

March 31, 2023

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

Re: Market Structure Proposed Rules (File Numbers S7-29-22, S7-30-22, S7-31-22, and S7-32-22)

Dear Ms. Countryman:

JPMorgan Chase & Co. (“JPMC”) appreciates the opportunity to respond to the Securities and Exchange Commission’s (the “SEC” or the “Commission”) request for public comment on its market structure proposals addressing Disclosure of Order Execution Information;<sup>1</sup> Tick Sizes, Access Fees, and Transparency of Better Priced Orders;<sup>2</sup> Regulation Best Execution;<sup>3</sup> and Order Competition<sup>4</sup> (together the “Proposals”).

Through its affiliates, JPMC is active in nearly all segments of the financial markets, including institutional equity and fixed-income brokerage, retail brokerage, discretionary account management, and asset management for mutual funds and large institutional clients. Our customers, clients, and businesses will be significantly impacted if these rules are adopted as proposed. We identify in this letter our collective concerns related to the Proposals, and provide suggestions we believe may improve them.<sup>5</sup>

The U.S. market provides a highly effective trading environment for market participants, including retail investors. In proposing these four rules, the Commission seeks to make significant changes to a market that is not in need of major reform. The Proposals, especially if adopted all at once, would have far-reaching impacts that could jeopardize, rather than enhance, market efficiency and performance. We believe that changes of this magnitude warrant further analysis to understand their cumulative impact and potential risks.

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<sup>1</sup> Release No. 34-96493; File No. S7-29-22 (December 14, 2022), 88 Fed. Reg. 3786 (January 20, 2023) (“Disclosure of Order Execution Information Proposing Release”).

<sup>2</sup> Release No. 34-96494; File No. S7-30-22 (December 14, 2022); 87 Fed. Reg. 80266 (December 29, 2022) (“Reg NMS Proposing Release”).

<sup>3</sup> Release No. 34-96496; File No. S7-32-22 (December 14, 2022), 88 Fed. Reg. 5440 (January 27, 2023) (“Regulation Best Execution Proposing Release”).

<sup>4</sup> Release No. 34-96495; File No. S7-31-22 (December 14, 2022); 88 Fed. Reg. 128 (January 3, 2023) (“Order Competition Rule Proposing Release”).

<sup>5</sup> JPMC has actively engaged with, and generally supports the views expressed in the comment letters of the Securities Industry and Financial Markets Association (“SIFMA”) and the Investment Company Institute (“ICI”).

Incremental, carefully tailored changes would be more beneficial and could prevent market disruption and unintended consequences. Therefore, we recommend that the Commission prioritize the adoption of Rule 605 amendments to provide the Commission and market participants with sufficient data regarding execution quality to evaluate a gradual adoption of the Reg NMS amendments and Reg Best Ex. We believe the proposed Order Competition Rule should be abandoned.

Our comments can be summarized as follows:

- The Commission needs to be able to observe how each of these proposed rules will independently and cumulatively affect the market. If the Commission decides to adopt any of these rules, it should do so one at a time and in a sequential order that will enable an informed evaluation of how each incremental change affects the market.
- We generally support the Rule 605 amendments. The data obtained under the amended rule will allow the Commission and market participants to better understand what drives order execution efficiency and performance in the current market structure.
- We believe the proposed amendments to Regulation National Market System (“Reg NMS”) would benefit from the following modifications: (1) simplification of the approach to quoting tick size for tick-constrained stocks; (2) a single trading tick size that would apply across all execution venues; (3) a single access fee cap; and (4) implementation of certain aspects of the Market Data Infrastructure Rules (“MDI Rules”) in their previously adopted form.
- We believe that the existing best execution rules already provide strong protection for investors, however, we do not object to a Commission-level best execution standard (“Reg Best Ex”), subject to several modifications to the scope of the proposed rule and the application of the conflicted transactions provisions; we also offer views on the definition of institutional customer, and recommend that the existing MSRB and FINRA best execution rules should be rescinded.
- We oppose the proposed Order Competition Rule, because we believe (1) it will negatively impact security prices for our clients and (2) the potential benefits have been overestimated.

## 1. Sequence of Adoption

We recommend that the Commission take a sequential approach to assessing and evaluating each of the Proposals. This would allow the Commission to measure how each new rule, independently and cumulatively, impacts market efficiency. The Commission should first adopt the proposed Rule 605 amendments as this will improve transparency and insight into execution quality.<sup>6</sup> Next, the enhanced data provided under Rule 605 would allow the market to more effectively monitor the impact of the amendments to tick size. Then, the combined insight

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<sup>6</sup> As part of the adoption of Rule 605 amendments, we support the adoption of the MDI Rules components contained within the proposed amendments to Reg NMS with the exception of the “best odd-lot” information.

from implementation of these amendments would in turn better position the Commission to identify order routing inefficiencies to more fully inform the proposed Reg Best Ex. A staggered approach will also allow for smoother implementation.

