



April 10, 2019

Vanessa Countryman
Acting Secretary
Securities and Exchange Commission
100 F Street NE., Washington, DC 20549

Re: ***SIFMA Comment Letter on the MIAX, Pearl and Emerald Rule Proposals to Increase and Establish Connectivity Fees: File Nos. SR-MIAX-2019-10; SR-PEARL-2019-08; SR-EMERALD-2019-11***

Dear Ms. Countryman:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ submits this letter to comment on the above-referenced filings submitted to the U.S. Securities and Exchange Commission (“Commission”) to increase connectivity fees by Miami International Securities Exchange LLC (“MIAX”),² MIAX PEARL, LLC (“Pearl”),³ and MIAX Emerald, LLC (“Emerald”),⁴ (together, “Exchanges”). As stated in the rule proposals, this is the third attempt by the Exchanges to increase and establish the connectivity fees, and once again, the Exchanges have not provided sufficient information to allow the Commission to determine that the proposed

¹ SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry’s nearly 1 million employees, we advocate for legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

² Securities Exchange Act Release No. 85318; File No. SR-MIAX-2019-10 (March 14, 2019) (“MIAX Proposal”).

³ Securities Exchange Act Release No. 85317; File No. SR-PEARL-2019-08 (March 14, 2019) (“Pearl Proposal”).

⁴ Securities Exchange Act Release No. 85316; File No. SR-EMERALD-2019-11 (March 14, 2019) (“Emerald”).

rule changes are consistent with Sections 6(b)(4),⁵ 6(b)(5),⁶ and 6(b)(8)⁷ of the Securities Exchange Act of 1934 (“Exchange Act”).

Consistent with the Commission’s recent and correct rejection of similar BOX connectivity fee filings,⁸ SIFMA recommends the Commission suspend the proposed rule changes and institute proceedings to determine whether to disapprove the proposed rule changes pursuant to Section 19(b)(3)(A) of the Exchange Act.⁹ For more than a decade, SIFMA has opposed the increases in exchange fees for market data products. More specifically, we argued that the exchanges’ market data fees are not constrained by significant competitive forces, and therefore no sufficient basis for finding the fees to be fair and reasonable absent evidence regarding the cost of producing the market data. Recent Commission decisions have agreed that the exchanges have not pointed to sufficient evidence of competitive constraints to warrant approval of exchange market-data fees based on market forces alone.

A similar situation to exchanges’ market data fees is present with the Exchanges’ connectivity fees. Each exchange is the exclusive provider of its connectivity service and the trade-through requirements under Regulation NMS¹⁰ and the Options Order Protection Plan¹¹ effectively require broker-dealers to connect to all exchanges. As a result, there are no competitive constraints on exchange connectivity fees. Considering that broker-dealers cannot trade on the Exchanges without first paying these connectivity fees, we disagree with the Exchanges’ statement that broker-dealers can choose to connect to the Exchanges.¹² That is why broker-dealers cannot avoid paying excessive fees by disconnecting from the Exchanges, and not being able to trade on that exchange, without potentially violating order protection requirements or sacrificing execution quality. This issue is particularly notable in the options markets. Over the last 8 years, the number of options exchanges has increased from 7 to 15, with corresponding (and increasing) connectivity costs at each one.

The competition the Exchanges face for executions has not constrained the prices for connectivity because the Exchanges do not compete for connectivity. The Exchanges contend that MIAX and Pearl’s market share for the U.S. options industry was less than 10%,¹³ but that is irrelevant where the Exchanges are the exclusive purveyor of its connectivity services,

⁵ 15 U.S.C. 78f(b)(4).

⁶ 15 U.S.C. 78f(b)(5).

⁷ 15 U.S.C. 78f(b)(8).

⁸ *See* Securities Exchange Act Release No. 85459; File Nos. SR-BOX-2018-24; SR-BOX-2018-37; SR-BOX-2019-04 (Mar. 29, 2019) (“BOX Order”).

⁹ 15 U.S.C. 78s(b)(3)(A).

¹⁰ 17 CFR 242.611.

¹¹ Securities Exchange Act Release No. 60405; File No. 4-546 (July 30, 2009).

¹² MIAX Proposal at 7; Pearl Proposal at 7; Emerald Proposal at 6.

