September 27, 2022

VIA ELECTRONIC SUBMISSION

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Exemption for Certain Exchange Members (No. S7-05-15)

Dear Ms. Countryman:

Cboe Global Markets, Inc. ("Cboe") submits this comment letter in response to the Securities and Exchange Commission ("SEC" or "Commission") Re-Proposal ("Re-Proposal")[1] to amend an exemption from Section 15(b)(8) of the Securities Exchange Act of 1934 (the "Act") regarding requiring any broker-dealer registered with the SEC to become a member of a national securities association (currently only the Financial Industry Regulatory Authority, Inc. or "FINRA"). The Re-Proposal would unnecessarily require options trading firms properly regulated by national securities exchanges to register with FINRA.

The Re-Proposal would amend Rule 15b9-1 by narrowing the available trading exemptions. Under the Re-Proposal, a Commission-registered broker-dealer would be required to become a member of FINRA if it effects transactions in securities other than on an exchange of which it is a member unless all of the following conditions are met: (1) it is a member of a national securities exchange; (2) it carries no customer accounts; and (3) such transactions (i) result solely from orders that are routed by a national securities exchange of which the broker-dealer is a member to comply with Rule 611 of Regulation NMS or the Options Order Protection and Locked/Crossed Market Plan; or (ii) are solely for the purpose of executing the stock leg of a stock-option order.

We operate four U.S. listed options exchanges ("Cboe Exchange, Inc.," "Cboe C2 Exchange, Inc.," "Cboe BZX Exchange, Inc.," and "Cboe EDGX Exchange, Inc."), including the largest U.S. options exchange ("Cboe Exchange, Inc."). Additionally, as self-regulatory organizations ("SROs"), Cboe's exchanges have a robust regulatory framework for overseeing trading activity on their markets, which includes regulatory service agreements, and other intermarket and cooperative regulatory programs. Cboe Exchange, Inc. is also currently a designated examining authority ("DEA") under Rule 17d-1[2] for numerous options trading firms.

[1] Securities Exchange Act Release No. 95388 (July 29, 2022), 87 FR 49930 (August 12, 2022).

[2] Rule 17d-1 under the Act authorizes the Commission to name a single SRO as the DEA to examine common members for compliance with the financial responsibility requirements imposed by the Act, or by Commission or SRO rules.

Cboe Exchange, Inc., as well as Cboe's other affiliated exchanges, are also parties to various Rule 17d-2[3] agreements.

Cboe is generally supportive of requiring FINRA membership for trading firms that effect the majority of their transactions off-exchange,[4] however, as highlighted, the Re-Proposal is considerably more expansive than that.[5] Cboe is concerned that the Re-Proposal would also require FINRA membership for options trading firms that primarily trade on exchanges where they are members, but sometimes trade on venues where they may not be members in furtherance of their home exchange activity. Cboe believes that any final rule should clearly exempt broker-dealers from FINRA membership if their away-market or off-exchange activity is for the purpose of hedging the risk of their home exchange activity, and/or in furtherance of best execution, order protection, or locked/crossed market compliance requirements (whether satisfying those requirements through exchange-provided routing services or other broker-dealer routing currently permitted under the distributive linkage rules in operation today). Accommodating these suggested improvements would help ensure that options market quality is not adversely impacted while allowing the Commission to largely achieve its stated objectives under the Re-Proposal.

Certain Exemptions Should Continue to be Allowed to Maintain a Robust Options Market

The Re-Proposal largely focuses on the lack of TRACE[6] reporting for non-FINRA members for their fixed income transactions. Cboe believes it is appropriate for non-FINRA broker-dealers that effect fixed income transactions to register with FINRA to ensure FINRA insight into, and sufficient regulatory coverage of, those transactions. However, the Re-Proposal also suggests that non-FINRA firms that conduct sizable equities volume should also register with FINRA. The Commission cites in the Re-Proposal that the amendments would result in 65 firms being required to join FINRA (unless they qualify for one of the proposed exceptions to the amended rule).[7] Part of the justification for this expansion of firms that would be required to register with FINRA is the amount of transaction volume being generated by these firms both in U.S. Treasury securities and equities.

