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September 13, 2017

Via Electronic Mail (rule-comments@sec.gov)

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

Re: File No. SR-PHLX-2017-54; SR-NASDAQ-2017-068; SR-BX-2017-032; SR-ISE-2017-77 and SR-GEMX-2017-31; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend the Exchange's Pricing Schedule With Respect to the Options Regulatory Fee

Dear Mr. Fields:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates the opportunity to comment on the above-referenced proposals filed by the Self-Regulatory Organizations (“SROs”), each of which is owned by Nasdaq (the “Filings” or “Nasdaq Filings”) with the Securities and Exchange Commission (“Commission”). In the Filings, Nasdaq proposes to revise parts of its Pricing Schedule to “more closely reflect the manner in which Nasdaq assesses and collects its ORF.”²

While SIFMA supports certain aspects of the filings, we recommend that the Commission suspend the Nasdaq filings under the applicable provisions of the Securities Exchange Act of 1934 (“Exchange Act”) so that the Commission can consider and analyze the proposal and determine whether the proposal should be approved or disapproved. This additional consideration is key because there are important issues in the ORF proposal that SIFMA believes must be resolved to ensure the assessment of ORF is fair and transparent, with a harmonized policy across all listed options exchanges. In particular:

- **Harmonization:** SIFMA supports a harmonized approach for the assessment and collection of ORF across all exchanges that have codified this regulatory fee.

¹ SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over \$2.5 trillion for businesses and municipalities in the U.S., serving clients with over \$20 trillion in assets and managing more than \$67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. 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 See Securities Exchange Act Release No. 34-81343 (August 8, 2017), 82 FR 37964 (August 14, 2017).

- **Assessment Methodology:** SIFMA recommends that the SEC review the data used by the exchanges to assess and collect ORF given the contrasts in the exchange filings surrounding the availability of certain data fields.
- **Assessment of ORF on Away Exchanges:** SIFMA does not support the practice of an options exchange assessing ORF on away exchange transactions, regardless of any regulatory nexus between the charging exchange and the transaction.

1. Harmonization

SIFMA agrees with Nasdaq and supports “a common approach for the assessment and collection of ORF among the various options exchanges that assess such a fee, as well as guidance from the Commission regarding regulatory cost structures to ensure equal knowledge and treatment among options markets assessing ORF.”³ SIFMA has engaged in, and supported, the collective efforts of the exchanges and Commission to harmonize certain, non-competitive rules, such as the obvious and catastrophic error rules. By harmonizing those rules which are regulatory in nature, investors will receive the similar trading experience on each options exchange, regardless of where the execution occurred. There is also a need for further clarification in ORF transparency which would go a long way in mitigating any industry doubts about how the funding is being spent. This enhances investor trust and confidence, and is consistent with the SEC’s mission to “protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.”⁴

SIFMA recommends that each exchange adopt the same rule set for ORF to achieve harmonization across the market since ORF is a regulatory fee (not intended to fund commercial activities).⁵ Many exchanges, including Nasdaq Gemini and Nasdaq ISE⁶, have established a precedent for harmonizing certain aspects of ORF, as evidenced by the adoption of SIFMA’s proposal that requires the Exchanges to provide 30 days written notice prior to a fee change.⁷ SIFMA urges Nasdaq to codify this on its exchanges that presently do not have this provision codified in their rule books, namely Nasdaq BX, Nasdaq Options Market and Nasdaq Phlx.

In a 2015, SIFMA sent a letter to Nasdaq highlighting a SIFMA comment letter in support of rules filings by NYSE Arca and NYSE MKT to amend their respective options fee schedules to specify the frequency with which the exchange may change ORF (February and August), and provide adequate notice to members of the impending change (minimum of 30 days). In its recent filings, this language was removed from the Nasdaq ISE and Nasdaq Gemini filings, which state “The Exchange is proposing to eliminate the requirement that its ORF may be only increased or decreased semi-annually because the Exchange believes it requires the flexibility to amend its ORF as needed to meet its regulatory requirements and adjust its ORF to account

³ Id.

⁴ “What We Do,” U.S. Securities and Exchange Commission, June 10, 2013, <https://www.sec.gov/Article/whatwedo.html>.

⁵ ORF was first introduced by CBOE in 2009, and was designed to cover a portion of the Exchange’s regulatory costs, as opposed to subsidizing for-profit commercial expenditures.

