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VIA E-MAIL: [rule-comments@sec.gov](mailto:rule-comments@sec.gov)

Brent J. Fields  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-0609

*Re: Exchange Act Release No. 34-74581; File No. S7-05-15  
Exemption for Certain Exchange Members*

Dear Mr. Fields:

The FIA Principal Traders Group (“FIA PTG”)<sup>1</sup> appreciates the opportunity to comment on the Securities and Exchange Commission’s (the “SEC” or “Commission”) proposal to amend Rule 15b9-1 under the Securities Exchange Act of 1934 (the “Exchange Act”), which currently provides proprietary trading broker-dealers (each a “Proprietary BD” and collectively, “Proprietary BDs”) engaged in off-exchange trading<sup>2</sup> with an exemption from membership in a national securities association (the “Proposal”)<sup>3</sup>. If adopted, the Proposal would generally require Proprietary BDs engaged in off-exchange trading, including several FIA PTG member firms, to become members of the Financial Industry Regulatory Authority, Inc. (“FINRA”) (being the sole national securities association).<sup>4</sup>

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<sup>1</sup> FIA PTG is an association of more than 20 firms that trade their own capital on exchanges in futures, options and equities markets worldwide. FIA PTG members engage in manual, automated and hybrid methods of trading, and they are active in a wide variety of asset classes, including equities, fixed income, foreign exchange and commodities. FIA PTG member firms serve as a critical source of liquidity, allowing those who use the markets, including individual investors, to manage their risks and invest effectively. FIA PTG advocates for open access to markets, transparency and data-driven policy.

<sup>2</sup> “Off-exchange trading” refers to any securities transaction in an exchange-listed security: (i) that is not effected, directly or indirectly, on a national securities exchange, including trading that occurs on alternative trading systems and directly with a broker-dealer, acting as either agent or principal; or (ii) that is effected by, or on behalf of, a registered broker-dealer on a national securities exchange of which such broker-dealer is not a member.

<sup>3</sup> Exchange Act Release No. 74581 (Mar. 25, 2015), 80 FR 18035 (Apr. 2, 2015).

<sup>4</sup> Alternatively, some Proprietary BDs could decide to change their business models and either: (i) trade solely upon exchanges of which they are members; (ii) cease trading exchange-listed equity securities; or (iii) terminate their registrations as broker-dealers with the SEC.

As noted in our letter submitted to you, dated May 6, 2015, FIA PTG values the opportunity to evaluate and respond to the detailed questions contained in the Proposal, particularly the questions related to the costs associated with FINRA membership. The evaluation of these costs merits careful analysis and thoughtful consideration.

FINRA membership would impose significant regulatory and compliance-related obligations and associated costs on Proprietary BDs, both initially and on an ongoing basis, many of which may not be necessary or appropriate for firms without customer businesses. FINRA is working to mitigate some of these costs and to modify some of its rules and processes to make them more applicable to firms without customers. For example, FINRA is currently conducting a retrospective rule review of its membership application rules to assess their effectiveness and efficiency and requested comments to questions regarding specified membership application rules under review.<sup>5</sup> The comment period expired May 14, 2015.

Additionally, and most significantly from a cost perspective, FINRA is currently requesting comment on a proposal to exclude FINRA's Trading Activity Fee ("TAF") on transactions by a Proprietary BD on exchanges of which the firm is a member.<sup>6</sup> The comment period expires June 19, 2015. We also anticipate that FINRA may take other steps to modify its rules or processes for firms without customers. Adjustments to TAF and other potential changes to fees, rules or processes could represent significant changes in the cost structure of FINRA membership for Proprietary BDs and may significantly change the perspective of FIA PTG in its comments to the Proposal. Changes to TAF fees alone could potentially reduce the total costs of the Proposal to some firms by 90% or more.

Until FINRA provides additional information or guidance on these efforts, it will be challenging for anyone commenting on the Proposal to provide the Commission with a meaningful analysis of the costs of the Proposal or helpful feedback on the questions contained therein. Accordingly, we hope you approve our request to extend the public comment deadline for the Proposal to afford the public time to consider these forthcoming FINRA initiatives in connection with the questions set forth by the Commission in the Proposal.

In the meantime, we provide the following broad comments regarding the Proposal.

#### A. OVERVIEW

In the Proposal, the Commission expressed: (i) its concern that some of the most active cross-market proprietary trading firms may not be subject to effective regulatory oversight by an exchange with respect to the full range of their market activity, since the individual exchanges on which these firms are members are not well-positioned to oversee off-exchange activity; and (ii) its preliminary belief that the current exemption of proprietary trading firms from FINRA membership undermines the effectiveness of regulatory supervision and leaves FINRA charged with the responsibility for the oversight of the off-exchange market without jurisdiction over broker-dealers that conduct a substantial amount of off-exchange trading activity.