A more tailored version of the Re-Proposal would further the Commission's objectives without imposing unnecessary financial burdens on options trading firms that already are subject to robust regulatory oversight. Volume effected by these firms in the equities market is hedging activity and often processed

[3] Rule 17d-2 under the Act permits SROs to propose joint plans among two or more SROs for the allocation of regulatory responsibility with respect to their common members.
[4] *See* Re-Proposal, at FN 6 (defining "off-exchange" for the purposes of the Re-Proposal as any securities transaction covered by Section 15(b)(8) of the Act that is not effected, directly or indirectly, on a national securities exchange).
[5] Under the existing Rule 15b9-1 provisions, the exemption from national securities association membership applies to any broker-dealer if it (1) is a member of a national securities exchange, (2) carries no customer accounts, and (3) has annual gross income derived from purchases and sales of securities otherwise than on a national securities exchange of which it is a member in an amount no greater than $1,000. The gross income limitation does not apply to income derived from transactions (1) for the dealer's own account with or through another registered broker or dealer or (2) through the Intermarket Trading System, which refers to the intermarket communications linkage operated jointly by certain self-regulatory organizations pursuant to a plan filed with, and approved by, the Commission pursuant to Rule 608 of Regulation NMS.
[6] *See* FINRA Rule 6700 Series.
[7] Re-Proposal at 49941.

through FINRA members. Thus, they are effectively trading as customers. All SROs, including the options exchanges and FINRA, already have access to these trades via the Consolidated Audit Trail ("CAT") and requiring registration of options trading firms with FINRA is no more useful than requiring registration for any non-broker-dealer customers that trade in the equities market through a FINRA registered broker-dealer. Narrowing the amendments to Rule 15b9-1 to focus on non-option trading firms that primarily transact off-exchange in equities and that trade U.S. Treasury securities would largely achieve the policy goals of the Re-Proposal without unnecessarily disrupting the listed options market.

The existence of a stock-option exemption in the Re-Proposal is an acknowledgment that activity critical to the functioning of the options market should not be adversely impacted by the Re-Proposal. Facilitating hedging activity by options market makers is certainly essential to a well-functioning options market also. Yet, the Re-Proposal states that a proposed hedging exemption might "swallow the amended rule, as proposed, and would not be appropriate."[8] Cboe disagrees and believes such an exemption is prudent and necessary. In response to the Re-Proposal's question on whether a hedging exemption outside of the limited stock-options order exemption would be appropriate,[9] Cboe suggests that a broader, separate hedging exemption be included to ensure options liquidity provision is not harmed or compromised.

It is widely understood that options market makers are critically important to the price discovery process for listed options and hedging their options transactions is crucial for risk management and liquidity provision purposes. Importantly, options market making firms conduct the vast majority of their trading activity on exchanges of which they are members with off-exchange and non-member exchange trading conducted through third-party broker-dealers that may themselves be FINRA members. These options firms are already appropriately regulated (and subject to jurisdiction of at least one exchange SRO), and this type of hedging activity should be expressly exempt. Cboe suggests that any final rule should clearly exempt broker-dealers from FINRA membership if their away exchange activity in equities or listed options is for the purpose of hedging the risk of their home exchange market making activity or in furtherance of that activity.

The Re-Proposal contains an exemption for orders that are routed by member exchanges in order to comply with Rule 611 or the Options Order Protection and Locked/Crossed Market Plan and seeks input on if the scope of the routing exemption should be broadened to include broker-dealer routing that is not done by the member exchange.[10] Cboe believes any final rule should contain a broader routing exemption for options traders. Specifically, options trading firms may need to route to non-member exchanges through non-exchange routers. These types of listed options orders are typically routed to non-member exchanges via another broker-dealer and importantly, this type of trading activity is directly related to and in furtherance of their home exchange listed options trading activity and fulfilling their market-making or brokerage agency duties, as applicable. These suggested changes would help ensure the listed options market is not harmed. Importantly, regulation of the listed options and equities markets would not be compromised in any way.

[8] Re-Proposal at 49949.
[9] Re-Proposal at 49950.
[10] Re-Proposal at 49946.