⁶ While Nasdaq provided 30 days-notice for the recent Nasdaq BX and Nasdaq Options Market ORF rate change, SIFMA recommends that these exchanges, along with Nasdaq Phlx, codify this provision of their ORF rules.

⁷ See Securities Exchange Act Release No. 34-81342 (August 8, 2017), 82 FR 37972 (August 14, 2017) and Securities Exchange Act Release No. 34-81345 (August 8, 2017), 82 FR 37940 (August 14, 2017).

for the regulatory revenue that it receives and the costs that it incurs... and to conform the rule with Phlx, NOM and BX.”⁸ SIFMA urges Nasdaq to reconsider this since as it benefits the broker-dealer community if ORF is only modified two times a year. This allows firms to minimize risk and ensure that their systems are configured properly to account for ORF modifications. Additionally, SIFMA members specifically requested that exchanges not modify ORFs in January, since most financial institutions generally prohibit technological changes to their systems between early December and mid-January in an annual code freeze.

Additionally, SIFMA recommends that the Commission require that the options exchanges maintain standardized files which would enhance transparency and ensure the ORF is charged uniformly. In CBOE’s initial ORF filing, the Exchange stated that “revenue generated from the ORF, when combined with all of the Exchange’s other regulatory fees, will be less than or equal to the Exchange’s regulatory costs... In general, on a year over year basis, regulatory fee revenue (not including regulatory fine revenue) only covers about 65% of the Exchange’s regulatory costs.”⁹ Today, exchanges do not include any financial details about ORF, other than the rate. Accordingly, all exchanges should disclose fully and publicly how ORF revenue is allocated and detail the percentage of regulatory costs covered by the ORF. Each exchange should provide a breakdown of the types of costs associated with its regulation and supervision of members’ customer options business.

2. Assessment Methodology

In the Nasdaq Filings, the Exchange illustrates which transactions are assessed an options regulatory fee. Like other exchanges, Nasdaq assesses ORF on all transactions that are executed by a member on Nasdaq that clear in the customer range at OCC. Nasdaq also assesses an ORF for each Customer option transaction that is “cleared by a Nasdaq member at the OCC in the Customer range, even if the transaction was executed by a non-member of Nasdaq, regardless of the exchange on which the transaction occurs.”¹⁰ Nasdaq does not assess ORF “[i]n the case where a member executes a transaction on an away market and a non-member clears the transaction... the ORF is not assessed to the member who executed the transaction or collected from the non-member who cleared the transaction because the Exchange does not have access to the data to make absolutely certain that ORF should apply.”¹¹

The Nasdaq methodology differs notably from other exchanges that assess ORF on all transactions that are executed or cleared by the member in the customer range at OCC regardless of the exchange on which the transaction occurs. Several exchanges, including BOX,¹² C2,¹³ and CBOE¹⁴ utilize this method but do not state in their respective SEC filings

⁸ See 82 FR at 37972 and 37941.

⁹ See Securities Exchange Act Release No. 34-58817 October 20, 2008), 73 FR 63744 (October 27, 2008)

¹⁰ See 82 FR at 37964.

¹¹ See 82 FR at 37965.

¹² See Securities Exchange Act Release No. 34-74201 (February 4, 2015), 80 FR 7512 (February 10, 2015).

¹³ See Securities Exchange Act Release No. 34-76995 (January 28, 2016), 81 FR 5795 (February 3, 2016).

¹⁴ See Securities Exchange Act Release No. 34- 76993 (January 28, 2016), 81 FR 5800 (February 3, 2016).

the source for the data. MIAX¹⁵ and PEARL¹⁶ state in their respective ORF filings that each exchange “uses reports from OCC to determine the identity of the executing clearing firm and ultimate clearing firm”¹⁷ to determine who to collect ORF from, including “a non-Member that was the ultimate clearing firm where a Member was the executing clearing firm for the transaction.”¹⁸ SIFMA questions how some exchanges have transparency into certain data that allows them to collect ORF from non-members on away transactions while other exchanges, including Nasdaq, specify in their SEC filings that they do not have visibility into this information. SIFMA requests that the SEC investigate why this dichotomy exists to ensure the investing public that the options regulatory fee is being fairly assessed, which in turn will boost investor trust and confidence in the U.S. listed-options markets.

