

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-94258; File No. SR-PEARL-2022-03)

February 15, 2022

Self-Regulatory Organizations; MIAX PEARL LLC; Notice of Filing of a Proposed Rule Change to Amend the MIAX PEARL Options Fee Schedule to Adopt a Tiered-Pricing Structure for Certain Connectivity Fees; Suspension of and Order Instituting Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change

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 February 1, 2022, MIAX PEARL, LLC (“MIAX Pearl” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) a proposed rule change as described in Items I and II 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 and is, pursuant to Section 19(b)(3)(C) of the Act, hereby: (i) temporarily suspending the rule change; and (ii) instituting proceedings to determine whether to approve or disapprove the proposed rule change.

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

The Exchange is filing a proposal to amend the MIAX Pearl Options Fee Schedule (the “Fee Schedule”) to amend certain connectivity fees.

The text of the proposed rule change is available on the Exchange’s website at <http://www.miaxoptions.com/rule-filings>, at MIAX’s principal office, and at the Commission’s Public Reference Room.

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

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

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 proposed rule change. The text of these statements may be examined at the places specified in Item IV [sic] 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 Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend the Fee Schedule to adopt a tiered-pricing structure for the 10 gigabit (“Gb”) ultra-low latency (“ULL”) fiber connection available to Members<sup>3</sup> and non-Members. The Exchange initially filed this proposal on July 30, 2021, with the proposed fee changes effective beginning August 1, 2021 (“First Proposed Rule Change”).<sup>4</sup> The First Proposed Rule Change was published for comment in the Federal Register on August 17, 2021.<sup>5</sup> The Commission received one comment letter on the First Proposed Rule Change.<sup>6</sup> The Exchange withdrew the First Proposed Rule Change on September 24, 2021 and re-submitted the proposal on September 24, 2021, with the proposed fee changes being immediately effective

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<sup>3</sup> The term “Member” means an individual or organization that is registered with the Exchange pursuant to Chapter II of these Rules for purposes of trading on the Exchange as an “Electronic Exchange Member” or “Market Maker.” Members are deemed “members” under the Exchange Act. See Exchange Rule 100.

<sup>4</sup> See Securities Exchange Act Release No. 92644 (August 11, 2021), 86 FR 46055 (August 17, 2021) (SR-PEARL-2021-36).

<sup>5</sup> Id.

<sup>6</sup> See Letter from Richard J. McDonald, Susquehanna International Group, LLC (“SIG”), to Vanessa Countryman, Secretary, Commission, dated September 7, 2021 (“SIG Letter 1”).

(“Second Proposed Rule Change”).<sup>7</sup> The Second Proposed Rule Change was published for comment in the Federal Register on October 4, 2021.<sup>8</sup> The Second Proposed Rule Change provided additional justification for the proposed fee changes and addressed certain points raised in the single comment letter that was submitted on the First Proposed Rule Change. The Commission received four comment letters from three separate commenters on the Second Proposed Rule Change.<sup>9</sup> The Commission suspended the Second Proposed Rule Change on November 22, 2021.<sup>10</sup> The Exchange withdrew the Second Proposed Rule Change on December 1, 2021 and submitted a revised proposal for immediate effectiveness (“Third Proposed Rule Change”).<sup>11</sup> The Third Proposed Rule Change meaningfully attempted to address issues or questions that have been raised by providing additional justification and explanation for the

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<sup>7</sup> See Securities Exchange Act Release No. 93162 (September 28, 2021), 86 FR 54739 (October 4, 2021) (SR-PEARL-2021-45).

<sup>8</sup> Id.

<sup>9</sup> See letters from Richard J. McDonald, SIG, to Vanessa Countryman, Secretary, Commission, dated October 1, 2021 (“SIG Letter 2”) and October 26, 2021 (“SIG Letter 3”). See also letter from Tyler Gellasch, Executive Director, Healthy Markets Association (“HMA”), to Hon. Gary Gensler, Chair, Commission, dated October 29, 2021 (commenting on SR-CboeEDGA-2021-017, SR-CboeBYX-2021-020, SR-Cboe-BZX-2021-047, SR-CboeEDGX-2021-030, SR-MIAX-2021-41, SR-PEARL-2021-45, and SR-EMERALD-2021-29 and stating that “MIAX has repeatedly filed to change its connectivity fees in a way that will materially lower costs for many users, while increasing the costs for some of its heaviest of users. These filings have been withdrawn and repeatedly refiled. Each time, however, the filings contain significantly greater information about who is impacted and how than other filings that have been permitted to take effect without suspension”) (emphasis added) (“HMA Letter”); and Ellen Green, Managing Director, Equity and Options Market Structure, Securities Industry and Financial Markets Association (“SIFMA”), to Vanessa Countryman, Secretary, Commission, dated November 26, 2021 (“SIFMA Letter”).

