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VIA E-MAIL

Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: **Securities Exchange Act Release No. 34-77899 (May 24, 2016), 81 FR 34393 (May 31, 2016) (SR-NYSE-2016-37) (the “Proposal”)**

Dear Mr. Fields:

The New York Stock Exchange LLC (the “NYSE” or “Exchange”) appreciates the opportunity to respond to the comment letter submitted in connection with the Proposal to remove from its rules certain internal procedures regarding the use of fine income which were approved in 2007 (the “Fine Income Procedures”).¹ For the reasons set forth in the Proposal and in this response, the Exchange believes that its Proposal is consistent with Sections 6(b)(1), 6(b)(4), and 6(b)(5) of the Securities Exchange Act of 1934, as amended (the “Act”).²

Summary of the Proposal

In 2006, New York Stock Exchange, Inc., merged with Archipelago Holdings, Inc. (the “Archipelago Merger”).³ Prior to approval of rule changes related to the Archipelago Merger, in conversation with the staff of the Securities and Exchange Commission (“Commission”), the

¹ See Letter from Michael Walsh, attorney, to Brent J. Fields, Secretary, Securities and Exchange Commission, submitted June 7, 2016 (“Comment Letter”). Capitalized terms that are not defined herein are used as defined in the Proposal.

² 15 U.S.C. 78f(b)(1), 15 U.S.C. 78f(b)(4), and 15 U.S.C. 78f(b)(5).

³ The Archipelago Merger had the effect of “demutualizing” New York Stock Exchange, Inc. and converting it to a for-profit entity. See Securities Exchange Act Release No. 53382, 71 FR 11251, 11254 (February 27, 2006) (SR-NYSE-2005-77). In the resulting re-organization, the Exchange succeeded to New York Stock Exchange, Inc.’s registration as a national securities exchange under the Exchange Act. See *id.*, at 11255.

Exchange undertook to subsequently file a proposed rule change regarding the use of fines collected from member organizations following disciplinary action against such member organizations.⁴ On January 31, 2007, the Commission approved the proposed rule change establishing the Fine Income Procedures.⁵ In its Proposal, the Exchange proposes to delete the Fine Income Procedures from the Exchange rules.

The Exchange's Fine Income Procedures referred to actions to be taken by the Exchange's subsidiary, NYSE Regulation, Inc. ("NYSE Regulation"), and NYSE Regulation's board of directors (the "NYSE Regulation Board"), because at the time performance of certain of the Exchange's regulatory functions was delegated to NYSE Regulation. Such delegation was made in 2006 pursuant to a Delegation Agreement (the "Delegation Agreement") between the Exchange, NYSE Regulation, and NYSE Market (DE), Inc.⁶

As a general matter, the Fine Income Procedures provided that fines would play no role in the annual NYSE Regulation budget process and the use of fine income by NYSE Regulation would be subject to specific review and approval by the NYSE Regulation board of directors.⁷

Effective February 16, 2016, the Delegation Agreement terminated and NYSE Regulation ceased performing regulatory functions on behalf of the Exchange, which has re-integrated its regulatory functions. The Regulatory Oversight Committee ("ROC") of the Exchange's Board of Directors now provides independent oversight of the regulatory function of the Exchange.⁸ In its filing proposing the creation of the ROC and termination of the Delegation Agreement, the Exchange "reiterate[d] the previous commitments that fines would play no role in the annual regulatory operating budget process and that the use of fine income by Exchange regulatory staff would be subject to review and approval by the proposed ROC."⁹ Accordingly, the ROC has assumed the responsibilities previously held by the NYSE Regulation Board.

⁴ See id., at 11270, note 231.

⁵ See Securities Exchange Act Release No. 55216 (January 31, 2007), 72 FR 5779 (February 7, 2007) (NYSE-2006-109) ("Order Approving the Fine Income Procedures").

⁶ See Securities Exchange Act Release No. 75991 (September 28, 2015), 80 FR 59837 (October 2, 2015) (SR-NYSE-2015-27) ("NYSE Approval Order"), at 59839.