## 2. Disclosure of Order Execution Information

Reg NMS is a set of rules adopted in 2005 by the SEC to modernize and strengthen the equity markets. Rule 605 is a provision of Reg NMS that requires market makers, alternative trading systems (“ATS”), national securities exchanges, and national securities associations to disclose certain order execution performance statistics on a monthly basis. The proposed Rule 605 amendments would: (1) expand the scope of entities subject to the reporting obligation; (2) expand the scope of covered orders that must be included in the reports; (3) expand the information required to be reported regarding covered orders; and (4) require reporting of monthly summary statistics in addition to machine readable reports.

We support the Commission’s efforts to modernize Rule 605 to address market fragmentation and changes to the speed and nature of trading that have occurred since the adoption of Rule 605, as well as to enhance overall market performance transparency.<sup>7</sup> Accordingly, we generally support the proposed Rule 605 amendments and believe they will help advance market participants’ and regulatory authorities’ understanding of key drivers of market quality. We also support the operational and interpretive recommendations and clarifications set forth in the SIFMA comment letter.<sup>8</sup>

## 3. Tick Sizes, Access Fees, and Transparency of Better Priced Orders

The SEC also proposes amendments to other aspects of Reg NMS (“Reg NMS Proposal”). Specifically, these amendments would: (1) reduce minimum pricing increments (“tick sizes”) and apply them to quoting as well as trading; (2) reduce access fee caps, which are limits on the fees exchanges are permitted to charge market participants; and (3) implement certain changes that were adopted in 2020 as part of the MDI Rules. As the national market system has evolved since 2005, the Commission is proposing these amendments to “reflect the current trading environment” and “enhance trading opportunities for all investors.”<sup>9</sup> While we appreciate the Commission’s effort to reevaluate and modernize Reg NMS, we recommend the following adjustments to make the proposed amendments more effective.

### a. Tick Size

Under current Rule 612, tick size is \$0.01 (penny) for stocks trading at or above \$1.00. The Reg NMS Proposal would implement a variable model that creates 4 levels of tick sizes

<sup>7</sup> Disclosure of Order Execution Information Proposing Release at 2, 22, and 26.

<sup>8</sup> See Letter from Ellen Greene, Managing Director, Equity and Options Market Structure, SIFMA, to Vanessa Countryman, Secretary, SEC, RE: *File No. S7-32-22; Release No. 34-96496; Regulation Best Execution. File No. S7-31-22; Release No. 34-96495; Order Competition Rule, File No. S7-30-22; Release No. 34-96494; Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, File No. S7-29-22; Release No. 34-96493; Disclosure of Order Execution Information* (March 31, 2023).

<sup>9</sup> Reg NMS Proposing Release at 8-9.

(\$0.01, \$0.005, \$0.002, and \$0.001) for stocks trading at or above \$1.00. Under this model, tick sizes would be determined every quarter based on the Time Weighted Average Quoted Spreads calculated by the primary exchange for each NMS stock.<sup>10</sup>

*i. Quoting Tick Size*

We applaud the Commission for being receptive to the industry's recommendation to improve trading in tick-constrained stocks that are almost always quoted in the permitted minimum increment.<sup>11</sup> We agree with the SEC that these stocks can benefit from reduced tick sizes, as the current penny tick size "creates an artificial price constraint...and prevents such stocks from reaching a natural price that would be within a penny spread."<sup>12</sup> Reduction in tick size for tick-constrained stocks would allow price discovery and execution opportunities at smaller increments and make trading in these stocks more efficient, which would ultimately reduce transaction costs.

However, as discussed in the SIFMA letter, tick sizes that are too granular can bring unintended consequences and more research needs to be done to determine the optimal tick sizes for this market.<sup>13</sup> We are concerned that reducing tick sizes to \$0.002 (1/5 penny) and \$0.001 (1/10 penny) from today's penny tick size could risk disrupting the market. Therefore, we recommend that the Commission initially reduce the quoting tick size to \$0.005 (1/2 penny) for tick-constrained stocks.<sup>14</sup> We would define tick-constrained stocks as those that are priced at or above \$1.00 per share and have an average quoted spread of 1.1 cents or less. This approach would incrementally improve trading in tick-constrained stocks without unnecessary disruption and help the Commission ascertain whether further changes would be beneficial.

*ii. Evaluation Period*

The Reg NMS Proposal requires the average quoted spreads that determine the tick size buckets to be calculated on a quarterly basis. This approach adds unnecessary complexity and burdensome requirements for market participants to update their systems every quarter. If the Commission elects to reduce tick size only for truly tick-constrained stocks, stocks will likely move less frequently across different tiers and thus not require a frequent reclassification. Consequently, we believe it will be sufficient for tick-constrained stocks to be determined semi-

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<sup>10</sup> Time Weighted Average Quoted Spread would be defined as the average dollar value difference between the highest price that someone has offered to buy the stock (the national best bid or NBB) and the lowest price that someone is willing to sell the stock for (national best offer or NBO), together the NBBO, during regular trading hours where each instance of a unique NBB and NBO is weighted by the length of time that the quote prevailed as the NBB or NBO. Reg NMS Proposing Release at 68.

<sup>11</sup> Industry participants have recommended through various forums that any change in tick size should not assume that one tick size is ideal for all stocks.

<sup>12</sup> Reg NMS Proposing Release at 61.