<sup>10</sup> See Securities Exchange Act Release No. 93639 (November 22, 2021), 86 FR 67758 (November 29, 2021).

<sup>11</sup> See Securities Exchange Act Release No. 93774 (December 14, 2021), 86 FR 71952 (December 20, 2021) (SR-PEARL-2021-57).

proposed fee changes and directly respond to the points raised in SIG Letters 1, 2, and 3, as well as the SIFMA Letter submitted on the First and Second Proposed Rule Changes,<sup>12</sup> and feedback provided by Commission Staff during a telephone conversation on November 18, 2021 relating to the Second Proposed Rule Change. The Third Proposed Rule Change was published for comment in the Federal Register on December 20, 2021.<sup>13</sup> The Exchange receive no comment letters on the Third Proposed Rule Change. The Commission suspended the Third Proposed Rule Change on January 27, 2022.<sup>14</sup> The Exchange withdrew the Third Proposed Rule Change on February 1, 2022 and now submits this proposal for immediate effectiveness (“Fourth Proposed Rule Change”). This Fourth Proposed Rule Change provides additional justification and explanation for the proposed fee changes.

#### 10Gb ULL Tiered-Pricing Structure

The Exchange proposes to amend Sections 5)a)-b) of the Fee Schedule to provide for a tiered-pricing structure for 10Gb ULL connections for Members and non-Members. Prior to the First Proposed Rule Change, the Exchange assessed Members and non-Members a flat monthly fee of \$10,000 per 10Gb ULL connection for access to the Exchange’s primary and secondary facilities.

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<sup>12</sup> The Exchange notes that while the HMA Letter applauds the level of disclosure the Exchange included in the First and Second Proposed Rule Changes, the HMA Letter does not raise specific issues with the First or Second Proposed Rule Changes. Rather, it references the Exchange’s proposals by way of comparison to show the varying levels of transparency in exchange fees filings and recommends changes to the Commission’s review process of exchange fee filings generally. Therefore, the Exchange does not feel it is necessary to address the issues raised in the HMA Letter.

<sup>13</sup> See supra note 11.

<sup>14</sup> See Securities Exchange Act Release No. 94088 (January 27, 2022) (Suspension of and Order Instituting Proceedings to Determine Whether to Approve or Disapprove Proposed Rule Changes to Amend the Fee Schedules to Adopt a Tiered-Pricing Structure for Certain Connectivity Fees).

The Exchange now proposes to move from a flat monthly fee per connection to a tiered-pricing structure under which the monthly fee would vary depending on the number of 10Gb ULL connections each Member or non-Member elects to purchase per exchange. Specifically, the Exchange proposes to decrease the fee for the first and second 10Gb ULL connections for each Member and non-Member from the current flat monthly fee of \$10,000 to \$9,000 per connection. To encourage more efficient connectivity usage, the Exchange proposes to increase the per connection fee for Members and non-Members that purchase more than two 10Gb ULL connections. In particular, (i) the third and fourth 10Gb ULL connections for each Member or non-Member will increase from the current flat monthly fee of \$10,000 to \$11,000 per connection; and (ii) for the fifth 10Gb ULL connection, and each 10Gb ULL connection purchased by Members and non-Members thereafter, the fee will increase from the flat monthly fee of \$10,000 to \$13,000 per connection. The proposed 10Gb ULL tiered-pricing structure and fees are collectively referred to herein as the “Proposed Access Fees.”

The Exchange believes the other exchanges’ connectivity fees are a useful example of alternative approaches to providing and charging for connectivity and provides the below table for comparison purposes only to show how its proposed fees compare to fees currently charged by other options exchanges for similar connectivity. As shown by the below table, the Exchange’s proposed highest tier is still less than fees charged for similar connectivity provided by other options exchanges.

Exchange	Type of Port	Monthly Fee
MIAX Pearl Options (as proposed)	10Gb ULL	1-2 connection. \$9,000.00 3-4 connections. \$11,000.00 5 or more. \$13,000.00
The NASDAQ Stock Market LLC (“NASDAQ”) <sup>15</sup>	10Gb Ultra fiber	\$15,000.00
Nasdaq ISE LLC (“ISE”) <sup>16</sup>	10Gb Ultra fiber	\$15,000.00
Nasdaq PHLX LLC (“PHLX”) <sup>17</sup>	10Gb Ultra Fiber	\$15,000.00
NYSE American LLC (“Amex”) <sup>18</sup>	10Gb LX LCN	\$22,000.00

The Exchange will continue to assess monthly Member and non-Member network connectivity fees for connectivity to the primary and secondary facilities in any month the Member or non-Member is credentialed to use any of the Exchange APIs or market data feeds in the production environment. The Exchange proposes to pro-rate the fees when a Member or non-Member makes a change to the connectivity (by adding or deleting connections) with such pro-rated fees based on the number of trading days that the Member or non-Member has been credentialed to utilize any of the Exchange APIs or market data feeds in the production environment through such connection, divided by the total number of trading days in such month

