accompanies the Proposal on best execution. Better Markets, Comment Letter to the SEC on Order Competition Rule (filed Mar. 31, 2023). That comment letter also expresses our view that the Commission must be wary of industry opposition to all of the pending market structure reforms and must discount their exaggerated predictions of harm to the markets or investors they say will follow from the proposals. We incorporate by reference herein both the report and the comment letter cited above, and we contend that with respect to the instant Proposal on the disclosure of order execution information, the Commission has more than met its duty to evaluate the three "ECCF" factors.