<sup>13</sup> Examples include queue jumping, flickering quote, and reduced liquidity at the inside quotation, as discussed in the SIFMA comment letter, *supra* note 8.

<sup>14</sup> The Proposal states that for all alternatives discussed, including the 2-tier alternative, one of the conditions is that "the Commission would not amend rule 612 to apply to trading situations. Thus, all alternatives here apply tick sizes only to quoting." Reg NMS Proposing Release at 278.

annually based on the previous 6-months' average spread. We agree with the Commission that the primary listing exchanges have the necessary market data and are best positioned to perform this calculation. Extending the calculation period to 6 months will also reduce the variability and complexity of the proposed rule, as well as the frequency at which the market participants would need to adapt to the changing tick size.

### *iii. Trading Tick Size*

Under the current rule, tick sizes apply solely to quoting and not executions. Execution in sub-penny trading is permitted. The Commission believes that exchanges and ATSS are disadvantaged because they cannot practically provide sub-penny price improvements that over-the-counter market makers are able to provide through internalization of order flow.<sup>15</sup> To address this “competitive disparity,” the Reg NMS Proposal would require trades to be executed at the applicable quoting tick size in an effort to promote “fair competition” and ensure “equal regulation” among market participants.<sup>16</sup> We do not believe that harmonizing quoting and trading tick sizes is necessary to achieve these objectives. To the contrary, it would significantly reduce price improvement opportunities for investors, and potentially harm execution quality by mandating all orders to be executed at wider quoting tick sizes.

As an alternative, we recommend applying a \$0.001 trading tick size to all stocks trading at \$1.00 or above across all venues, while preserving the midpoint and benchmark trade exceptions discussed in the Reg NMS Proposal.<sup>17</sup> This approach will not only preserve price improvement opportunities, but will also promote the Commission’s objective of leveling the playing field by subjecting all execution venues to the same trading tick size. In addition to the midpoint and benchmark trade exceptions, we recommend that the Commission add derivatively priced trades to the list of exceptions. Similar to benchmark trades, derivatively priced trades execute at prices that are not “reasonably determinable” at the time the commitment to execute the order is made.<sup>18</sup>

Our recommended \$0.001 trading tick size is similar to retail liquidity programs (RLPs) the Commission already approved for the exchanges to provide them with an additional competitive advantage. RLPs allow the exchanges to offer sub-penny price improvements for retail orders, usually in increments of \$0.001, but have not been widely used in the market.<sup>19</sup> In conjunction with this recommendation, we also encourage the Commission to reevaluate the workability of RLPs and why they have not attracted more retail order flow on exchange venues. If utilized more widely by market participants, RLPs could serve as a preexisting solution for promoting the fair competition the Commission seeks to achieve.

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<sup>15</sup> Reg NMS Proposing Release at 32.

<sup>16</sup> Reg NMS Proposing Release at 74.

<sup>17</sup> The Proposal also suggests \$0.001 trading increment as a reasonable alternative while preserving exceptions for midpoint and benchmark trades (e.g., VWAP and TWAP trades). Reg NMS Proposing Release at 267.

<sup>18</sup> Reg NMS Proposing Release at 73.

<sup>19</sup> *Id.* at 158.

b. Access Fees

Today, exchanges typically impose access fees on market participants who take liquidity and offer rebates to those who provide liquidity. Under current Rule 610, the access fee is capped at \$.003 (30 mils) per share for stocks trading at or above \$1.00. The purpose of the 30 mil access fee cap was “to prevent exchanges from charging excessive fees to orders that were required to trade with a protected quote.”<sup>20</sup> In conjunction with the reduction in tick size, the Reg NMS Proposal introduces a variable 2-tier model that reduces access fee caps to \$0.001 (10 mils) and \$0.0005 (5 mils) per share, which does not correspond to the proposed 4-tier reduction in tick sizes.

While we agree with the Commission that access fee caps need to be reduced in concert with the reduction in tick sizes, we are concerned that the proposed approach would add unnecessary complexity to the market by creating another set of variable metrics. More importantly, the proposed approach creates a disparity in liquidity for similarly situated securities that are in different access fee buckets for a nominal difference. Specifically, in the event two similarly priced securities fall into different access fee tiers (and likely different rebates), there may be a disparity in the trading dynamics and liquidity available for otherwise similar securities, which could result in a direct impact to both institutional and retail trading experiences.

Therefore, we recommend a simple, uniform access fee cap of \$0.001 (10 mils) for all stocks trading at or above \$1.00.<sup>21</sup> This approach would be more aligned with the tick size reduction recommended above and consistent with the Commission’s objective of ensuring that access fees make up a meaningfully smaller proportion of the per share quotation price, while also minimizing unintended consequences that could result from the proposed variable access fee model.

c. MDI Rules: Round Lot and Odd-Lot Definitions

The Reg NMS Proposal would accelerate implementation of certain parts of the MDI Rules that were adopted in 2020, specifically the round lot and odd-lot definitions (with the addition of “best odd-lot” information). Round lot refers to the number of shares that make up a standard quoting increment for a security, currently 100 shares, and is used to determine the best price available (national best bid and offer, or “NBBO”), while odd-lot refers to any quantity less than a round lot. Today, information about odd-lot orders is available only on proprietary data feeds of each exchange (which need to be purchased separately) but not included in the consolidated market data distributed through the exclusive securities information processors (“SIP data”). The MDI Rules, if implemented, would amend the round lot definition to reduce

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<sup>20</sup> *Id.* at 168.