⁷ See Securities Exchange Act Release No. 55003 (December 22, 2006), 71 FR 78497, 78498 (December 29, 2006) (NYSE-2006-109) (the "Proposing Release").

⁸ See NYSE Approval Order, supra note 6, at 59838.

⁹ See Securities Exchange Act Release No. 75288 (June 24, 2015), 80 FR 37316 (June 30, 2015) (SR-NYSE-2015-27), note 25.

Response to Comment Letter

The Comment Letter sets forth six arguments in opposition to the Proposal. We address each argument in order below. For ease of reference, we have used the Comment Letter's numbers and subtitles.

For the reasons discussed herein, the Exchange believes that the Comment Letter does not provide any credible argument why the Exchange's Proposal is not consistent with the requirements of the Act. Rather, the Exchange believes that the Fine Income Procedures are no longer necessary and are duplicative of the limitations on the use of regulatory assets and income, including fine income, set forth in Article IV, Section 4.05 of the operating agreement of the Exchange ("Section 4.05"). Section 4.05 prohibits the Exchange from using any regulatory assets or any regulatory fees, fines or penalties collected by the Exchange's regulatory staff for commercial purposes or distributing such assets, fees, fines or penalties to NYSE Group, Inc., the Exchange's member, or any other entity.¹⁰ Together, Section 4.05 and the provisions governing the ROC adequately address the concerns underlying the Fine Income Procedures and provide sufficient protections to ensure the proper use of fine income by the Exchange.

1. Rule Text

First, the Comment Letter contends that the Proposal does not include text showing the proposed change, or include the text of the Fine Income Procedures, and that obtaining paper copies from the Commission or the Exchange would be impracticable and inconvenient. The Comment Letter is incorrect on this point: the text of the Fine Income Procedures and proposed changes are in fact included in the Proposal. There is no need to seek paper copies.

When a self-regulatory organization ("SRO") files a proposal to change its rules pursuant to Rule 19b-4 under the Act, it files the proposal on Form 19b-4. Form 19b-4 requires the SRO to provide the proposed changes.¹¹ The Fine Income Procedures are considered rules of the Exchange, and therefore are subject to the Rule 19b-4 process.

However, what the Comment Letter does not seem to fully appreciate is that the Fine Income Procedures are internal procedures and, as such, are not part of the numbered New York Stock Exchange Rules or its governing documents. Indeed, as originally adopted, they were internal procedures of NYSE Regulation, not of the Exchange itself—and were described as such in the 2006 Form 19b-4 proposing the adoption of the Fine Income Procedures, the notice of the

¹⁰ See Ninth Amended and Restated Operating Agreement of New York Stock Exchange LLC (the "Operating Agreement"), Art. IV, Sec. 4.05; see also NYSE Approval Order, supra note 6, at 59839.

¹¹ See Form 19b-4 at <https://www.sec.gov/about/forms/form19b-4.pdf>.

proposed rule change, and the order approving their adoption.¹² That they are internal procedures is also stated in the title of the Proposal and in the definition of “Fine Income Procedures.”¹³

The 2006 Form 19b-4 did not include a separate exhibit with the proposed Fine Income Procedures, but rather stated them in the text of the Form 19b-4.¹⁴ Consistent with that approach, the Proposal restated the Fine Income Procedures in the text of the Proposal rather than in an exhibit.¹⁵ Further, the Proposal clearly stated, immediately under the heading “Proposed Amendment,” that the Exchange proposed to delete the Fine Income Procedures from the Exchange rules.¹⁶

2. *Other SROs*

In its Proposal, the Exchange notes that removing the Fine Income Procedures from its rules would make the Exchange’s rules more consistent with the limitations on the use of regulatory assets and income of other SROs. No other SRO limits the use of fine income to extra-budgetary use or subjects the use of fine income to specific review and approval by a regulatory oversight committee or any other governing body. Rather, other SROs’ limitations on the use of regulatory funds are generally similar to Section 4.05, in that they provide that regulatory funds shall be used to fund the relevant SRO’s legal, regulatory and (in some cases) surveillance operations, and shall not be used to make a distribution to the SRO’s member or

¹² See SR-NYSE-2006-109 (December 6, 2006) (the “2006 Form 19b-4”), at <https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-filings/filings/2006/NYSE-2006-109.pdf>; Proposing Release, *supra* note 7, at 78498; and Order Approving the Fine Income Procedures, *supra* note 5, at 5779.