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<sup>15</sup> See NASDAQ Rules, General 8: Connectivity, Section 1. Co-Location Services.  
<sup>16</sup> See PHLX Rules, General 8: Connectivity.  
<sup>17</sup> See ISE Rules, General 8: Connectivity.  
<sup>18</sup> See NYSE American Options Fee Schedule, Section IV.

multiplied by the applicable monthly rate. The Exchange will continue to assess monthly Member and non-Member network connectivity fees for connectivity to the disaster recovery facility in each month during which the Member or non-Member has established connectivity with the disaster recovery facility.

The Exchange's MIAX Express Network Interconnect ("MENI") can be configured to provide Members and non-Members of the Exchange network connectivity to the trading platforms, market data systems, test systems, and disaster recovery facilities of both the Exchange and its affiliate, Miami International Securities Exchange, LLC ("MIAX"), via a single, shared connection. Members and non-Members utilizing the MENI to connect to the trading platforms, market data systems, test systems, and disaster recovery facilities of the Exchange and MIAX via a single, shared connection will continue to only be assessed one monthly connectivity fee per connection, regardless of the trading platforms, market data systems, test systems, and disaster recovery facilities accessed via such connection.

## 2. Statutory Basis

The Exchange believes that the Proposed Access Fees are consistent with Section 6(b) of the Act<sup>19</sup> in general, and furthers the objectives of Section 6(b)(4) of the Act<sup>20</sup> in particular, in that they provide for the equitable allocation of reasonable dues, fees and other charges among Members and other persons using any facility or system which the Exchange operates or controls. The Exchange also believes the Proposed Access Fees further the objectives of Section 6(b)(5) of the Act<sup>21</sup> in that they are designed to promote just and equitable principles of

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<sup>19</sup> 15 U.S.C. 78f(b).

<sup>20</sup> 15 U.S.C. 78f(b)(4).

<sup>21</sup> 15 U.S.C. 78f(b)(5).

trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general protect investors and the public interest and are not designed to permit unfair discrimination between customers, issuers, brokers and dealers.

On March 29, 2019, the Commission issued an Order disapproving a proposed fee change by the BOX Market LLC Options Facility to establish connectivity fees for its BOX Network (the “BOX Order”).<sup>22</sup> On May 21, 2019, the Commission Staff issued guidance “to assist the national securities exchanges and FINRA ... in preparing Fee Filings that meet their burden to demonstrate that proposed fees are consistent with the requirements of the Securities Exchange Act.”<sup>23</sup> Based on both the BOX Order and the Guidance, the Exchange believes that the Proposed Access Fees are consistent with the Act because they (i) are reasonable, equitably allocated, not unfairly discriminatory, and not an undue burden on competition; (ii) comply with the BOX Order and the Guidance; (iii) are supported by evidence (including comprehensive revenue and cost data and analysis) that they are fair and reasonable because they will not result in excessive pricing or supra-competitive profit; and (iv) utilize a cost-based justification framework that is substantially similar to a framework previously used by the Exchange, and its affiliates MIAX Emerald, LLC (“MIAX Emerald”) and MIAX, to amend other non-transaction fees.<sup>24</sup>

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<sup>22</sup> See Securities Exchange Act Release No. 85459 (March 29, 2019), 84 FR 13363 (April 4, 2019) (SR-BOX-2018-24, SR-BOX-2018-37, and SR-BOX-2019-04) (Order Disapproving Proposed Rule Changes to Amend the Fee Schedule on the BOX Market LLC Options Facility to Establish BOX Connectivity Fees for Participants and Non-Participants Who Connect to the BOX Network).

<sup>23</sup> See Staff Guidance on SRO Rule Filings Relating to Fees (May 21, 2019), at <https://www.sec.gov/tm/staff-guidance-sro-rule-filings-fees> (the “Guidance”).

<sup>24</sup> See Securities Exchange Act Release Nos. 91460 (April 2, 2021), 86 FR 18349 (SR-EMERALD-2021-11) (proposal to adopt port fees, increase connectivity fees, and increase additional limited service ports); 91033 (February 1, 2021), 86 FR 8455 (February 5, 2021) (SR-EMERALD-2021-03) (proposal to adopt trading permit fees);



### The Proposed Access Fees will not Result in a Supra-Competitive Profit

The Exchange believes that exchanges, in setting fees of all types, should meet very high standards of transparency to demonstrate why each new fee or fee amendment meets the requirements of the Act that fees be reasonable, equitably allocated, not unfairly discriminatory, and not create an undue burden on competition among market participants. The Exchange believes this high standard is especially important when an exchange imposes various access fees for market participants to access an exchange's marketplace. The Exchange deems connectivity to be access fees. It records these fees as part of its "Access Fees" revenue in its financial statements.

