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

July 14, 2023

RE: File Number S7-31-22 Request for Comment on the Proposed Order Competition Rule

Dear Vanessa,

This comment letter on the SEC's proposed changes to individual investor order execution is jointly submitted by me, Omri Even-Tov, and my co-authors, Eric So, Shimon Kogan, and Kimberlyn Munevar. We have extensively studied an issue related to the proposed amendments – the effects of commission fees on retail investor trading behavior and participation. Our recent work provides insights that staff may find beneficial to include in the economic analysis of the costs of the proposed rule.

Our expertise derives from research conducted for our recent working paper that utilizes data from eToro, an international online retail brokerage. The data includes daily trade and position data, as well as demographic information on over 160,000 eToro users. Our study leverages the removal of fees by eToro on certain trades in certain countries in 2019 as a natural experiment to study the effect of commission fees on retail investor trading behavior and participation. Specifically, eToro removed fees only on non-leveraged equity trades and only for users in certain countries. This implementation allows us to isolate the causal effect of fees on trading behavior while controlling for unrelated changes in trading behavior using a triple difference-in-difference research design.

To briefly summarize our results: the removal of eToro's 80bps trading fee led to:

(1) an over 30% increase in users' monthly number of trades and portfolio turnover,

(2) a significant increase in users' portfolio diversification, and

(3) no change in before-fee portfolio performance and a significant improvement in net-of-fee performance.

The fee removal also prompted a significant increase in new users, specifically those who are younger, less experienced, and have smaller account sizes.

Although eToro is an international brokerage that primarily serves non-U.S. retail investors investing in U.S. equities, we have confirmed the external validity of our findings during our sample period. Specifically, we documented a significant association between the trading behavior of our eToro user sample and the trading behavior of U.S. retail investors, as evidenced by the NASDAQ "Retail Trading Activity Tracker" data. Thus, we believe our results are applicable to the U.S. setting.

We respond to the following SEC requests for comments on the economic analysis of the costs and benefits of the proposed rules on individual investor order execution:

57. *Does the Economic Analysis in this release account for all relevant costs? If not, which other costs should the economic analysis consider? Please provide estimates of additional costs, other than compliance costs, that you believe should be considered.*

While the proposed rules outline in Section VII.C.2.b.ii a variety of reasons to expect that retail brokerages will not return to a commission fee revenue model, it is worth noting that multiple brokerage firms have submitted comments on the proposed amendments that mention the potential return of commission fees (UBS p.8; Robinhood p. 5; Schwab p. 21-22). To the extent that this is a probable outcome, it is important for the staff to consider the effects this change will have on retail investor trading activity, participation, and capital formation.

Our evidence suggests that such a move would discourage retail participation and diversification in financial markets. We document that retail traders are highly sensitive to trading fees – leading them to trade less frequently and hold fewer securities of reduced variety. Our evidence also suggests that the removal of trading fees spurred an increase in capital market participation by younger, less sophisticated investors with less money to invest. The reintroduction of fees may deter participation from this group.

Additionally, the staff have requested comments on their analysis of the effects of the proposed rule on capital formation. The proposal states on p.331:

"As investors would benefit from improved execution quality as a result of the proposed amendments, these investors would also likely benefit from lower transaction costs. Higher transaction costs may hinder customers' trading activity that would support efficient adjustment of prices and, as a result, may limit prices' ability to reflect fundamental values."

Our research supports the statement that transaction costs hinder retail investors' trading activity. To the extent that the proposed rules, if adopted, prompt the reintroduction of commission fees that outweigh improvements in transaction costs from order competition, it is possible that retail investors' trading activity will be reduced, potentially harming capital formation.

In summary, we urge the commission to further consider the possibility that the proposed amendments will lead brokerage firms to reintroduce trading fees, and to factor in the costs of this change into the economic analysis of the amendments.

Respectfully,

Omri Even-Tov

Omri Even-Tov, Ph.D.
University of California, Berkeley

Eric So

Eric So, Ph.D.
Massachusetts Institute of Technology (MIT)

Shimon Kogan
Reichman University;
University of Pennsylvania

Shimon Kogan

Kimberlyn Munevar
University of California, Berkeley

Kimberlyn Munevar