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October 14, 2016

**Via Electronic Mail ([rule-coments@sec.gov](mailto:rule-coments@sec.gov))**

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

Re: Bats BZX Exchange, Inc., Suspension of and Order Instituting Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change to Modify the Bats BZX Options Regulatory Fee (File No. SR-BatsBZX-2016-42)

Dear Mr. Fields:

The Securities Industry and Financial Markets Association (“SIFMA”)<sup>1</sup> appreciates the opportunity to comment on the above-referenced filing made by Bats BZX Exchange, Inc. (“BZX”) with the Securities and Exchange Commission (“Commission”). In that filing, BZX applied its newly reduced Options Regulatory Fee (“ORF”) from \$0.0010 per contract side to \$0.0008 per contract side. In addition, BZX filed a rule that would apply the ORF to all customer options transactions on all options exchanges, regardless of whether they are executed or cleared by a BZX member. BZX proposed to accomplish this by collecting the ORF from The Options Clearing Corporation (“OCC”) on all options transactions OCC clears in the “customer” range on all options exchanges.

The Commission has suspended the BZX proposal and requested comment on specific questions related to the justification of imposing the ORF on non-members and on non-BZX options transactions.<sup>2</sup> No other options exchange has sought authority to apply the ORF (or other transaction-based fee) to a non-member. As discussed below, however, we have reason to believe that certain exchanges are assessing non-members an ORF without a rule supporting such fees.

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<sup>1</sup> SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA’s mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit [www.sifma.org](http://www.sifma.org).

<sup>2</sup> Bats BZX Exchange, Inc.; Suspension of and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Modify the Options Regulatory Fee, Exchange Act Release No. 34-78849 (Sept. 15, 2016), 81 FR 64960 (Sept. 21, 2016) (suspending the BZX proposal and soliciting comments on the same).

As an initial matter, SIFMA understands that the self-regulatory model in the securities markets is premised on being supported by broker-dealer funding, and SIFMA supports the need for broker-dealers to contribute to the funding of regulation of listed options trading. Since the introduction of the ORF by the various options exchanges, SIFMA generally has supported a transaction-based fee to contribute to the costs associated with an exchange's supervision and regulation of a member's or trading permit holder's customer options business. However, the exchanges, including BATS, are for-profit entities and do not have unlimited authority to charge broker-dealers. SIFMA objects to the proposal that an exchange be permitted to levy regulatory fees on non-members.

Given the issues raised by the BZX proposal, we urge the Commission to review the ORF program at all of the options exchanges. The Commission should direct the exchanges to provide full public disclosure of the categories of regulatory activity covered by the fees and the specific total costs of those activities, along with the total amount revenue they receive from the ORF.<sup>3</sup> Currently, the exchanges make no such disclosure to the public or to member firms. As the BZX proposal demonstrates, transparency is necessary to evaluate whether the fees are reasonable and appropriately related to the exchange's stated purpose in imposing them.

In its order suspending the BZX proposal, the Commission noted that it is considering whether assessing the ORF on transactions of non-members—where no BZX member executed or cleared the trade—is consistent with the statutory requirements applicable to national securities exchanges under the Securities Exchange Act of 1934 (“Exchange Act”). On its face, the proposal to charge a transaction fee to a broker-dealer that is not a member of the exchange is inconsistent with the Exchange Act. 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*.”<sup>4</sup>

Allowing BZX to charge non-members that do not use BZX exchange facilities and whose customers do not use BZX exchange facilities would render the statutory language meaningless. SIFMA fails to see how a broker-dealer that executes a transaction away from BZX and that never seeks to use BZX exchange services could be viewed as “using its facilities.” Put another way, there is no regulatory nexus between the non-member and BZX to justify the proposed fee where there is no connection to the transaction services offered by BZX.

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<sup>3</sup> SIFMA recently made a similar request in connection with funding the Consolidated Audit Trail. Letter from Theodore R. Lazo, Managing Dir. & Assoc. Gen. Counsel, Sec. Indus. & Fin. Mkts. Ass'n, and Ellen Greene, Managing Dir., Sec. Indus. & Fin. Mkts. Ass'n, to Brent J. Fields, Sec'y, U.S. Sec. & Exchange Comm'n (July 18, 2016). SIFMA asked the Commission to require self-regulatory organizations (“SROs”) “to engage an independent third-party to conduct an audit and review of the SROs’ current regulatory revenues and how that money is allocated, and the [Commission] should publish the results of that audit.” *Id.* at 14.

<sup>4</sup> 15 U.S.C.A. § 78f(b)(4) (2016) (emphasis added).

Furthermore, the premise of Section 6 is that each exchange must have “the capacity...to enforce compliance by its members and persons associated with its members” with the rules of the exchange and with the Exchange Act and the rules thereunder.<sup>5</sup> Members of BZX have agreed to abide by the exchange’s rules and are subject to the jurisdiction of BZX to enforce those rules and the Exchange Act with respect to activity on BZX.<sup>6</sup> In contrast, non-members have no such agreements with BZX. Instead, non-members are subject to the jurisdiction of the exchanges of which they are members to enforce exchange rules and the Exchange Act. BZX is limited to enforcing its rules and the Exchange Act within the disciplinary processes set forth in BZX rules. Simply put, BZX has no jurisdictional reach over non-members.<sup>7</sup> As such, BZX cannot justify its proposed fee for non-members because it does not have the capacity to enforce compliance of the proposed fee as required under the Exchange Act.

