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Markets

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March 31, 2023

Ms. Vanessa Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549

RE: File No. S7-32-22; Release No. 34-96496; Regulation Best Execution

Dear Ms. Countryman:

On behalf of RBC Capital Markets (“RBCCM”), thank you for the opportunity to comment on the above referenced proposal (hereinafter “the Proposal”) from the U.S. Securities and Exchange Commission (“Commission” or “SEC”).<sup>1</sup> RBCCM is the investment banking platform of Royal Bank of Canada.<sup>2</sup> RBCCM is an SEC-registered broker-dealer that, among other activities, provides equities trading and execution services to retail and institutional investors. These investors include large investment managers with trillions of dollars in assets under management. Those assets reside in employee pension funds, mutual funds, and other vehicles that hold the savings of individual investors.

### **Background and Overview**

RBCCM has supported the Commission’s recent efforts to strengthen the fairness, transparency, and efficiency of U.S. equity markets. These efforts include the rule on Market Data Infrastructure (“MDI”) and the rule to establish a transaction fee pilot, among other Commission actions.<sup>3</sup> RBCCM has appreciated opportunities to discuss these

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<sup>1</sup> Regulation Best Execution, Release No. 34-96496 (Dec. 14, 2022), 88 FR 5440 (Jan. 27, 2023) (File No. S7-32-22), available at <https://www.govinfo.gov/content/pkg/FR-2023-01-27/pdf/2022-27644.pdf>.

<sup>2</sup> Royal Bank of Canada (RBC), headquartered in Toronto, Ontario, is a global provider of financial services, including personal and commercial banking, wealth management services, corporate and investment banking, and life insurance and transaction process services. RBC’s approximately 97,000 employees serve more than 17 million personal, business, public sector, and institutional clients worldwide through offices in Canada, the United States, and 27 other countries. In the United States, RBC’s approximately 13,000 employees primarily provide corporate and investment banking, wealth management, asset management, and retail banking services to customers and clients in more than 40 states.

<sup>3</sup> See, e.g., comment letter dated November 12, 2020, from Rich Steiner, Head of Global Market Structure, RBC Capital Markets, related to Joint Industry Plan; Notice of Filing of a National Market System Plan Regarding Consolidated Equity Market Data, available at <https://www.sec.gov/comments/4-757/4757-8011716-225373.pdf>; comment letter dated May 27, 2020, from Rich Steiner, RBC Capital Markets, related to Market Data Infrastructure, available at <https://www.sec.gov/comments/s7-03-20/s70320-7239991-217149.pdf>; two comment letters dated February 4, 2020, from Rich Steiner, RBC Capital Markets, related to two SRO NMS rule proposals for confidentiality and conflicts of interest policies for their NMS Plans, available at <https://www.sec.gov/comments/sr-ctacq-2019-04/srctacq201904-6768288-208067.pdf> and <https://www.sec.gov/comments/sr-ctacq-2019-01/srctacq201901-6768289-208068.pdf>; comment letter dated December 10, 2019, from Rich Steiner, RBC Capital Markets, in support of the SEC Proposal to Rescind the Effective-Upon-Filing Procedure for NMS Plan Fee Amendments, available at <https://www.sec.gov/comments/s7-15-19/s71519-6526196-200406.pdf>; comment letter dated October 25, 2019, from Rich Steiner, RBC Capital Markets, providing analysis related to market data and access, available at <https://www.sec.gov/comments/4-729/4729-6353203-195588.pdf>; Brief of Amicus Curiae, RBC Capital Markets, LLC, In Support of Respondent and Denial of the Petitions for Review, New York Stock Exchange LLC, Et Al. v Securities and Exchange Commission, D.C. Cir. Docket No. 19-1042, filed August 1, 2019; comment

and other important reforms with Commission officials and has presented RBCCM research and analyses in the course of the discussions.

We are encouraged that the SEC is focusing generally on equity market structure topics and specifically concentrating on ways to ensure investors benefit from robust broker order handling and best execution. Below we share our views and observations on the Proposal, along with recommendations to help ensure positive outcomes for investors should this rule be implemented.