¹³ See Proposal, 81 FR at 34393 and 34394. The Fine Income Procedures are defined as “certain internal procedures regarding the use of fine income which were approved in 2007.”

¹⁴ See 2006 Form 19b-4, *supra* note 12, at pp. 5-6.

¹⁵ Proposal, 81 FR at 34394.

¹⁶ *Id.* at 34395. The Comment Letter states that the author was not able to find Section 4.05 on the Exchange web site. The Operating Agreement is on the Exchange’s web site under “Regulation—Governing Documents, Related Information and NMS Plans—New York Stock Exchange LLC—Ninth Amended and Restated Operating Agreement of New York Stock Exchange LLC” at <https://www.nyse.com/regulation/governing-documents-related-information-nms-plans>.

stockholder, as the case may be. The Proposal cites the governing documents of its affiliates NYSE MKT LLC and NYSE Arca, Inc., as well as those of more than a dozen other SROs.¹⁷

The Comment Letter contends that, in making these points, the Exchange is arguing that the Commission should approve the Proposal simply because other exchanges have provisions similar to Section 4.05.¹⁸ The Comment Letter misses the point. The Exchange cites the other SROs' provisions to illustrate that the Fine Income Procedures are not the only way for the Commission to ensure that the Exchange utilizes its regulatory funds properly. Just as the Commission found that the provisions in these other SROs' governing documents were consistent with the Act, the Exchange believes that the Commission should conclude that Section 4.05, as an alternative to the Fine Income Procedures, is consistent with the Act.

The Comment Letter also maintains that the NYSE should be “single[d] out for different treatment than all the rest of the [e]xchanges” because it is a “world leader.”¹⁹ As a national securities exchange, the Exchange is subject to the same obligations and requirements under the Act as other national securities exchanges. To hold individual exchanges to different standards based on their size, economic worth, leadership or any of the other factors that the Comment Letter cites would be contrary to just and equitable principles of trade, would create impediments to a free and open market and national market system, and would impede the protection of investors and the public interest.

3. *Faulty Major Premise*

The Comment Letter next turns to the unique structure of SROs and “popular discontentment with business interests” to argue that the Fine Income Procedures “are about [the] legitimacy of the Exchange as a self-regulator.”²⁰ According to the Comment Letter, the Fine Income Procedures “provide an objectively justifiable arms-length limitation to separate business from regulation [and] ... take away economic incentive for the regulators.”²¹

¹⁷ Proposal, 81 FR at 34395-34396.

¹⁸ Comment Letter, at 1-2.

¹⁹ Id.

²⁰ Id., at 3. The Comment Letter's discussion of self-regulation falls outside the scope of the Proposal. We note, however, that SROs are a well-established structure. See *Concept Release Concerning Self-Regulation; Proposed Rule*, Securities Exchange Act Release No. 50700, 69 FR 71256 (December 8, 2004), 17 C.F.R. Part 240 (noting “Congress' determination to rely on self-regulation as a fundamental component of U.S. market and broker-dealer regulation”).

²¹ Comment Letter, at 4.

The Comment Letter overstates the significance of the Fine Income Procedures. Simply put, the Exchange does not rely on the Fine Income Procedures to ensure the independence of its self-regulatory responsibilities and regulatory performance from its business interests. Rather, its entire structure is set up to reinforce the independence of its self-regulatory responsibilities. For example, the Exchange Board of Directors must have a majority of independent directors and a director elected by Exchange members; the ROC is made up of independent directors; the Chief Regulatory Officer reports to the ROC; and the Committee for Review, which reviews disciplinary decisions and listing determinations, includes independent directors and individuals associated with member organizations of the Exchange.²² To be deemed independent, directors must satisfy the requirements in the Independence Policy of the Board of Directors, which policy is subject to Commission review.²³ Moreover, the Exchange's disciplinary rules specifically reflect and reinforce the principle of regulatory independence. For instance, the Exchange's disciplinary rules specifically provide that, in "performing the functions of investigation, complaint, examination, or proceeding authorized by Exchange rules, the CRO and Regulatory Staff shall function independently of the commercial interests of the Exchange and the commercial interests of the member organizations."²⁴