BZX claims that if the ORF was not applied to activity across all options exchanges – including for non-members – trading participants would send their orders to the least regulated exchange to avoid being assessed an ORF. We believe this argument misses the point. It is the obligation of each exchange to determine how to most effectively carry out its regulatory obligations and cover the costs of such regulation, subject to the Commission’s oversight. It is not the role of BZX or of any other exchange to charge regulatory fees to non-members based on the unsubstantiated view that other exchanges are insufficiently regulated. Furthermore, broker-dealers representing customer orders are subject to best execution obligations and must route orders based on those principles.

SIFMA’s view on BZX’s ability to charge non-members an ORF applies equally to other exchanges. Today, six exchanges (MIAX Options Exchange, Chicago Board Options Exchange, Inc., C2 Options Exchange, Inc., International Securities Exchange, LLC, ISE Gemini, LLC, and BOX Options Exchange LLC) assess an ORF on all contracts that are cleared in the customer range at OCC for all transactions that were either executed or cleared by a member firm or trading permit holder, regardless of the exchange used for execution. In our view, 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. What is more, SIFMA members have indicated

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<sup>5</sup> § 78f(b)(1).

<sup>6</sup> The Bats Global Markets, Inc. membership application states that “[b]y executing this Application, the undersigned agrees as follows: (1) To abide by, comply with, and adhere to the provisions of the Exchange’s Certificate of Incorporation, its By-Laws, the Exchange Rules, the policies, interpretations and guidelines of the Exchange and all orders and decisions of the Exchange’s Board of Directors and penalties imposed by the Board of Directors, and any duly authorized committee (such agreement is not to be construed as a waiver by the undersigned of any right to appeal provided in the Securities Exchange Act of 1934, as amended).” *Bats Global Markets, Inc. Membership Application*, BATSTRADING.COM 5 (updated Feb. 25, 2016), [http://cdn.batstrading.com/resources/membership/BATS\\_DirectEdge\\_Membership\\_Application.pdf](http://cdn.batstrading.com/resources/membership/BATS_DirectEdge_Membership_Application.pdf).

<sup>7</sup> See *Fiero v. Fin. Indus. Regulatory Auth.*, 660 F.3d 569 (2d Cir. 2011) (holding that SROs are limited to the SRO’s disciplinary processes to enforce the collection of fines and have no statutory authority to use the judicial process).

that they are currently being assessed the ORF by those six exchanges, even those of which they are not a member. This practice simply should not be allowed to continue given that the fees are not supported by relevant exchange rules or the Exchange Act itself. It will be important for the Commission to review these practices to verify that the current practice and assessment of fees is consistent with the existing authority in exchange rules and the Exchange Act. The Commission should review these practices both in terms of charging the ORF to non-members and to charging the ORF to members for their transactions on other exchanges.

As a part of its review, SIFMA urges the Commission to examine the method each exchange uses to calculate the ORF. Several exchanges have identical or parallel rules instituting an ORF and describing how the ORF is charged. In practice, however, the exchanges do not interpret or apply the ORF rules consistently. In addition to reviewing current practices, the Commission should require exchanges to maintain standardized files that would enhance transparency and ensure the ORF is charged uniformly.

SIFMA notes that BZX has committed to monitoring the amount of revenue collected from the ORF to ensure that it, in combination with its other regulatory fees and fines, does not exceed BZX's total regulatory costs. This does not go far enough. SIFMA urges the Commission to require BZX and all of the options exchanges to disclose fully and publicly how ORF revenue is allocated and to 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. For example, BZX notes that it has costs associated with performing routine surveillance and investigation, policy, rulemaking, interpretive and enforcement activities. Members and the public have no insight into these costs and no way to judge whether the fee revenue proposed to subsidize these costs falls short or exceeds the needed amounts.

SIFMA is particularly concerned that exchanges could use ORF revenue to offset costs that go beyond appropriate regulatory expenses. For new exchanges with negligible transaction volume, an ORF assessed on every transaction cleared in the "customer" range at the OCC by its members or by non-members could be a windfall of revenue well in excess of any reasonable and appropriate regulatory costs. It would be inappropriate for a new exchange to use the ORF revenue to subsidize its startup costs for operating the exchange.

In addition, SIFMA is concerned that the ORF might be collected on the premise of covering costs already covered by other fees. Without transparency as to the ORF revenues collected and the specific types and costs of regulatory activities covered, it is impossible for regulators and the industry to monitor for such duplication.<sup>8</sup>

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<sup>8</sup> SIFMA has noted this concern in previous comment letters. See Letter from Theodore R. Lazo, Managing Dir. and Assoc. Gen. Counsel, Sec. Indus. & Fin. Mkts. Ass'n, to Mary Jo White, Chair, U.S. Sec. & Exchange Comm'n (July 31, 2013). "There is little transparency into the magnitude of regulatory and related fees received by SROs and the amounts the SROs spend on regulatory activities. This lack of transparency makes it impossible for SRO members to consider the reasonableness of fees or to be

The BZX proposal and the important questions raised within the Commission's order demonstrate that there are significant inconsistencies in applying the ORF across the industry. Given that the exchanges and the industry have several years of experience with the ORF since its introduction in 2009, it is time that the current practices for assessing the ORF be reviewed and the exchanges be required to make available a detailed analysis of the ORF revenue attributed to each exchange and how that revenue is utilized.

SIFMA greatly appreciates the Commission's consideration of our comments in connection with File No. SR-BatsBZX-2016-42. 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 (212) 313-1287 or [egreene@sifma.org](mailto:egreene@sifma.org).

Sincerely,



Ellen Greene  
Managing Director

cc: The Honorable Mary Jo White, Chair, SEC  
The Honorable Michael S. Piwowar, Commissioner, SEC  
The Honorable Kara M. Stein, Commissioner, SEC

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