<sup>21</sup> This is also consistent with the SEC’s proposed rule. While the SEC also proposes a 5-mil access fee cap for stocks with the \$0.001 tick size, a 10-mil access cap would be sufficient given that our recommended approach does not have such a granular tick size. *See* Reg NMS Proposing Release at 97.

the round lot size for higher priced stocks.<sup>22</sup> In addition, the rules would require information about odd-lot orders to be included in SIP data to increase transparency about better priced orders available in the market.<sup>23</sup> The Reg NMS Proposal adds an additional element, known as the “best odd-lot” order information, which refers to the highest priced odd-lot order to buy and the lowest priced odd-lot order to sell that are better than the NBBO.

We are concerned about the dissemination of the best odd-lot information. The Commission believes such information would “enhance the usefulness of odd-lot information” and allow investors to better “assess the execution quality of their orders.”<sup>24</sup> However, we believe best odd-lot information, which would essentially be an odd-lot NBBO, could create investor confusion. An odd-lot NBBO could appear as a new benchmark, even though it would not be a protected quote, causing investors to believe that they could have received better price improvement for their orders. Furthermore, if there is a best odd-lot price better than the protected price in the market, Rule 605 could show misleading negative price improvement while ignoring the order’s size. We believe that the round lot and odd-lot information definitions as previously adopted in the MDI Rules in 2020 are sufficient to provide increased transparency for better priced orders available in the market for investors while minimizing unnecessary confusion.

In addition, we are concerned that if the round lot and odd-lot definitions are implemented before other components, the implementation of the remainder of the MDI Rules (*i.e.*, depth of data and auction information, introduction of competing consolidators and self-aggregators) could be delayed indefinitely. The unimplemented components of the MDI Rules, especially the introduction of competing consolidators and self-aggregators that collect market data and disseminate to the public (or use internally), are especially valuable means for introducing greater competition for market data, enhancing the quality of market data and reducing costs. We encourage the Commission to continue to recognize the importance of all components of the MDI Rules. We believe that the desired policy objectives and the full benefits will only be achieved when the MDI Rules reach their full implementation.

#### **4. Regulation Best Execution**

The SEC’s proposed Reg Best Ex would, for the first time, establish an SEC-level best execution rule or standard similar to those implemented today under FINRA Rule 5310 and MSRB Rule G-18 and would require broker-dealers to establish, maintain, and enforce procedures to comply with that standard. JPMC notes that the current rules already establish standards and requirements that effectively provide for best execution for customers. JPMC does not object to the creation of a single, SEC-level standard provided that it is appropriately tailored to allow brokerage firms to best serve their customers across the fixed income and equities markets, as discussed below. Specifically, we recommend a definition of institutional customer,

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<sup>22</sup> As an example, for stocks priced higher than \$250 and less than \$1,000, 40 shares would constitute 1 round lot. Reg NMS Proposing Release at 113.

<sup>23</sup> Odd-lot information would include information about trades that occur at a price that is at or better than the NBBO.

<sup>24</sup> Reg NMS Proposing Release at 143.

and also that the conflicted transaction requirements be abandoned or, at minimum, modified with respect to both the scope and types of transactions captured. Should the SEC adopt this rule, we believe FINRA Rule 5310 and MSRB Rule G-18 should be rescinded.

a. A Single, Commission-Level Best Execution Standard

While we do not object to a Commission-level best execution standard, we are concerned with the potential challenges of complying with three separate best execution rules. Given that the Commission's proposed standard prescribes different requirements than those of FINRA and the MSRB, this could create a conflict of rules, creating increased uncertainty for broker-dealers if the rules are interpreted differently by different regulators. We therefore recommend that, if the SEC adopts Reg Best Ex, the FINRA and MSRB rules should contemporaneously be rescinded.

b. Institutional Customer Exemption for Fixed Income

The MSRB provides an exemption from its best execution standard for institutional customers.<sup>25</sup> We recommend that the SEC incorporate a similar exemption into proposed Reg Best Ex for fixed income transactions. For the purpose of this exemption, we recommend that the SEC define institutional customer in such a way as to capture those investors currently defined as such by either the MSRB or FINRA rules.<sup>26</sup> Specifically, this definition would include: (1) a bank, savings and loan association, insurance company or registered investment company; (2) an investment adviser registered either with the SEC under Section 203 of the Investment Advisers Act or with a state securities commission (or any agency or office performing like functions); or (3) any other person (whether a natural person, corporation, partnership, trust or otherwise) with total assets of at least \$50 million. We also recommend that the Commission maintain the "opt-in" framework provided for in the MSRB rule.<sup>27</sup> This would allow institutional customers to choose to avail themselves of best execution protections or not.