### **Retail Order Handling and Conflicts of Interest**

We agree with the Commission's belief that retail customers would benefit from brokers employing robust efforts to seek midpoint executions, additional liquidity sources and other price improvement opportunities. Expanding this segment of investor orders to a more diverse group of trading venues and market participants could lead to greater competition and price improvement. This could lead to increased opportunities for institutional investors and others to interact with this liquidity across venues they have access to. Currently, the vast majority of marketable retail orders are routed to wholesalers and frequently internalized. We agree with the agency's view that merely routing customer orders for automated execution or internalizing customer orders at the National Best Bid and Offer ("NBBO") does not necessarily satisfy a broker's duty of best-ex for small orders in stocks. We also agree with the Commission and believe market participants would benefit from, among other things, "robust considerations by retail brokers...regarding the possibility of available liquidity priced at the midpoint..." Further, we agree with the agency's view that "...currently, broker-dealers' reviews of execution quality vary in rigor."

Investors stand to benefit from additional efforts to bolster best-ex reviews, particularly when brokers have certain conflicts of interest. That notwithstanding, any gains from this proposal may be nominal or even counterproductive, as investors experience very good executions under the current best-ex regime. By mandating a very prescriptive, rigid protocol for order routing, it is foreseeable that innovation could be harmed and – particularly for larger orders – an investor's intent could more easily be recognized and disadvantaged by other market participants.

### **Material Potential Liquidity Sources**

The proposed description of a "market" is expansive. It would require broker-dealers to take into consideration a broad range of potential trading venues and market centers that *may* provide the best market for customers' orders so that the resulting prices to the customers are as favorable as possible under prevailing market

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letter dated August 15, 2019, from Rich Steiner, RBC Capital Markets, regarding Proposed Rule Change to Introduce a Liquidity Provider Protection, available at <https://www.sec.gov/comments/sr-cboeedga-2019-012/srcboeedga2019012-5977239-190213.pdf>; comments of RBC participant Rich Steiner, RBC Capital Markets, SEC Roundtable on Market Data and Market Access, October 25-26, 2018, available at <https://www.sec.gov/spotlight/equity-market-structure-roundtables/roundtable-market-data-market-access-102618-transcript.pdf>; comment letter dated October 16, 2018, from Rich Steiner, RBC Capital Markets, in support of the proposed SEC Transaction Fee Pilot, available at <https://www.sec.gov/comments/s7-05-18/s70518-4527261-176048.pdf>; comment letter dated May 24, 2018, from Rich Steiner, RBC Capital Markets, in support of the proposed SEC Transaction Fee Pilot, available at <https://www.sec.gov/comments/s7-05-18/s70518-3711236-162472.pdf>; comment letter dated September 23, 2016, from Rich Steiner, RBC Capital Markets, in support of Equity Market Structure Advisory Committee (EMSAC) Recommendation for an Access Fee Pilot, available at <https://www.sec.gov/comments/265-29/26529-86.pdf>; comment letter dated May 24, 2016, from Rich Steiner, RBC Capital Markets, regarding EMSAC Framework for Potential Access Fee Pilot, available at <https://www.sec.gov/comments/265-29/26529-70.pdf>.

conditions. Brokers would need to consider if a market center is reasonably accessible and if it should be considered a material potential liquidity source. Because of the highly prescriptive language in the proposal, it is likely that brokers would effectively need to connect to nearly every liquidity source, including exchanges, ATSs, single dealer platforms and technology platforms. We are concerned that the high cost of complying with the proposed standards could be prohibitive, particularly for smaller brokers. The fixed costs that would ensue would be significant, and effectively serve as a tax on the industry and, ultimately, one that would be passed on to retail investors. These fees include those for market data products, testing, circuits, order entry ports, network access, wireless connections, hosting fees, colocation, fiber cross connects and connectivity to vendor systems and others. Brokers would need to dedicate considerable resources to connect, test and monitor all of these venues as well, particularly in relation to pre-trade risk controls designed to comply with the Market Access Rule (Exchange Act Rule 15c3-5). Brokers would also need to implement robust market access controls, policies and procedures, and surveillance tools. Along with the aforementioned additional fees and resource requirements, the challenges resulting from the proposed standard could reduce competition and raise the bar for new entrants, particularly retail-focused introducing brokers. Furthermore, because of the sheer number and breadth of trading venues available, not only would connecting to all of them be prohibitive from a cost standpoint, but the requirement to do so also raises concerns around unnecessary complexity and increased technology risks. This may also further incentivize new exchange and ATS entrants in what is already a crowded space, simply because they can be even more assured of the ability to collect a toll on other market participants.