3. Assessment of ORF on Away Exchanges:

In its filing, Nasdaq states that “it is reasonable and appropriate for the Exchange to charge the ORF for options transactions regardless of the exchange on which the transactions occur.”¹⁹ Nasdaq uses several justifications to rationalize this practice.

1. “The Exchange has a statutory obligation to enforce compliance by members and their associated persons under the Act and the rules of the Exchange and to surveil for other manipulative conduct by market participants (including non-members) trading on the Exchange. The Exchange cannot effectively surveil for such conduct without looking at and evaluating activity across all options markets... In so doing, the Exchange believes that assessing ORF on member clearing firms in certain instances equitably distributes the collection of ORF in a fair and reasonable manner. Also, the Exchange and the other options exchanges are required to populate a consolidated options audit trail (“COATS”) system to surveil a member’s activities across markets.”²⁰
2. “The Exchange believes that assessing the ORF... where the execution occurs on another exchange and is cleared by a Nasdaq member is an equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities... The Exchange believes that this collection practice is reasonable and appropriate because higher fees are assessed to those members that require more Exchange regulatory services based on the amount of Customer options business they conduct.”²¹
3. “Regulating Customer trading activity is more labor intensive and requires greater expenditure of human and technical resources than regulating non-Customer trading activity, which tends to be more automated and less labor intensive. As a result, the costs associated with administering the Customer component of the Exchange’s overall regulatory program are anticipated to be typically higher than the costs associated with administering the non-Customer component of its regulatory program. The Exchange

¹⁵ See Securities Exchange Act Release No. 34- 81063 (June 30, 2017), 82 FR 31668 (July 7, 2017).

¹⁶ See Securities Exchange Act Release No. 34-80875 (June 7, 2017), 82 FR 27096 (June 13, 2017).

¹⁷ Id.

¹⁸ See 82 FR at 27096-27097.

¹⁹ See 82 FR at 37965.

²⁰ Id.

²¹ Id.

proposes assessing higher fees to those members that will require more Exchange regulatory services based on the amount of Customer options business they conduct.”²²

As we have stated previously, SIFMA appreciates that exchanges have certain statutory obligations to regulate their members and that there has been a traditional practice of exchanges using fees to defray their regulatory expenses. However, the proposal to charge a regulatory fee to a broker-dealer for transactions on away exchanges is inconsistent with the Exchange Act. According to the Exchange Act, the “term ‘facility’ when used with respect to an exchange includes its premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any service thereof for the purpose of effecting or reporting a transaction on an exchange... and any right of the exchange to the use of any property or service.”²³ Additionally, Section 6(b)(4) of the Exchange Act expressly states that an exchange’s rules must provide for the “equitable allocation of reasonable... fees, and other charges among its members... and other persons using *its facilities*.”²⁴ Accordingly, SIFMA questions how an exchange can charge fees to their members for transactions or services that do not occur on its “facilities,” regardless of any regulatory nexus.

SIFMA strongly disagrees with the current codified SRO rules that allow Exchanges to assess regulatory fees for activity that occurs off exchange. SIFMA recommends that the exchanges adopt simplified ORF rules that assess ORF only for those transactions which occur on the exchange, and clear in the customer range at OCC. ORF should be collected by the OCC from the ultimate firm that clears the trade, including non-Members, and distributed to the respective exchange that executed the trade.

For the reasons set forth above, SIFMA recommends that the Commission suspend the Nasdaq filings since the collection of ORF on away transactions is inconsistent with the Securities Exchange Act of 1934. SIFMA re-affirms our view that this is an overly broad application of the ORF, and we urge the Commission to reconsider the ability of any options exchange to charge an ORF on transactions executed on other exchanges.

* * *

SIFMA greatly appreciates the Commission’s consideration of our comments on File No. SR-NASDAQ-2017-54. We would be pleased to discuss these comments in greater detail with the staff of the Commission. If you have any questions, please contact Ellen Greene at [REDACTED] or [REDACTED].

Sincerely,



Ellen Greene
Managing Director

cc: The Honorable Jay Clayton, Chairman, SEC
The Honorable Michael S. Piwowar, Commissioner, SEC

²² See 82 FR at 37965-37966.

²³ 15 U.S.C. § 78f(b)(4) (2016).

²⁴ Id. (emphasis added).

The Honorable Kara M. Stein, Commissioner, SEC

Heather Seidel, Acting Director, Division of Trading and Markets, SEC
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