By contrast, the Fine Income Procedures are extremely limited in scope. At the time they were approved, the Commission stated that the Fine Income Procedures were "to assure the proper exercise by NYSE Regulation of its power to fine member organizations of the Exchange and the proper use by NYSE Regulation of the funds so collected."²⁵ Even assuming that the Comment Letter was limiting its argument to these concerns, the Exchange believes that they are adequately addressed by Section 4.05 and the operating agreement provisions governing the ROC, and so the Fine Income Procedures may be removed from the Exchange rules.

First, the Exchange believes that limitations on the use of fines is not the most effective way to assure proper exercise by Exchange regulatory staff of the Exchange's power to fine member organizations. As the Comment Letter itself acknowledges,²⁶ usage limitations on fine income do not provide oversight of regulatory performance; they just monitor how the resulting income is spent. The Exchange believes that the responsibility to assure proper exercise by Exchange regulatory staff of the Exchange's power to fine member organizations more properly

²² See Operating Agreement, Art. II, Section 2.03, and Securities Exchange Act Release No. 75991 (September 28, 2015), 80 FR 59837 (October 2, 2015) (SR-NYSE-2015-27).

²³ See Securities Exchange Act Release No. 67564 (August 1, 2012), 77 FR 47161 (August 7, 2012) (SR-NYSE-2012-17; SR-NYSEArca-2012-59; SR-NYSEMKT-2012-07).

²⁴ See Rule 8210(a).

²⁵ Order Approving the Fine Income Procedures, supra note 5, at 5779.

²⁶ Comment Letter, at 4.

lies with the ROC, which is responsible to oversee the Exchange's regulatory and self-regulatory organization responsibilities and assess the Company's regulatory performance.²⁷

Second, the Exchange believes that, by setting clear limitations on its use, Section 4.05 is sufficient to ensure the proper use by the Exchange of fine income. Section 4.05 addresses this concern by prohibiting the use of fines for commercial purposes or distributions. Indeed, because Section 4.05 encompasses all regulatory assets and income, not just fines, it ensures the proper use by the Exchange of a broader range of regulatory funds, by prohibiting their use for commercial purposes or distributions.

The Commission stated in its Order Approving the Fine Income Procedures that it believed the Fine Income Procedures would "guard against the possibility that fines may be assessed to respond to budgetary needs rather than to serve a disciplinary purpose."²⁸ Section 4.05 also guards against this possibility by limiting the use of fines. However, unlike the Fine Income Procedures, Section 4.05 also guards against the possibility that other regulatory income, such as examination, access, registration, qualification, arbitration, dispute resolution and other regulatory fees, or regulatory assets, could be used or assessed to respond to budgetary needs, by making them unavailable for commercial purposes or distributions. At the same time, the ROC is specifically charged with reviewing the regulatory budget of the Exchange and inquiring into the adequacy of resources available in the budget for regulatory activities.²⁹ Accordingly, the Exchange believes that removing the Fine Income Procedures and relying on Section 4.05 and the provisions governing the ROC would provide adequate protections against the use of regulatory assets, or assessment of regulatory income, to respond to budgetary needs.

4. *Faulty Minor Premise*

The Comment Letter challenges the Exchange's assertion that the disciplinary process, and the appellate process in particular, contains a powerful check on the improper exercise by Exchange regulatory staff of the power to fine members and member organizations. It argues that, instead, it is the Fine Income Procedures that provide the "checks and balances" through which "it is possible to create institutional and systemic rules that minimize the possibility of regulator misbehavior."³⁰

The Exchange respectfully disagrees that the Fine Income Procedures create a greater check on regulatory misbehavior than the appellate process. As noted above, usage limitations on

²⁷ See Operating Agreement, Art. II, Sec. 2.03(h)(ii).