What's more, this prescriptive language may force rigid policies or rule interpretations, harming innovation and the discretionary order handling that provides a better execution for client orders. For example, if a client sends a marketable limit order, should a broker be mandated to try and get a midpoint execution before accessing displayed liquidity (and possibly reserve liquidity) at the far touch of the NBBO? Could an investor be harmed by a broker first seeking a midpoint execution across numerous trading venues? If there were any midpoint executions, this information would of course be widely disseminated. Could market participants anticipate a more aggressive buy or sell order to be forthcoming as a result, particularly in a less liquid security? Could displayed markets be negatively impacted? If orders were necessarily routed at less aggressive / midpoint prices first, and those midpoint prices are based on displayed orders, would those providing pre-trade price discovery in the form of displayed orders be disenfranchised? Would the markets become darker as more liquidity providers would post midpoint peg orders to get a speedier execution? Furthermore, how might brokers manage the potentially competing mandates of considering the speed of executions with seeking out additional liquidity at venues to ascertain the best possible market center?

These are important questions the Commission should consider and answer before adopting the proposal and implementing the new best execution regime. Routing to additional venues would increase the time to an execution and could result in inferior execution prices. A more optimal process would be for a broker to utilize a data driven approach to maximize the likelihood of finding liquidity to satisfy the order. There are also instances where price improvement is not the most important factor to an investor. Some may prioritize speed of execution and maximum liquidity access. Furthermore, severely restricting the discretionary order handling brokers use to route investor orders across myriad trading strategies, tactics and time horizons will make order routing more homogenous and easier for those looking to identify larger orders in the market.

FINRA has provided updated guidance on Rule 5310 over the years, particularly addressing a number of the specific issues included in Proposed Rule 1100, including a broker's obligation to consider new trading venues, stating: "This obligation would include reviewing new markets and trading centers that become available as potential markets to which the firm may route orders; thus, a firm should regularly consider execution quality at venues to which it is not connected and assess whether it should connect to such venues," as well as "[a] firm

must take into account market and technology changes that might alter its best execution analysis.”<sup>4</sup> The current best-ex regime allows brokers to strike the right balance between connecting to low volume venues with little differentiation and those with more trading volume and / or more innovative systems. There are implicit as well as explicit costs to connecting to trading venues. It is not the case that more is always better. Where some see competition, others see fragmentation and lack of innovation. Simply sending an order to more venues is hardly optimal. Better to analyze and optimize what venues to go to and when, considering market conditions, liquidity of the individual security and investor timeframe / immediacy to name a few.

As a general matter, institutional investors have more variability than retail clients. There is less need or benefit to highly prescriptive rules which could inhibit the myriad ways index funds, open end funds, ETFs and others have their orders handled. Asset managers have the ability to select brokers that provide the best performance and tools for their investors. Even if the Commission does apply the proposed rules and requirements to brokers’ routing decisions for institutional investors, clearly defining institutional vs. retail is critical for the industry to understand what obligations apply. We think an approach similar to that in Regulation Best Interest would be best, insofar as defining retail investors as “natural persons and their legal representatives.”

### **Conflicted Transactions**

We appreciate that, as proposed, only retail orders are in scope. However, there are concerns that this puts in place a foundation to expand the mandate to include other potential broker conflicts, including those affecting institutional orders, as the proposal seeks further comments (see question 85 in the Proposal).<sup>5</sup> This would introduce an onerous process for both brokers and investors to align on the proper order handling procedures to navigate broker routing conflicts which are being managed well today. FINRA Rule 5310 addresses this issue and institutional investors are in a better position than retail investors to analyze and direct their orders accordingly. Would the new SEC standard alter this? Would brokers effectively be mandated to access all other, smaller trading venues and platforms, or would the discretion that exists today satisfy the proposed best-ex obligations? There is a tradeoff between routing to more venues, accessing liquidity and minimizing information leakage and market impact. These considerations weigh into a broker’s discretion and should be aligned with clients to ensure the best outcome for them. Our experience is that having a measure of flexibility serves investors well. As proposed, an overly structured routing protocol could lead brokers to design systems that look very similar to each other, increasing information leakage. Has the agency considered how changes in technology over time could have deleterious effects? Will brokers be so concerned about violating an especially rigid regulatory structure that they walk back differentiated and innovative technologies that benefit investors?