While the Reg Best Ex Proposing Release observes that customers that meet the MSRB's Sophisticated Municipal Market Professional (SMMP) exemption would benefit from the protections provided by the proposed rule, the Commission has not articulated how these protections would benefit such clients. As the Commission notes, in fixed income markets, institutional customers are well-positioned to determine prevailing market prices and use their discretion to execute at the most favorable prices.<sup>28</sup> We believe many such customers would prefer to retain the flexibility to direct broker-dealers to execute their trades in a manner that they believe enables them to obtain most favorable execution in light of their own priorities.

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<sup>25</sup> MSRB Rule G-48 ("The broker, dealer, or municipal securities dealer shall not have any obligation under Rule G-18 to use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the [Sophisticated Municipal Market Professional] is as favorable as possible under prevailing market conditions.").

<sup>26</sup> MSRB Rule D-15 and FINRA Rule 4512(c)(3).

<sup>27</sup> MSRB Rule G-48(c).

<sup>28</sup> Regulation Best Execution Proposing Release, footnote 114.



Requiring an opt-in would allow sophisticated investors to elect to be exempted, and has the additional benefits of operational consistency with the current regime.

c. Conflicted Transactions

We are concerned that the prescriptive nature of the proposed conflicted transactions provisions of Reg Best Ex go too far, are unworkable, and will significantly deter transactions that are consistent with providing clients with best execution. Importantly, the existing best execution standards and current rules already contemplate the risks that the SEC has identified as areas for concern. We therefore recommend that the SEC not adopt the conflicted transaction provisions, and look to existing standards instead. Should the SEC proceed, we offer the following recommendations to the obligations, scope and type of transactions included, to limit the negative impacts for clients.

i. *Obligations of a Broker-Dealer in a Conflicted Transaction*

Under the current MSRB and FINRA best execution standards, broker-dealers may enter into what the Commission calls “conflicted transactions” if, after *reasonable diligence*, they determine that it is the best way to obtain the best price for the customer under prevailing market conditions (the Reasonable Diligence Standard). Reg Best Ex includes this same Reasonable Diligence Standard,<sup>29</sup> but, according to the proposing release, it would require broker-dealers to evaluate “a broader range of markets, beyond those identified as material potential liquidity sources” prior to entering into a conflicted transaction.<sup>30</sup> This may result in worse pricing for customers’ orders in certain circumstances.

The proposing release does not clarify the definition of “beyond material sources.” We are concerned that broker-dealers would have to check all liquidity sources, including potentially immaterial ones, which would take a significant amount of time. During that time, the pricing and depth of liquidity for the ordered security could turn against the client, especially when volatility is high. This price worsening could, at least in part, be caused by the obligatory review of immaterial liquidity sources. Forcing a broker-dealer to check immaterial venues may cause information leakage, leading to unnecessary price shifts that do not reflect the underlying value of a security.

To prevent this harm, the Commission should abandon this provision of Reg Best Ex. Instead, it should rely on Reg Best Ex’s (1) Reasonable Diligence Standard;<sup>31</sup> (2) policies and

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<sup>29</sup> Regulation Best Execution Proposing Release at 49.

<sup>30</sup> Regulation Best Execution Proposing Release at 111.

<sup>31</sup> See Regulation Best Execution Proposing Release at 49, “...must 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.”

procedures requirement;<sup>32</sup> and (3) execution quality review requirements.<sup>33</sup> Pursuant to the execution quality review requirements, broker-dealers would conduct reviews of execution quality across markets including a comparison of the quality of the executions being obtained via current order routing and execution arrangements to the quality of the executions that could have been obtained from competing markets. Broker-dealers typically also examine markets' likelihood of execution; accessibility of competing markets/systems and costs; speed of execution and/or ability to handle orders of certain sizes. Based on such reviews, they adjust their routing and execution as necessary. Mandating broker-dealers to check liquidity sources they have determined are not worth accessing is unnecessary, duplicative, and would not improve the ultimate price received by the customer.

## ii. Scope of the Conflicted Transactions Provision

Should the Commission still decide to adopt the conflicted transaction provisions of Reg Best Ex, it should (1) strictly tailor the definition of covered customers and orders as well as (2) limit the types of transactions that are considered "conflicted."

### a. Covered Customers and Orders

The conflicted transaction provision of Reg Best Ex sets out new requirements for broker-dealers when entering into certain "conflicted transactions" for or with accounts of "retail customers."<sup>34</sup> As proposed, "retail customers" would include accounts of "a natural person or held in legal form on behalf of a natural person or group of related family members."<sup>35</sup> We note that the proposed definition would include certain customers that have traditionally been considered institutional investors (such as family offices, private investment companies or other investment vehicles held in corporate form for a sophisticated investor). Accordingly, we encourage the Commission to narrowly tailor the definition of "retail customers" to exclude orders originating from family offices, consistent with the no-action relief issued under Regulation Best Interest, and that are from discretionary accounts that are held by natural persons or families. Since these orders are submitted to a broker-dealer by registered investment advisers, the Commission could do this by relying on our proposed definition of institutional customer<sup>36</sup> and the proposed exemption for when "an institutional customer, exercising independent judgment executes its order against the broker-dealer's quotation."<sup>37</sup> This would

<sup>32</sup> See Regulation Best Execution Proposing Release at 63, "...establish, maintain, and enforce written policies and procedures reasonably designed to comply with the best execution standard...".