FINRA Oversight Would be Duplicative and Unnecessary for Broker-Dealers Who are Already Subjected to Effective Regulatory Oversight

The U.S. securities markets operate within a sophisticated regulatory regime that relies on self-regulation as a key component. We agree with the Commission that the exchange SROs have expertise in supervising their members' on-exchange trading activity, and that this robust oversight is complimented by FINRA's oversight of off-exchange securities trading. However, Cboe believes the regulatory framework for oversight of exchange activity, including cross-exchange activity, is already sufficient, and the Re-Proposal adds unnecessary duplication for options broker-dealers not currently obligated to be FINRA members. Cboe believes a more tailored proposal as suggested above would address any perceived gaps in the regulatory framework and avoid detrimental market structure implications.

Under the regulatory framework for the U.S. securities markets, an SRO has an obligation to ensure its members and persons associated with its members, comply with the provisions of the Act, the rules and regulations thereunder, and the SRO's own rules, unless the SRO is otherwise relieved of the obligations under the Act. The current framework for SRO oversight of on-exchange activity works. Exchange SROs are front-line experts and are best situated to provide regulatory oversight of their member firms' on-exchange activity (including cross-exchange activity). The exchanges know their markets best, including the products traded, the intricacies of the trading mechanics, and their members' business models. Requiring FINRA membership for broker-dealers that operate across exchange markets but do not raise retail investor protection concerns reaps little regulatory benefit, if any, compared to the additional burden of FINRA membership.

Just like any other customer, a broker-dealer that is not a member of an exchange must access the exchange through a member. In any instance where a non-member violates the rules of the exchange, that exchange can take action against its member for violations associated with the conduct (including, e.g., violations of the Market Access Rule (Rule 15c3-5 under the Act), failure to supervise, or failure to ------observe just and equitable principles of trade). In addition, where the primary actor is another broker-dealer, the activity may be referred to another SRO(s) where that broker-dealer is a member (whether that be FINRA or another exchange SRO). Further, there is precedent for SROs to adopt rules that specifically enforce the rules of another exchange by its members where that member is not a member of the other exchange on which the transaction was effected.[11] In these circumstances, and others like it, FINRA membership may have the unwarranted effect of duplicative disciplinary actions and additional regulatory fines. In fact, this already occurs under the current market structure for violations by dual FINRA and exchange members for activity occurring on a single market.

In addition to the above, the SROs have a longstanding history of regulatory cooperation to close any perceived gaps in coverage and that cooperation continues to evolve to meet the demands of the current environment. This is demonstrated where multiple memberships result in duplication of regulatory efforts. As noted in the *Staff Paper on Cross-Market Regulatory Coordination*, "[w]hile multiple SROs reviewing the same securities activities can have benefits, in that the resources and expertise from several

[11] *See, e.g.*, Cboe BZX Exchange, Inc. Rule 18.7, *Position Limits*, which in paragraph (a)(3) allows for BZX to have jurisdiction where an Options Member or its Customer "exceed[s] the applicable position limit fixed from time to time by another exchange for an options contract not traded on BZX Options, when the Options Member is not an options member of the other exchange on which the transaction was effected."

organizations can be brought to bear on assessing these activities, it also can lead to duplication and inefficiencies in the regulatory process and increased burdens on member firms."[12]

To combat duplication of efforts in the limited circumstances where this occurs,[13] the SROs already have a robust process for regulatory cooperation where a broker-dealer is a member of multiple exchanges and/or FINRA. Each of us is a member of the International Surveillance Group ("ISG") formed to facilitate the coordination amongst its members to identify possible fraudulent and manipulative activities across markets and to facilitate information sharing related to those efforts.[14] In recent years, the Cross Market Regulation Working Group ("CMRWG") was established as a working group of the ISG U.S. Subgroup to focus on additional ways to reduce unnecessary regulatory duplication.[15] The CMRWG serves as a non-exclusive forum for its SRO participants' regulatory employees to share information and collaborate in connection with their ongoing surveillance, investigation, and enforcement efforts. Through the efforts of the CMRWG, SROs with jurisdiction over a matter continue to conduct independent investigations, but coordinate information requests, interviews, and other communications with the subject broker-dealer(s) to reduce time and resources expended at both the SROs and the subject firm. The CMRWG has demonstrated its effectiveness in recent ongoing regulatory matters. Even before establishment of the CMRWG, the SROs cooperated through coordination under ISG.