### **New Regulation Versus Modifying Existing Regulations**

The Proposal notes that “...the Commission is proposing Regulation Best Execution to further the goals of the national market system and reinforce broker-dealer best execution obligations.”<sup>6</sup> It is unclear that this rule is going to achieve that goal, and requiring the industry to comply with multiple rules from different regulators with significantly overlapping mandates is suboptimal. The proposed rules raise serious questions around how brokers are to fulfill their best execution obligations. Additional direction and transparency from the Commission and its staff are critical. For example, when the Proposal states that “[t]he proposed rule would set forth the standard of

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<sup>4</sup> See Guidance on Best Execution Obligations in Equity, Options and Fixed Income Markets, FINRA Regulatory Notice 15-46, Nov. 20, 2015, available at <https://www.finra.org/rules-guidance/notices/15-46>.

<sup>5</sup> Proposal at 5469.

<sup>6</sup> Proposal at 5550.

best execution....” should brokers therefore expect that by complying with this new standard and related obligations, they will also satisfy their obligations under FINRA Rule 5310, or will there be different interpretations? Should the industry anticipate additional findings by the SEC and a rule amendment by FINRA? Will enforcement of the SEC rules be consistent across large and small brokers? Has the agency thought through the challenges and costs to the industry to comply with multiple best execution rules enforced by both a government regulator and an SRO? We have concerns that the costs for the industry to implement the many changes to policies, procedures and trading systems could harm investors and competition rather than help them.

In addition, how does the SEC envision FINRA's role in the review and examination process? We have seen with regard to other SEC rulemaking that FINRA has clarified the position of its role in certain instances. For example, with Regulation Best Interest, FINRA released guidance that stated in part that “[t]hese assessments [of a group of firms] were not undertaken with the purpose of making findings of anticipated violations of Reg BI or Form CRS, but rather as a helpful dialogue with firms about their ongoing efforts and potential challenges.”<sup>7</sup> Will FINRA be expected to fulfill certain roles under the SEC's rule and also have additional mandates as an SRO?

### **Review Process**

If Rules 1100, 1101 and 1102 are adopted as they are currently proposed, RBCCM recommends a formal review process during a defined period after implementation, through which economists review performance metrics and the effects to the industry and investors to ensure the rule is fulfilling the Commission's original objectives and importantly, not creating unintended consequences that are detrimental to our well-functioning markets. One example could be a cost benefit analysis looking at the costs incurred by the industry to subscribe to proprietary exchange market data feeds and to connect to additional trading platforms versus any performance benefits received by investors.

### **Conclusion**

RBCCM again appreciates the opportunity to comment on the Proposal. We further appreciate the Commission's consideration of the matters raised, as referenced above. We are encouraged that the SEC is focusing generally on equity market structure topics and specifically concentrating on ways to ensure investors benefit from robust broker order handling and best execution. We strongly urge the Commission to revise the Proposal to ensure that the ensuing best execution standard and related requirements will advance the SEC's objectives of greater transparency, reduce conflicts of interest, and create greater efficiencies for investors and other market participants. We recommend a more principles-based, less prescriptive approach to order routing with a single best execution regulatory regime, along with a formal review process.

Furthermore, brokers and investors face additional challenges navigating this process with the other equity market structure rulemaking proposals, as there is significant overlap among them (and the MDI rule has not yet been implemented). Each will certainly be subject to exogenous factors stemming from the others. Therefore, we recommend a staggered approach to the implementation of the various rules. It may be best for the industry and investors to get the enhanced disclosure and best execution rules, if adopted, implemented first, to put in place a foundation to better monitor and track the changes to tick sizes, trade increments, auctions, etc.

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<sup>7</sup> See FINRA Highlights Firm Practices from Regulation Best Interest Preparedness Reviews, available at <https://www.finra.org/rules-guidance/key-topics/regulation-best-interest/preparedness>.

Vanessa Countryman  
March 31, 2023  
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We would be pleased to discuss these comments in greater detail and provide additional information should there be any questions about the matters raised in this letter.

Sincerely,

A handwritten signature in black ink, appearing to read "R. Steiner". The signature is written in a cursive, flowing style.

Rich Steiner  
Head of Global Market Structure

cc: Gary Gensler, U.S. Securities and Exchange Commission, Chair  
Hester M. Peirce, U.S. Securities and Exchange Commission, Commissioner  
Caroline A. Crenshaw, U.S. Securities and Exchange Commission, Commissioner  
Jaime Lizárraga, U.S. Securities and Exchange Commission, Commissioner  
Mark T. Uyeda, U.S. Securities and Exchange Commission, Commissioner  
Haixiang Zhu, U.S. Securities and Exchange Commission, Director, Division of Trading and Markets