<sup>33</sup> See Regulation Best Execution Proposing Release at 44, "would require broker-dealers to review the execution quality of customer orders at least quarterly, and how such execution quality compares with the execution quality that might have been obtained from other markets, and revise their best execution policies and procedures, including order handling practices, accordingly." The Commission notes that this proposed rule is "designed to be consistent with FINRA Rule 5310.09." Regulation Best Execution Proposing Release at 131.

<sup>34</sup> We agree with the Commission that institutional customers should remain excluded from the scope of conflicted transactions.

<sup>35</sup> Regulation Best Execution Proposing Release at 103.

<sup>36</sup> See *infra* §4(b).

<sup>37</sup> Regulation Best Execution Proposing Release at 51.

allow, as the ICI notes in its letter, a “continuation of existing advisory bunching and order handling practices, in which the orders of discretionary advisory accounts are grouped together for better average execution prices that benefit investors.”<sup>38</sup> If the Commission removes the ability to group orders, these customers could receive worse pricing.

In addition to narrowly tailoring the definition of “retail customer” we also recommend certain large orders be excluded from the requirements of this rule. Executing large orders under the conflicted transactions requirements of Reg Best Ex could lead to information leakage that will negatively affect the price of the customer’s order. Consistent with the definition of block size in Reg NMS Rule 600, we recommend to exclude orders (1) of at least 10,000 or more shares or (2) with a market value of \$200,000 or more. As the Commission notes, this threshold is “the same dollar amount as in other Regulation NMS rules to exclude orders or trades that are so large as to warrant different treatment than smaller orders.”<sup>39</sup> As the SEC states in the proposal, when a broker-dealer is handling and executing such large orders, “it may likely be more sensitive to the possibility of information leakage and price impact that could harm the execution quality of such orders.”<sup>40</sup> Broker-dealers may use strategies like splitting large orders into smaller child orders and executing those in a series of transactions to prevent this harm.<sup>41</sup> Scoping out orders of this size would allow broker-dealers to continue achieving best execution for large customer orders through tactical routing decisions.

#### *b. Transaction Types*

Should the SEC proceed with adopting the conflicted transaction provisions despite the potential harm it would cause, we recommend modifications to the scope of transactions identified as conflicted. Specifically, we recommend that transactions with an affiliate of the broker-dealer, transactions executed on a principal basis, and transactions for which a broker-dealer receives exchange rebates not be considered conflicted transactions.<sup>42</sup> The Reg Best Ex proposing release states that the Commission considers these transaction types to be “conflicted,” because a broker-dealer “has an incentive to handle those orders in a manner that prioritizes its own interests over its customers’ interests.”<sup>43</sup>

We believe the current best execution standards and rules already address and mitigate potential conflicts of interest that may arise in context of such transactions, and the SEC should replicate this approach.<sup>44</sup> In many cases, such transactions provide value to customers as significant sources of liquidity. The proposed enhanced obligations are significant enough to

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<sup>38</sup> Letter from Sarah A. Bessin, Deputy General Counsel, Investment Company Institute, to Vanessa Countryman, Secretary, SEC, *RE: Regulation Best Execution; File No. S7-32-22, Order Competition Rule; File No. S7-31-22*, 9 (March 31, 2023).

<sup>39</sup> Order Competition Rule Proposing Release at 102.

<sup>40</sup> *Id.* at 91.

<sup>41</sup> *Id.*, note 169 at 91.

<sup>42</sup> Regulation Best Execution Proposing Release at 100-1.

<sup>43</sup> *Id.* at 111.

<sup>44</sup> FINRA Rule 5310 and MSRB Rule G-18.

disincentivize broker-dealers from providing liquidity in a manner that could be construed as “conflicted.” Existing procedures, and requirements that would exist under Reg Best Ex for non-conflicted transactions, are sufficient to address the Commission’s concerns.<sup>45</sup> If the Commission adopts Reg Best Ex, it could examine these procedures and offer guidance or seek enhancements as appropriate.

*i. Affiliated Trading*

Reg Best Ex would consider any transaction “where a broker-dealer...routes an order to, or receives an order from, an affiliate for execution” as conflicted.<sup>46</sup> The Commission has expressed that such affiliated trading might lead a broker-dealer to self-deal against its customers’ orders.<sup>47</sup> We understand that, despite its benefits, affiliated trading is a longstanding concern of the SEC, but we disagree with how the Commission proposes to address the noted conflict.<sup>48</sup> Rather, we think that this conflict is adequately addressed by existing disclosures and the Reasonable Diligence Standard that would continue to exist under Reg Best Ex. Therefore, affiliate transactions should be removed from the proposed list of conflicted transactions.