¹³ MIAX Proposal at 8; Pearl Proposal at 8.

particularly in light of the Order Protection Rule requirement noted above. Further, providing different connection speeds are not true alternatives promoting competition because the Exchanges remain the only source for connectivity.¹⁴ Contrary to the Exchanges' claim,¹⁵ allowing market participants to resell connectivity at exchange determined prices to other market participants does not foster competition from a substitute product. The connectivity fees cannot be constrained by competition when there are no alternative mechanisms or substitute products to connect to the exchange than paying separate connectivity fees to each of the Exchanges. As evidence of the lack of market forces' ability to constrain the connectivity fees, the Exchanges state they had no reduction in demand for its services despite a 9% to 27% increase in fees,¹⁶ which defies the Law of Demand.¹⁷

Given the requirement for large broker-dealers to connect to all the exchanges, the exchanges should be providing comprehensive information, including cost information, on why their connectivity fees are reasonable. It is not enough for exchanges to justify connectivity fee increases simply by pointing to vague descriptions of undefined categories of costs, or of similar fees charged by other exchanges.¹⁸ Additionally, the connectivity fees cannot be based on the "market value" of the connection when broker-dealers are effectively required to connect to each exchange. Indeed, the filings refer to their connectivity pricing in terms of reasonable value to the customer, rather than any pricing based on competing offerings, as would be the case in a competitive market. SIFMA, as a representative of the customers that ultimately pay these high fees, has repeatedly objected to the purported "reasonableness" of the Exchanges' pricing.

The Exchanges' filings lack sufficient information regarding cost and competition for the Commission to conclude that the proposed fees meet the requirements of the Exchange Act as outlined in the Commission's recent Order disapproving connectivity fees for separate options exchange.¹⁹ Per the Order, the Exchanges must do more than identify the categories of costs it incurs with a broad statement that the proposed fees would offset these costs.²⁰ The Exchanges must provide support for its assertion that the proposed fees will offset the Exchange's costs by providing details on the monthly, marginal and fixed costs of the connectivity fees and whether

¹⁴ *Contra*, MIAX Proposal at 7; Pearl Proposal at 7.

¹⁵ *See* Letter from Joseph Ferraro III, SVP & Deputy General Counsel, MIAX to Vanessa Countryman, Acting Secretary, Commission, at 3, dated April 5, 2019 ("MIAX Exchanges Letter"). MIAX Exchanges argue that competition for purchasing connectivity to the MIAX Exchanges exist because third-parties can resell connectivity to multiple market participants over that same connection.

¹⁶ MIAX Proposal at 9; Pearl Proposal at 9.

¹⁷ The Law of Demand is a fundamental concept of a market economy that states that the higher the price of a good, the less people will demand that good.

¹⁸ BOX Order at 22-24.

¹⁹ *See Id.*

²⁰ *Id.* at 22.

these costs always exceed the revenues from connectivity fees.²¹ Considering the Commission cannot simply rely on the Exchanges' statements and analysis²² and needs "detailed and specific information to support an affirmative Commission finding,"²³ the Exchanges must provide detailed information on their actual costs to allow the Commission to make independent findings on whether the proposed fees comply with the Exchange Act.

While we appreciate the Exchanges' attempt to explain the reason for the proposed price increase—both in their third proposed filing and, to the extent it is relevant, their subsequent April 5 "supplement"—the Exchanges must provide more details on their costs. Rather than providing examples of approximate increases in categories of costs, such as price increases in the cost of fiber, expanding the datacenter, increasing personnel,²⁴ the Exchanges should state specifically the actual dollar amounts of the costs, the assumptions made for allocating joint costs, attempts to mitigate costs and avoid price increases, and whether those costs exceeded the revenues from connectivity feeds, and if so by how much. Providing the categories of costs, and the related percentage increases in those categories does not allow the Commission to verify the Exchanges' statement that the connectivity fees the Exchanges collect are less than the total annual expenses.²⁵ Moreover, the Exchanges cannot simply state the proposed prices are consistent with other products' pricing²⁶ without stating why the comparison is relevant with a discussion on similar costs,²⁷ especially when the Exchanges say nothing about whether those baseline prices were reasonable in the first place.

In its consideration of the proposed rule changes, the Commission should establish a framework for determining whether fees for exchange products and services are reasonable when those products and services are not constrained by significant competitive forces. This framework should be based on the Exchanges' actual costs incurred compared to the anticipated revenues from the connectivity fees.

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²¹ *Id.* at 24.

²² *Susquehanna International Group v. SEC*, 866 F.3d 442, 447 (D.C. Circ. 2017).

²³ 17 CFR 201.700(b)(3).

²⁴ MIAX Proposal at 12; Pearl Proposal at 12; Emerald at 13.

²⁵ MIAX Exchanges Letter at 11.

²⁶ MIAX Proposal at 14; Pearl Proposal at 14; Emerald Proposal at 15-16.

²⁷ BOX Order at 25.

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SIFMA greatly appreciates the Commission's consideration of the issues raised above and would be pleased to discuss these comments in greater detail with the Commission and the Staff. If you have any questions or need any additional information, please contact me (at [REDACTED] or [REDACTED]).

Sincerely,

A handwritten signature in blue ink, appearing to read "Theodore R. Lazo", with a long horizontal flourish extending to the right.

Theodore R. Lazo
Managing Director and
Associate General Counsel

cc: The Honorable Jay Clayton, Chairman
The Honorable Robert J. Jackson, Jr., Commissioner
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner

Brett Redfearn, Director, Division of Trading and Markets: