

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-81342; File No. SR-GEMX-2017-31)

August 8, 2017

Self-Regulatory Organizations; Nasdaq GEMX, LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend GEMX's Schedule of Fees With Respect to the Options Regulatory Fee

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup>, and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 26, 2017, Nasdaq GEMX, LLC ("GEMX" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III, below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to revise GEMX's Schedule of Fees to: (i) more closely reflect the manner in which GEMX assesses and collects its ORF; and (ii) remove rule text related to the timing when the Exchange may increase or decrease the amount of the ORF.

The text of the proposed rule change is available on the Exchange's website at [www.ise.com](http://www.ise.com), at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

GEMX initially filed to establish its ORF in 2013.<sup>3</sup> At this time, the Exchange proposes to: (i) more closely reflect the manner in which GEMX assesses and collects its ORF; and (ii) remove rule text related to the timing when the Exchange may increase or decrease the amount of its ORF.

The Exchange supports a common approach for the assessment and collection of ORF among the various options exchanges that assess such a fee. Furthermore, the Exchange supports guidance from the Commission regarding regulatory cost structures to ensure equal knowledge and treatment among options markets assessing ORF.

Proposal 1 -Reflect the manner in which GEMX assesses and collects its ORF

Currently, GEMX assesses an ORF of \$0.0010 per contract side. This proposed rule change does not seek to amend the amount of the ORF. Currently, GEMX assesses its ORF for each customer option transaction that is either: (1) executed by a member on GEMX; or (2) cleared by a GEMX member at The Options Clearing Corporation ("OCC") in the customer range,<sup>4</sup> even if the transaction was executed by a non-member of GEMX, regardless of the

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<sup>3</sup> See Securities Exchange Act Release Nos.70200 (August 14, 2013), 74 FR 51242 (August 20, 2013) (SR-Topaz-2013-01) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Establish the Schedule of Fees).

<sup>4</sup> Members must record the appropriate account origin code on all orders at the time of entry in order. The Exchange represents that it has surveillances in place to verify that members mark orders with the correct account origin code.

exchange on which the transaction occurs.<sup>5</sup> If the OCC clearing member is a GEMX member, ORF is assessed and collected on all cleared customer contracts (after adjustment for CMTA<sup>6</sup>); and (2) if the OCC clearing member is not a GEMX member, ORF is collected only on the cleared customer contracts executed at GEMX, taking into account any CMTA instructions which may result in collecting the ORF from a non-member.

By way of example, if Broker A, a GEMX member, routes a customer order to CBOE and the transaction executes on CBOE and clears in Broker A's OCC Clearing account, ORF will be collected by GEMX from Broker A's clearing account at OCC via direct debit. While this transaction was executed on a market other than GEMX, it was cleared by a GEMX member in the member's OCC clearing account in the customer range, therefore there is a regulatory nexus between GEMX and the transaction. If Broker A was not a GEMX member, then no ORF should be assessed and collected because there is no nexus; the transaction did not execute on GEMX nor was it cleared by a GEMX member.

In the case where a member both executes a transaction and clears the transaction, the ORF is assessed to and collected from the member only. In the case where a member executes a transaction and a different member clears the transaction, the ORF is assessed to and collected from the member who clears the transaction and not the member who executes the transaction. In the case where a non-member executes a transaction at an away market and a member clears the transaction, the ORF is assessed to and collected from the member who clears the transaction. In the case where a member executes a transaction on GEMX and a non-member clears the transaction, the ORF is assessed to the member that executed the transaction and

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<sup>5</sup> The Exchange uses reports from OCC when assessing and collecting the ORF.

<sup>6</sup> CMTA or Clearing Member Trade Assignment is a form of "give-up" whereby the position will be assigned to a specific clearing firm at OCC.

collected from the non-member who cleared the transaction. In the case where a member executes a transaction at 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. Further, the data does not allow the Exchange to identify the member executing the trade at an away market.

#### ORF Revenue and Monitoring of ORF

The Exchange monitors the amount of revenue collected from the ORF to ensure that it, in combination with other regulatory fees and fines, does not exceed regulatory costs. In determining whether an expense is considered a regulatory cost, the Exchange reviews all costs and makes determinations if there is a nexus between the expense and a regulatory function. The Exchange notes that fines collected by the Exchange in connection with a disciplinary manner offset ORF.

The ORF is designed to recover a material portion of the costs to the Exchange of the supervision and regulation of its members, including performing routine surveillances, investigations, examinations, financial monitoring, and policy, rulemaking, interpretive, and enforcement activities.

The Exchange believes that revenue generated from the ORF, when combined with all of the Exchange's other regulatory fees, will cover a material portion, but not all, of the Exchange's regulatory costs. The Exchange will continue to monitor the amount of revenue collected from the ORF to ensure that it, in combination with its other regulatory fees and fines, does not exceed regulatory costs. If the Exchange determines regulatory revenues exceed regulatory costs, the Exchange will adjust the ORF by submitting a fee change filing to the Commission.

Finally, the Exchange notes that it is amending GEMX's Schedule of Fees to remove certain rule text and include new rule text to make clear the manner in which ORF is assessed and collected on GEMX.

#### Proposal 2 – Semi-Annual Changes to ORF

The Exchange's current ORF rule text provides that, "The Exchange may only increase or decrease the Options Regulatory Fee semi-annually, and any such fee change will be effective on the first business day of February or August." 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 for the regulatory revenue that it receives and the costs that it incurs. While the Exchange is eliminating the requirement to adjust only semi-annually, it will continue to submit a rule proposal with the Commission for each modification to the ORF and notify participants via an Options Trader Alert of any proposed change in the amount of the fee at least thirty (30) calendar days prior to the effective date. The Exchange believes that the prior notification to market participants will provide guidance on the timing of any changes to the ORF and ensure market participants are prepared to configure their systems to properly account for the ORF.

The Exchange also notes it now issues Options Trader Alerts instead of circulars to provide notification to members. The Exchange is amending the rule text to reflect this change.

#### 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>7</sup> in

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<sup>7</sup> 15 U.S.C. 78f(b).

general, and furthers the objectives of Sections 6(b)(4) and 6(b)(5) of the Act<sup>8</sup> in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using its facility and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Exchange believes the proposed clarifications in the Fee Schedule to the ORF further the objectives of Section 6(b)(4) of the Act and are equitable and reasonable since they expressly describe the Exchange's existing practices regarding the manner in which the Exchange assesses and collects its ORF.

Proposal 1 - Reflect the manner in which GEMX assesses and collects its ORF

The Exchange believes it is reasonable and appropriate for the Exchange to charge the ORF for options transactions regardless of the exchange on which the transactions occur. 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. Many of the Exchange's market surveillance programs require the Exchange to look at and evaluate activity across all options markets, such as surveillance for position limit violations, manipulation, front-running and contrary exercise advice violations/expiring exercise declarations. The Exchange, because it lacks access to information on the identity of the entering firm for executions that occur on away markets, believes it is appropriate to assess the ORF on its member's clearing activity, based on information the Exchange receives from OCC, including for away market activity. Among other reasons, doing

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<sup>8</sup> 15 U.S.C. 78f(b)(4) and (5).

so better and more accurately captures activity that occurs away from the Exchange over which the Exchange has a degree of regulatory responsibility. 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”)<sup>9</sup> system in order to surveil a member’s activities across markets.<sup>10</sup>

The Exchange believes that assessing the ORF to each Exchange member for options transactions cleared by OCC in the customer range where the execution occurs on another exchange and is cleared by a GEMX member is an equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities. The ORF is collected by OCC on behalf of GEMX from Exchange clearing members for all customer transactions they clear or from non-members for all customer transactions they clear that were executed on GEMX. 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.

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<sup>9</sup> COATS effectively enhances intermarket options surveillance by enabling the options exchanges to reconstruct the market promptly to effectively surveil certain rules.

<sup>10</sup> In addition to its own surveillance programs, the Exchange works with other SROs and exchanges on intermarket surveillance related issues. Through its participation in the Intermarket Surveillance Group (“ISG”), the Exchange shares information and coordinates inquiries and investigations with other exchanges designed to address potential intermarket manipulation and trading abuses. The Exchange’s participation in ISG helps it to satisfy the requirement that it has coordinated surveillance with markets on which security futures are traded and markets on which any security underlying security futures are traded to detect manipulation and insider trading. See Section 6(h)(3)(I) of the Act. ISG is an industry organization formed in 1983 to coordinate intermarket surveillance among the SROs by co-operatively sharing regulatory information pursuant to a written agreement between the parties. The goal of the ISG's information sharing is to coordinate regulatory efforts to address potential intermarket trading abuses and manipulations.

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 proposes assessing higher fees to those members that will require more Exchange regulatory services based on the amount of customer options business they conduct. Additionally, the dues and fees paid by members go into the general funds of the Exchange, a portion of which is used to help pay the costs of regulation. The Exchange has in place a regulatory structure to surveil, conduct examinations and monitor the marketplace for violations of Exchange Rules. The ORF assists the Exchange to fund the cost of this regulation of the marketplace.

#### Proposal 2 - Semi-Annual Changes to ORF

The Exchange believes that the proposed rule change to remove the limit to amend the ORF only semi-annually, with advance notice, is reasonable because the Exchange will continue to provide market participants with thirty (30) days advance notice of amending the amount of the ORF. Also, the Exchange is required to monitor the amount of revenue collected from the ORF to ensure that it, in combination with its other regulatory fees and fines, do not exceed regulatory costs. Therefore, the Exchange believes it is reasonable to remove the semi-annual limit to amend its ORF in order to permit the Exchange to make amendments to its ORF as necessary to comply with the Exchange's obligations. This proposed change would conform this



rule with that of NASDAQ PHLX LLC (“Phlx”), The NASDAQ Options Market LLC (“NOM”) and NASDAQ BX, Inc. (“BX”).<sup>11</sup>

The Exchange believes that the proposed rule change to remove the limit to amend the ORF only semi-annually, with advance notice, is equitable and not unfairly discriminatory because it will apply in the same manner to all members that are subject to the ORF. The Exchange has in place a regulatory structure to surveil for, conduct examinations and monitor the marketplace for violations of Exchange Rules. The ORF assists the Exchange to fund the cost of this regulation of the marketplace.

**B. Self-Regulatory Organization's Statement on Burden on Competition**

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The ORF is not intended to have any impact on competition. Rather, it is designed to enable the Exchange to recover a material portion of the Exchange’s cost related to its regulatory activities. The Exchange is obligated to ensure that the amount of regulatory revenue collected from the ORF, in combination with its other regulatory fees and fines, does not exceed regulatory costs.

**C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

No written comments were either solicited or received.

**III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act.<sup>12</sup> At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such

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<sup>11</sup> See Phlx’s Pricing Schedule and NOM and BX Rules at Chapter XV, Sections 5.

<sup>12</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

action is: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR- GEMX-2017-31 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File No. SR- GEMX-2017-31. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be

available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR- GEMX-2017-31, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).