As noted above, transacting with affiliates comes with potential benefits to the end-customer, not just the affiliated entities. Customers may benefit from, among other things, reduced commissions, and efficient access based on shared infrastructure. This can be the case when, for example, an affiliate is the dominant liquidity source for certain securities (as is often the case with respect to fixed income securities) or a firm routes orders in foreign securities to its locally registered affiliate.<sup>49</sup> Today, affiliated routing is adequately addressed by disclosure of routing arrangements to customers and the existing Reasonable Diligence Standard.<sup>50</sup>

Requiring a broker-dealer to check immaterial liquidity sources before it can route an order to an affiliate/execute an order received from an affiliate, will potentially result in worse pricing. We believe the Commission should rely on the Reasonable Diligence Standard and policies and procedures requirements (for non-conflicted transactions) of Reg Best Ex to address the Commission’s concerns.<sup>51</sup> If the Commission adopts Reg Best Ex, it could examine these procedures and offer guidance or seek enhancements as appropriate.

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<sup>45</sup> FINRA Rule 3110(b) and MSRB Rule G-27(c).

<sup>46</sup> Regulation Best Execution Proposing Release at 100-1.

<sup>47</sup> *Id.* at 111.

<sup>48</sup> See Regulation Best Execution Proposing Release at 111 (providing the Commission view that such affiliated trading might lead a broker-dealer to self-deal against its customers’ orders).

<sup>49</sup> *Infra* 3(ii)(c)(2)(B).

<sup>50</sup> As discussed above, currently a broker-dealer may route a customer’s order to an affiliate after it has conducted reasonable diligence that the execution will result in a price “as favorable as possible under prevailing market conditions.” *Supra* § 3(c)(1). See FINRA, Rule 5310(a)(1) and Rule G-18.

<sup>51</sup> FINRA Rule 3110(b) and MSRB Rule G-27(c).

*ii. Principal Trading*

Under proposed Reg Best Ex, a conflicted transaction would occur where a transaction in which a broker dealer executes a retail customer’s order as principal or riskless principal would be considered a conflicted transaction. We do not believe such transactions should be considered conflicted.

Broker-dealers commonly engage in principal transactions to provide liquidity to customers dealing in both equity and fixed income securities. In both markets, broker-dealers often principally facilitate customer orders in illiquid securities and/or orders of a size that could have impact to the market. Principally executing against the customer in these scenarios provides the customer with price certainty (*i.e.*, the order is not affected by any potential market movement the order could cause) and the broker-dealer can provide price stability (*i.e.*, the broker-dealer is able to manage liquidating the risk associated with facilitating the customer’s order in a manner that limits impact to the market). Allowing broker-dealers to trade as principal in the fixed income markets is critical. As SIFMA explains in its letter, “most fixed income securities are quoted or traded infrequently if at all – some may go weeks, months or even years without trading. There are no continuous two-sided quoted markets for the large majority of fixed income products.”<sup>52</sup> Without principal trading, customers may have to wait significant periods of time to find a counterparty to their trade. This is especially true when an order involves a thinly traded bond or market volatility is high.

If the Commission were to adopt Reg Best Ex in its current form, investors would be denied access to timely and easily accessible liquidity. The FINRA and MSRB requirements to obtain the best price possible under prevailing market conditions<sup>53</sup> apply to principal transactions as they do to those executed on an agency basis, and the Commission has not pointed to any issues with these existing standards that would merit imposing additional obligations. Furthermore, FINRA’s rule regarding fair prices and commissions<sup>54</sup> prevents broker-dealers from unfairly marking up or down the price for client orders when acting as principal, while providing liquidity to a market that may otherwise lack it. The Commission should rely on the language of its own proposed Reasonable Diligence Standard<sup>55</sup> and FINRA Rule 2121 to prevent unfair dealing in principal transactions rather than deterring such transactions by labeling them as conflicted and exposing them to unnecessary, and possibly harmful, obligations.

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<sup>52</sup> Letter from Leslie M. Norwood, Managing Director and Associate General Counsel, SIFMA and Christopher B. Killian Managing Director, SIFMA, to Vanessa Countryman, Secretary, SEC, *Re: Proposed Regulation Best Execution, Release No. 34-96496; File No. S7-32-22*, 12 (March 31, 2023).

<sup>53</sup> See FINRA Rule 5310(a)(1) (“...a member and persons associated with a member shall use reasonable diligence to ascertain the best market for the subject 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.”) and MSRB, Rule G-18 (“...a dealer must use reasonable diligence to ascertain the best market for the subject security and buy or sell in that market so that the resultant price to the customer is as favorable as possible under prevailing market conditions.”).

<sup>54</sup> FINRA Rule 2121.

<sup>55</sup> Regulation Best Execution Proposing Release at 49.

*iii. Transactions Receiving Exchange Rebates*

Reg Best Ex would consider transactions where a broker dealer receives exchange rebates as conflicted. We believe the Commission’s proposal to address this perceived conflict is harmful for the customer, unworkable and unnecessary.<sup>56</sup>

Currently, broker-dealers are held to best execution standards that preclude them from making routing decisions solely on the availability of exchange rebates. As a result, they may only route trades to a venue that pays a rebate if they believe that venue will provide the customer with the best price under the prevailing market conditions. Requiring a broker-dealer to evaluate immaterial potential liquidity sources for such transactions could result in worse pricing for customers, for reasons stated above.<sup>57</sup> We believe this additional requirement could deter broker-dealers from routing orders to certain venues that could ultimately provide the best execution possible for the customer to avoid the conflicted transaction obligations, to the detriment of the customer.