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<sup>5</sup> See FINRA Regulatory Notice 15-10, *Retrospective Rule Review* (Mar. 30, 2015), at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Notice\\_Regulatory\\_15-10\\_0.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_15-10_0.pdf).

<sup>6</sup> See FINRA Regulatory Notice 15-13, *Trading Activity Fee (TAF)* (May 5, 2015), at [https://www.finra.org/sites/default/files/notice\\_doc\\_file\\_ref/Notice\\_Regulatory\\_15-13.pdf](https://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_15-13.pdf).

While FIA PTG supports the Commission's desire to enhance the regulatory oversight of off-exchange trading, we are concerned that the costs for firms affected by the Proposal would be substantial (both monetarily and otherwise) and might outweigh the Proposal's limited benefits. We are also concerned that imposing unnecessary costs on Proprietary BDs could hinder competition among liquidity providers, which could negatively impact market liquidity and transaction costs. Moreover, we believe there may be less burdensome alternatives to accomplish the underlying goal set forth in the Proposal. If the Commission decides to move forward with the Proposal, FIA PTG requests that the Commission work with FINRA to reduce the costs of this requirement in ways that are appropriate for the business models of Proprietary BDs.

## B. CONSIDERATION OF COSTS AND BENEFITS

### 1. Benefits appear limited

The Proposal indicates that the primary expected benefit of requiring Proprietary BDs to obtain FINRA membership would be to "supplement the oversight of the exchanges" with respect to off-exchange trading, and that this would "further assist the Commission in obtaining a more complete picture of the activity that occurs on ATSS and elsewhere in the off-exchange market." The specifics of this, however, are hard to understand.

There does not appear to be a significant benefit to market surveillance from this Proposal. It is our understanding that FINRA currently sees 99.6% of exchange volume via OATS reporting by its members<sup>7</sup> and that the 0.4% missing is data from the Chicago Stock Exchange, Inc. (the "CHX"), which FINRA could obtain from the CHX via a regulatory services agreement between the CHX and FINRA. We also note that both the CHX and FINRA are members of the Intermarket Surveillance Group ("ISG"), participants of which already have an information sharing agreement in place. Additionally, because all off-exchange trading needs to go through a FINRA member with its own reporting obligations (*i.e.*, an ATS), we believe all off-exchange messages (*e.g.*, orders, modifies, cancels, etc.), including those of non-FINRA member Proprietary BDs, are currently being reported.

We think the actual issue is not that FINRA doesn't have all of the messages, but rather that some of the messages, including those of non-FINRA member Proprietary BDs, do not carry the necessary identifying information to allow attribution to a particular market participant. Rather than requiring Proprietary BDs engaged in off-exchange trading to become FINRA members, we suggest it would be far simpler and less costly to add the "MPID" or "sender sub-ID" to existing OATS reporting, which would allow for the identification of the market participant. FINRA has already proposed to add this information to OATS reports and we support this proposal.<sup>8</sup>

The Commission asserts that, as an additional benefit, the Proposal would equalize regulatory requirements across FINRA member and non-member firms. This fails to recognize that different firms with different business models may require different types of regulation. FINRA is

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<sup>7</sup> See Proposal, *supra* note 3, at 72, n.172.

<sup>8</sup> See FINRA Regulatory Notice 14-51, *Equity Trading Initiatives: OATS and ATS Reporting Requirements* (Nov. 14, 2014), at <https://www.finra.org/sites/default/files/14-51.pdf>.

currently, and has been historically, geared towards regulating customer business, and it is unclear that all of the costs of FINRA membership are appropriate for firms without customers. Currently Proprietary BDs are regulated by the exchanges of which they are members and by their designated examining authorities (“DEAs”). These self-regulatory organizations (“SROs”) have specific expertise in overseeing Proprietary BDs without customers, and while the actual surveillance functions may be outsourced to FINRA, the programs have been created by the exchange based on its experience with its Proprietary BD members. The Commission argues that FINRA might perform oversight functions better than these SROs or DEAs; however, we fail to see the validity of this argument given the specialized expertise of the existing regulators for Proprietary BDs.

We acknowledge that requiring FINRA membership would likely have some limited jurisdictional benefit. If FINRA identified a rule violation by a Proprietary BD that occurred exclusively off-exchange, they would now have the jurisdiction to seek disciplinary action or enforcement directly, rather than needing to refer the matter to the FINRA member through which the trade occurred, the SEC, the firm’s DEA or an exchange of which the firm is a member. However, it is important to note that the Proposal would only result in FINRA having direct jurisdiction over a relatively small number of Proprietary BDs that trade off-exchange. FINRA would continue to have only indirect jurisdiction (through the FINRA members who operate the ATSS) over the majority of participants in these off-exchange markets, including hedge funds and other investors that are not structured as broker-dealers.

## 2. Costs to Proprietary BDs may be substantial

FIA PTG believes that the costs associated with FINRA membership presently outweigh the perceived benefits. These costs include both one-time and recurring costs for the affected Proprietary BDs including, without limitation: initial membership application, continuing membership applications, daily OATS reporting, TAF fees, registration and examination fees, gross income assessment fees and ongoing audit/examination and reporting requirements.

