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November 2, 2016

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

Mr. Brent J. Fields
Secretary
U.S. Securities & Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: File No. SR-NYSE-2016-66: Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Amending Article IV, Section 4.05 of the Tenth Amended and Restated Operating Agreement of the Exchange

Dear Mr. Fields:

The Securities Industry and Financial Markets Association (SIFMA)[1] submits this letter to comment on the above-referenced proposed rule change, which the New York Stock Exchange ("NYSE") has filed for immediate effectiveness with the Securities and Exchange Commission ("Commission"). Under the proposed rule change, NYSE has made certain changes to its Limited Liability Company Operating Agreement (the "Operating Agreement"). SIFMA does not object to the changes to the NYSE Operating Agreement. However, one aspect of the rule change raises a broader issue of significant concern to SIFMA member firms – specifically, exchanges' use of regulatory revenues.

Under the proposed rule change, NYSE has amended Section 4.05 of its Operating Agreement to state that:

> Any regulatory assets or any regulatory fees, fines or penalties collected by [NYSE]'s regulatory staff will be applied to fund the legal, regulatory and surveillance operations of [NYSE], and [NYSE] shall not distribute such assets, fees, fines, or other penalties to [its parent entity] or any other entity.

[1] The Securities Industry and Financial Markets Association (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 (GFMA). For more information, visit http://www.sifma.org.

We request that the Commission clarify more specifically the permissible uses by an exchange of those regulatory assets, fees, fines or penalties ("Regulatory Revenues") collected by an exchange.

Background

Exchanges fulfill two separate roles under the terms of the Securities Exchange Act of 1934 ("Exchange Act"). First, an exchange acts as a marketplace for the trading of securities.[2] Second, an exchange acts as a self-regulatory organization ("SRO") overseeing its members.[3] In this way, the Exchange Act defines an exchange by reference to its market function, but it additionally requires an exchange to act as a SRO that enforces securities law compliance on its members.[4] The essential nature and purpose of a national securities exchange – operating a market – is separate from its role as an SRO. This distinction has become important as securities exchange operators have evolved from member-owned utilities to for-profit, often publicly-traded business enterprises.

In this context, SIFMA has raised the need for exchanges to provide increased transparency about their Regulatory Revenues and expenditures.[5] Although the exchanges operate as for-profit commercial enterprises, they still expect member firms to fund their regulatory operations. Accordingly, SIFMA has two areas of specific comment on the NYSE filing. First, we reiterate the need for exchanges to provide additional transparency on the amount of Regulatory Revenues they receive and how they are spent. Second, we question the scope of Section 4.05 of the Operating Agreement – as well as similar provisions in effect at other exchanges.

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[2] An "exchange" is defined as an organization that "constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities." Exchange Act § 3(a)(1). Rule 3b-16 under the Exchange Act interprets an organization to meet this definition if it both (i) "brings together the orders for securities of multiple buyers and sellers," and (ii) "uses established, non-discretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade." *See* Exchange Act Rule 3b-16; Exchange Act Release 40760 (Dec. 8, 1998); see also Section 6 of the Exchange Act (setting forth statutory requirements for the operation of exchanges).

[3] *See* Section 3(a)(26) of the Exchange Act (defining the term "self-regulatory organization" to include any national securities exchange; see also Section 19 of the Exchange Act (setting forth statutory requirements for the operation of self-regulatory organizations).

[4] *See* Exchange Act §§ 6(b), 19(g).

[5] *See* Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, SIFMA to Brent J. Fields, Secretary, Securities and Exchange Commission dated July 18, 2016 ("SIFMA Consolidated Audit Trail NMS Plan Letter"); *see also* Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, SIFMA to Brent J. Fields, Secretary, Securities and Exchange Commission dated June 1, 2015 ("SIFMA Proposed Rule 15b9-1 Letter").

Analysis

On the first point, SIFMA understands that the self-regulatory model in the securities markets is premised on being supported by broker-dealer funding, but exchanges do not have unlimited authority to charge broker-dealers to support their SRO function. Currently, exchanges receive a significant amount of regulatory revenue from broker-dealers through membership fees, registration and licensing fees, dedicated regulatory fees, options regulatory fees, and monetary fines. In addition, the SROs receive a significant amount of revenue from the sale of consolidated market data, and the Commission has long contemplated that that revenue is primarily intended to fund the costs of SROs' regulatory functions, particularly those relating to the SROs' market surveillance activities.[6]

In this regard, we urge the Commission to require the exchanges to engage an independent third-party to conduct an audit and review of their current regulatory revenues and how that money is allocated, and we believe the Commission should publish the results of that audit. Without this information, broker-dealers and other market participants have no way of determining whether the exchanges' regulatory fees are either reasonable or equitably allocated, as required by the Exchange Act.

On the second point, we question the exchanges' use of Regulatory Revenues to fund their legal operations. Under the rule change, NYSE is now expressly permitted to use Regulatory Revenues to fund NYSE's "legal" operations. NYSE notes that a number of other exchanges have given themselves similar authority. However, this aspect of the exchanges' authority could allow regulatory assets, fees, fines, or other penalties to be used for commercial purposes. In today's exchange companies, the "legal" operation can support both the SRO function of an exchange (*i.e.*, the function of regulating members) and the commercial operation of the exchange itself. The fact that an exchange is an SRO does not mean that all of its functions are SRO functions. Rather, the two functions are separate, and exchanges' governing documents properly reflect that Regulatory Revenue may not fund the exchanges' commercial function. However, the governing documents should go further, and they should specify that regulatory revenues may not fund the legal operations that support the exchange's commercial functions.

As a result, we ask that the Commission clarify that exchanges are not permitted to use Regulatory Revenues to fund legal operations that support their commercial activities. This prohibition should apply to obvious commercial activity such as corporate and litigation matters. In addition, this prohibition should extend to exchanges' preparation of rule changes filed with the Commission for their business operations, including filings on trading systems, and market data products, as well as fee filings related to the exchanges' business operations.

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[6] *See* Concept Release: Regulation of Market Information Fees and Revenue, Securities Exchange Act Release No. 42208 (Dec. 8, 1999)

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SIFMA 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, please contact either me (at 202-962-7383 or tlazo@sifma.org) or Timothy Cummings (at 212-313-1239 or tcummings@sifma.org).

Sincerely,

Theodore R. Lazo
Managing Director and
Associate General Counsel

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

Stephen Luparello, Director, Division of Trading and Markets
Gary Goldsholle, Deputy Director, Division of Trading and Markets
David S. Shillman, Associate Director, Division of Trading and Markets