Moreover, regulatory requirements governing the adoption of exchange fee schedules, which could include rebates, as well as extensive disclosures related to broker dealers’ routing decisions, mitigate potential conflicts of interest associated with the receipt of exchange rebates. Exchange rebates are set by each exchange and publicly disclosed. In setting their fee schedules, exchanges must ensure that their fees (and rebates) meet certain Exchange Act requirements—the fees are (i) reasonable, (ii) equitably allocated, (iii) not unfairly discriminatory, and (iv) not an undue burden on competition. As a result of these requirements, exchanges apply fees and rebates to all members equally. Separately, Rule 606 requires “broker-dealers to make publicly available on a quarterly basis certain aggregated order routing disclosures for held orders that provide, among other things, detailed disclosure of payments received from or paid to certain trading centers” in addition to “a discussion of the material aspects of broker-dealer’s relationships with those trading centers.”<sup>58</sup>

We believe these regulatory requirements coupled with Reg Best Ex’s Reasonable Diligence Standard and related procedural requirements are sufficient to address potential conflicts of interest posed by receiving exchange rebates.

## **5. Order Competition Rule**

The proposed Order Competition Rule would require certain orders of NMS stocks placed by individual investors to be exposed to open auctions before such orders can be executed internally by trading centers that restrict order-by-order competition. The proposed rule establishes requirements for qualified auctions including wide dissemination of auctions in consolidated market data, an auction duration between 100 milliseconds and 300 milliseconds, and specific pricing increments and fee structures. The proposing release explains that the

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<sup>56</sup> *Id.* at 111.

<sup>57</sup> *Supra* § 3(c)(1).

<sup>58</sup> SEC, *Staff Report on Equity and Options Market Structure Conditions in Early 2021* at 13 (2021).

auctions are intended to enhance the opportunity of individual investor orders to receive more favorable prices, and benefit institutional investors by giving them opportunities to trade directly with individual investor orders. We do not believe this will be the result.

On the contrary, we expect that individual investor auctions will result in worse pricing for customers. The proposed auction process would delay execution by at least 1/30<sup>th</sup> of a second, and will broadly disseminate the order and signal to the market that there is a demand to trade a given security. During this delay, the signal would allow market participants to react to the change in demand and adjust pricing accordingly.

Additionally, we believe the Commission vastly overestimates the increased price improvement that institutional traders would receive by being able to interact directly with individual investor order flow in qualified auctions.”<sup>59</sup> First, it is not likely that institutional and retail order flow would match in a meaningful way. Institutional and retail investors trade different stocks, in different sizes, at different times. Second, auctions would display and disseminate certain information that could identify investors and their positions. Institutional investors may forgo participation in the auctions to avoid information leakage.

Finally, we do not believe the Commission has accurately assessed the scale and complexity of the infrastructure that would be required to implement the Order Competition Rule. If the rule is adopted, market participants would need to design, build, and test an expansive and complicated technology framework. This will divert human and financial resources that could be better utilized to benefit customers.

In light of our view that such auctions will not benefit either institutional or retail investors, and that, developing the operational capacity to participate in this auction system would take a significant investment that may outweigh any expected benefit, we recommend the Commission abandon this proposed rule.<sup>60</sup>

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<sup>59</sup> Order Competition Rule Proposing Release at 310.

<sup>60</sup> JPMC generally agrees with the positions of SIFMA regarding the Order Competition Rule. See Letter from Ellen Greene, Managing Director, Equity and Options Market Structure, SIFMA, to Vanessa Countryman, Secretary, SEC, RE: *File No. S7-32-22; Release No. 34-96496; Regulation Best Execution. File No. S7-31-22; Release No. 34-96495; Order Competition Rule, File No. S7-30-22; Release No. 34-96494; Regulation NMS: Minimum Pricing Increments, Access Fees, and Transparency of Better Priced Orders, File No. S7-29-22; Release No. 34-96493; Disclosure of Order Execution Information* (March 31, 2023).

JPMC appreciates the opportunity to comment on the Proposals and provide our views on potential risks and recommendations on the topic of U.S. market structure. We would be pleased to provide any further information or respond to any questions that the Commission or the staff may have.

Very truly yours,

/s/ Michael Camacho

**Michael Camacho**

Chief Executive Officer  
Wealth Management Solutions

/s/ George C.W. Gatch

**George C.W. Gatch**

Chief Executive Officer  
J.P. Morgan Asset Management

/s/ Jason E. Sippel

**Jason E. Sippel**

Chief Executive Officer  
J.P. Morgan Securities LLC

Cc: The Honorable Gary Gensler, Chair  
The Honorable Hester M. Peirce, Commissioner  
The Honorable Caroline A. Crenshaw, Commissioner  
The Honorable Mark T. Uyeda, Commissioner  
The Honorable Jaime Lizárraga, Commissioner  
Haoxiang Zhu, Director, Division of Trading and Markets