FINRA membership is not a trivial endeavor.<sup>9</sup> Obtaining FINRA membership would require firms to review and analyze the applicability of a vast array of FINRA rules and interpretations that they were previously not subject to - many of which are not relevant to firms without customers. Subjecting firms to FINRA membership and the related costs thereto would simply create another layer of regulation, rules and costs for those firms and subject them to duplicative rules, costs, regulatory examinations and oversight.

Our research indicates that, unlike the exchange membership application process (which can take as little as a few days and no longer than a couple months), the current FINRA membership application process generally takes 6 to 9 months from submission of the application to approval. Similar concerns exist for Proprietary BDs who are not NASDAQ members with respect to FINRA’s continuing membership application process (NASD Rule

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<sup>9</sup> FINRA provides potential applicants for firm registration with the following warning on its website: “Firms should carefully consider applying for FINRA membership. It is a serious undertaking. Depending on your desired goals, you might consider alternatives to applying for membership. For instance, you might achieve your objectives by working for an existing member firm or managing a branch office, thus avoiding the rigorous firm application process. If you decide to apply, it is imperative that you fully understand all of FINRA’s substantive and procedural requirements.” See FINRA Website: *Register a New Firm*, <http://www.finra.org/industry/new-bd-firm-registration>.

1017) including the length of the application process and potential undue burden to Proprietary BDs based on the rule's broad language.

The monetary cost of the application process varies based on the size of the firm, number of registrants and whether you perform the functions internally or outsource them, but we estimate an average one-time cost of \$200,000 to \$250,000. To lessen this cost, both in monetary and human resources, should the Commission approve the Proposal, we request that the Commission require FINRA to develop a "fast track" application process for Proprietary BDs without customers who are already members of other SROs. If FINRA does not create an expedited application process for Proprietary BDs, we ask the Commission to extend the membership requirement from 360 days, to 360 days for submission of the application and 540 days for approval.

There are also significant annual costs directly associated with maintaining FINRA membership, including, without limitation, personnel assessment fees and gross income assessments. These fees would exceed \$100,000 per year for many Proprietary BDs.

Some Proprietary BDs are already required to submit OATS data upon request pursuant to NASDAQ and NYSE exchange rules, whereas others have no current OATS obligations. In either case daily reporting will be an additional requirement with new costs. These costs will be spread across IT and compliance personnel and include setup of an FTP site for data retrieval and submission, file creation and transmission, compliance review and research of file edits and errors, as well as data correction and resubmission. We estimate these costs to be \$150,000 to \$200,000 per year, likely higher for the first year. We note that our cost estimates are less than what the Commission projected in the Proposal, which we understand were based on consolidated audit trail reporting requirements. We also understand there may be outsourced options for OATS reporting; however, we would need more time to evaluate whether that could be a viable and more cost effective solution. Even if Proprietary BDs are required to become FINRA members, to mitigate the costs of the Proposal, such firms should only be required to submit OATS reports that do not duplicate data already reported to FINRA.

At present, only proprietary transactions executed on a national securities exchange in a member's capacity as an exchange specialist or market maker are excluded from the TAF. As a result if FIA PTG members and other Proprietary BDs are required to become FINRA members they would incur substantial TAF not previously incurred. Because TAF is a volume dependent calculation it is very difficult for us to estimate the annual cost, but we would not be surprised if it is greater than \$1,000,000 per year for many firms. As noted above, we appreciate that FINRA is in the process of revisiting its current fee structure, and the exemption proposed in its recent regulatory notice, if adopted, would result in significant savings.

The Commission should also consider that FINRA membership would create additional costs for Proprietary BDs trading corporate bonds who would be required to pay TRACE fees.

C. CONCLUSION

Evaluating the impact of required FINRA membership is challenging while FINRA is in the midst of revising their fees and processes; however, as defined today, we do not feel the benefits described in the Proposal warrant the costs.

If, however, the Commission decides to move forward with the Proposal, FIA PTG requests that the Commission require FINRA to make certain changes to its processes and fees to reduce the cost of this requirement on Proprietary BDs. Specifically, we would suggest that FINRA: (i) create a streamlined membership application process for Proprietary BDs who are already members of other SROs; (ii) exempt transactions executed by a FINRA member on an exchange of which the firm is a member from the TAF; and (iii) create an audit/examination program tailored to the activities of Proprietary BDs without customers.

We appreciate the opportunity to comment on the Proposal and look forward to working with the Commission going forward. If you have any questions, or if we can provide further information, please do not hesitate to contact Mary Ann Burns at [maburns@fia.org](mailto:maburns@fia.org).

Respectfully,

FIA Principal Traders Group



Mary Ann Burns  
Chief Operating Officer  
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cc: Mary Jo White, Chair  
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