²⁸ Order Approving the Fine Income Procedures, supra note 5, at 5780.

²⁹ See Operating Agreement, Art. II, Sec. 2.03(h)(ii).

³⁰ Comment Letter, at 4.

fine income do not provide oversight of regulatory performance. They just monitor how the resulting income is spent.

By contrast, the appellate process provides a comprehensive and meaningful check on the disciplinary process. Parties can appeal adverse disciplinary decisions and listings determinations to the CFR, which recommends a disposition to the Board of Directors. Pursuant to the Exchange's operating agreement, the CFR includes independent directors as well as representatives of Exchange member organizations that engage in a business involving substantial direct contact with securities customers (upstairs firms), designated market makers, and floor brokers.³¹ The CFR thereby provides for the fair representation of members in the administration of its affairs of the exchange, including the disciplinary process, consistent with Section 6(b)(3) of the Act.³² In addition to hearing appeals, CFR members receive all proposed settlements, and any member of the CFR may call a proposed settlement for review. The CFR's ability to call settlements for review provides an additional, significant check on the potential misuse of the disciplinary process. Finally, the majority of CFR members voting on a given matter must be independent directors. The Exchange believes that this structure provides an independent and timely check on the disciplinary process .

Further, final actions of the Exchange can be appealed to the Commission, and Commission determinations can be challenged in federal court – in other words, the last two tiers of the appellate process bring the review to bodies completely separate from the Exchange.

5. *The Specific Over the General*

The Comment Letter theorizes that a party could claim that the more specific Fine Income Procedures prevail over Section 4.05, such that if the Fine Income Procedures are removed, the party could claim that the previously covered conduct is no longer prohibited.³³

The Comment Letter is incorrect on this point. Presently, both Section 4.05 and the Fine Income Procedures apply to the Exchange's use of fine income. If the Fine Income Procedures are deleted from the Exchange rules, Section 4.05 will continue to apply to fine income.

6. *Change in Circumstances*

Finally, the Comment Letter disputes the Exchange's statement that the circumstances that led to the Fine Income Procedures no longer exist. Specifically, at the time the Fine Income Procedures were adopted, NYSE Regulation performed regulatory functions on the Exchange's

³¹ See Operating Agreement, Art. II, Sec. 2.03(h)(iii).

³² 15 U.S.C. 78f(b)(3).

³³ Comment letter, at 5.

behalf. Although a predecessor to Section 4.05 (the “Predecessor Section”) was then in effect, on its face, the Predecessor Section, found in the Exchange’s 2006 operating agreement, only limited the Exchange itself. Under the Delegation Agreement, NYSE Regulation had the obligation to assure compliance with the rules of the Exchange, but the Fine Income Procedures provided a more direct commitment by NYSE Regulation to ensure the proper exercise of NYSE Regulation’s power to fine member organizations and the proper use by NYSE Regulation of fines collected.

Today, because the Delegation Agreement is no longer in effect, the same entity that fines member organizations is directly subject to the limits of Section 4.05. Accordingly, the Exchange believes that removing the Fine Income Procedures and relying on Section 4.05 and the provisions governing the ROC would provide adequate protections against the concerns cited by the Commission in the Order Approving the Fine Income Procedures.

The Comment Letter states that although the author understands that NYSE Regulation previously performed regulatory functions, “the argument does not explain what circumstances occurred that will not occur again.”³⁴ The Exchange believes that it has, in fact, explained the changes: previously, NYSE Regulation fined member organizations, while the Predecessor Section applied to the Exchange. Now, because the Delegation Agreement is no longer in effect, the same entity that fines member organizations is directly subject to the limits of Section 4.05.

The Comment Letter also contests that the Proposal “does not explain what the guarantees of lack of reoccurrence are.”³⁵ To clarify, any change to the Exchange’s regulatory structure would require the approval of the Exchange’s Board of Directors and approval by the Commission.

The Exchange appreciates the opportunity to respond to the Comment Letter and respectfully requests the Commission approve the Proposal, as amended.

Very truly yours,



³⁴ Id.

³⁵ Id.