While the SROs actively cooperate with one another, to add additional layers of duplicative regulatory obligations via FINRA membership is unwarranted. The Re-Proposal indicates that when a non-FINRA member effects a securities transaction on an off-member-exchange, the firm is subject to the rules and interpretations of the various exchanges to which it is a member, and that rule interpretations can vary between exchanges. The reality is that adding FINRA as an additional layer, only adds to regulatory duplication and administrative burden by adding an additional set of rules and interpretations to which the current non-FINRA member must comply. Unless relieved of regulatory responsibility under the Act, the exchange SROs will continue to have jurisdiction over their members and are required by the Act to ensure compliance with their rules and the interpretations of the same.

There are also other means of addressing duplication and applications of common rules (as opposed to SRO-specific/centric rules). The Act allows for allocation of regulatory responsibility to a single SRO, and the efficiencies inherent in section 17(d)(1) of the Act are already ingrained in the fabric of today's regulatory framework. Historically, allocation of regulatory responsibility has focused on common SRO rules and statutory requirements best suited for examination and not on on-exchange or market-specific trading activities. For example, Rule 17(d)(1) under the Act allocates to a single SRO the designated examining authority role as well as responsibility to examine common members for financial responsibility requirements imposed by the Act.

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[12] See Staff of the Division of Trading and Markets, "Staff Paper on Cross-Market Regulatory Coordination" (December 15, 2020) (available at https://www.sec.gov/tm/staff-paper-cross-market-regulatory-coordination).

[13] For example, the CMRWG has a hotline for firms to raise concerns regarding regulatory duplication.

[14] *See* https://isgportal.org/.

[15] *See, e.g.*, Cboe Regulatory Circular RC20-008 and Notice to SRO Members ISG CMRWG 2020-01 (April 8, 2020) (https://cdn.cboe.com/resources/regulation/circulars/regulatory/RC20-028-Establishment-of-the-CMRWG.pdfRC20-028 Establishment of the CMRWG (cboe.com)).

Rule 17d-2 under the Act allows for the allocation of regulatory responsibility to a single SRO for other types of common rules. Today under 17d-2 plans, SROs generally allocate certain oversight to FINRA (or other exchange SROs) that typically focuses on examination of statutory and regulatory requirements and rarely includes oversight of trading violations, especially those plans involving the options markets.[16] Again, the exchanges are best positioned to monitor and enforce trade-related violations on their markets. Consequently, the trade practice rules of every exchange to which a broker-dealer is a member apply to the member and continue to apply to it, regardless of that member's FINRA status. As noted in the Re-Proposal, the exchange SROs carry the expertise to enforce rules associated with trading on their markets and remain very much focused on how cross-market trading impacts our exchanges. Requiring nearly all remaining non-FINRA members to become FINRA members is overly broad and only adds to regulatory duplication where the member's trading activity occurs on an exchange.

Exchanges may also rely on regulatory services agreements for provision of various regulatory services, including cross-market surveillance, by another SRO. However, many SROs, including the Cboe-affiliated Exchanges, also operate comprehensive in-house regulatory programs using sophisticated surveillance technology with specialized regulatory personnel who provide surveillance, supervision, and enforcement of their rules and the federal securities laws applicable to trading activity – including cross market surveillance.[17] SROs have numerous tools at their disposal to operate effective surveillance of cross-market activity, not least of all the recent implementation of CAT.[18] Regardless of whether an SRO conducts its regulatory program in-house or through implementation of a regulatory services agreement, the contracting SRO remains responsible for oversight of its members and the service provider's provision of services. Requiring FINRA membership for the remaining non-member FINRA firms would not change this. It merely adds regulatory duplication and administrative burden to the firms and SROs with whom the firm is already a member.

Cboe fails to see a gap in the regulatory oversight of exchange members trading on an exchange. Investors are not better protected if, for example, options trading firms that do not carry customer accounts are both FINRA members *and* overseen by their member exchange(s). Given the ample regulatory oversight and transparency that is already in place for these firms, Cboe shares the concerns of Commissioners Peirce and Uyeda that the SEC should not cede primary regulatory authority and oversight over broker-dealers to FINRA.[19] Non-FINRA members of options exchanges already have appropriate and robust regulatory oversight by their member exchanges and the SEC has the necessary tools and resources to

[16] *See, e.g.*, Amended Plan for the Allocation of Regulatory Responsibilities Between the Financial Industry Regulatory Authority, Inc., Cboe Exchange, Inc., and Cboe C2 Exchange Inc., Release No. 34-83208, File No. 4-536 (May 10, 2018), 83 FR 22732 (May 16, 2018) (containing surveillance coverage for Rule 14e-4(a)(1)(ii)(D) under the Act). *See also* Amended Plan for the Allocation of Regulatory Responsibilities Between the Financial Industry Regulatory Authority, Inc., Cboe BZX Exchange, Inc., Cboe BYX Exchange, Inc., Cboe EDGA Exchange, Inc., and Cboe EDGX Exchange, Inc., Release No. 34-87788, File No. 4-705 (December 18, 2019), 84 FR 71009 (December 26, 2019) (options surveillance coverage for Rule 14e-4(a)(1)(ii)(D) under the Act; equities surveillance coverage limited to short sales, trading ahead of customer orders and research reports, best execution, and front running of block transactions).

[17] For example, Cboe BZX Exchange, Inc. and Cboe EDGX Exchange, Inc. conduct in-house cross-market surveillance, investigations, and enforcement. All Cboe-affiliated Exchanges conduct in-house market-specific surveillance, investigations, and enforcement.

[18] For example, Consolidated Options Audit Trail ("COATS") and Consolidated Equity Audit Trail ("CAT").

[19] SEC.gov | Statement of Commissioners Hester M. Peirce and Mark T. Uyeda on Proposed Amendments to Exchange Act Rule 15b9-1.

effectively oversee these market participants in partnership with the exchanges. No regulatory purpose is served by adding an additional FINRA membership for broker-dealers that do not carry customer accounts and whose activity occurs on any national securities exchange.

There are more targeted and efficient ways to address any potential transparency and oversight concerns in the off-exchange market without creating unnecessary regulatory duplication for on-exchange trading activity. For example, specifically requiring broker-dealers participating in U.S. Treasury securities (or OTC options)[20] transactions to become FINRA members and report to the TRACE system (or proposed FINRA OTC options reporting system), is more appropriate than requiring FINRA membership for nearly *all* broker-dealers.

Overly Burdensome Cost Associated with FINRA Membership Will Have Negative Impacts on Options Market

Requiring FINRA membership would result in a significant financial burden for options trading firms. FINRA membership fees range in cost based on various factors, including trading volume, and can be quite consequential to many firms.[21] As stated earlier, options market makers are critical as they stream continuous quotes to help ensure there is adequate liquidity for investors. Given that important role, options market making firm resources should be deployed for liquidity provision to the greatest extent possible. Diverting resources to cover additional registrations and extra administrative burdens harm liquidity provision and should only be required if a clear regulatory benefit is articulated.

Smaller options market makers may not have the economies of scale to adequately absorb these costs, which could lead to consolidation and decreased competition – further amplifying the negative potential impacts on the options marketplace and on investors generally. Importantly, the Re-Proposal fails to explain how investors would stand to benefit if options market making firms that do not have customers or floor brokers that do not carry customer accounts were required to join FINRA. There is no discernible gap in regulatory oversight to be filled. Investors are not better protected. Rather, substantial costs will accrue to these important market participants to have redundant regulatory oversight put in place all while potentially negatively impacting market quality for investors.

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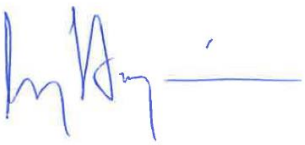
Cboe appreciates the opportunity to share its views on the Re-Proposal and welcomes the opportunity to discuss these comments further.

[20] See FINRA Regulatory Notice 22-14, *OTC Options Reporting* (June 22, 2022) (available at https://www.finra.org/sites/default/files/2022-06/Regulatory-Notice-22-14.pdf).

[21] In connection with the 2015 Proposal, options market making firms provided estimates of the significant costs associated with FINRA membership that ranged from several hundreds of thousands to millions of dollars.

Sincerely,

Angelo Evangelou
Chief Policy Officer
Cboe Global Markets, Inc.



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