In the Guidance, the Commission Staff stated that, "[a]s an initial step in assessing the reasonableness of a fee, staff considers whether the fee is constrained by significant competitive forces."<sup>25</sup> The Guidance further states that, "... even where an SRO cannot demonstrate, or does not assert, that significant competitive forces constrain the fee at issue, a cost-based discussion may be an alternative basis upon which to show consistency with the Exchange Act."<sup>26</sup> In its Guidance, the Commission Staff further states that, "[i]f an SRO seeks to support its claims that a proposed fee is fair and reasonable because it will permit recovery of the SRO's costs, or will not result in excessive pricing or supracompetitive profit, specific information, including quantitative information, should be provided to support that argument."<sup>27</sup> The Exchange does not assert that the Proposed Access Fees are constrained by competitive forces. Rather, the

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90980 (January 25, 2021), 86 FR 7602 (January 29, 2021) (SR-MIAX-2021-02) (proposal to increase connectivity fees).

<sup>25</sup> See Guidance, supra note 23.

<sup>26</sup> Id.

<sup>27</sup> Id.

Exchange asserts that the Proposed Access Fees are reasonable because they will permit recovery of the Exchange’s costs in providing access services to supply 10Gb ULL connectivity and will not result in the Exchange generating a supra-competitive profit.

The Guidance defines “supra-competitive profit” as “profits that exceed the profits that can be obtained in a competitive market.”<sup>28</sup> The Commission Staff further states in the Guidance that “the SRO should provide an analysis of the SRO’s baseline revenues, costs, and profitability (before the proposed fee change) and the SRO’s expected revenues, costs, and profitability (following the proposed fee change) for the product or service in question.”<sup>29</sup> The Exchange provides this analysis below.

Based on this analysis, the Exchange believes the Proposed Access Fees are reasonable and do not result in a “supra-competitive”<sup>30</sup> profit. The Exchange believes that it is important to demonstrate that the Proposed Access Fees are based on its costs and reasonable business needs. The Exchange believes the Proposed Access Fees will allow the Exchange to offset expenses the Exchange has and will incur, and that the Exchange provides sufficient transparency (described below) into the costs and revenue underlying the Proposed Access Fees. Accordingly, the Exchange provides an analysis of its revenues, costs, and profitability associated with the Proposed Access Fees. This analysis includes information regarding its methodology for determining the costs and revenues associated with the Proposed Access Fees. As a result of this analysis, the Exchange believes the Proposed Access Fees are fair and reasonable as a form of

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28 Id.

29 Id.

30 Id.

cost recovery plus present the possibility of a reasonable return for the Exchange's aggregate costs of offering connectivity to the Exchange and MIAX.

The Proposed Access Fees are based on a cost-plus model. In determining the appropriate fees to charge, the Exchange considered its costs and MIAX's costs to provide connectivity, using what it believes to be a conservative methodology (i.e., that strictly considers only those costs that are most clearly directly related to the provision and maintenance of 10Gb ULL connectivity) to estimate such costs,<sup>31</sup> as well as the relative costs of providing and maintaining 10Gb ULL connectivity, and set fees that are designed to cover its costs with a limited return in excess of such costs. However, as discussed more fully below, such fees may also result in the Exchange recouping less than all of its costs of providing and maintaining 10Gb ULL connectivity because of the uncertainty of forecasting subscriber decision making with respect to firms' connectivity needs and the likely potential for increased costs to procure the third-party services described below.

To determine the Exchange's costs to provide access services associated with the Proposed Access Fees, the Exchange conducted an extensive cost review in which the Exchange analyzed nearly every expense item in the Exchange's general expense ledger to determine whether each such expense relates to the Proposed Access Fees, and, if such expense did so relate, what portion (or percentage) of such expense actually supports access services associated with the Proposed Access Fees.

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<sup>31</sup> For example, the Exchange only included the costs associated with providing and supporting connectivity and excluded from its connectivity cost calculations any cost not directly associated with providing and maintaining such connectivity. Thus, the Exchange notes that this methodology underestimates the total costs of providing and maintaining connectivity.

The Exchange also provides detailed information regarding the Exchange's cost allocation methodology – namely, information that explains the Exchange's rationale for determining that it was reasonable to allocate certain expenses described in this filing towards the cost to the Exchange to provide the access services associated with the Proposed Access Fees. The Exchange conducted a thorough internal analysis to determine the portion (or percentage) of each expense to allocate to the support of access services associated with the Proposed Access Fees. This analysis<sup>32</sup> included discussions with each Exchange department head to determine the expenses that support access services associated with the Proposed Access Fees. This included numerous meetings between the Exchange's Chief Information Officer, Chief Financial Officer, Head of Strategic Planning and Operations, Chief Technology Officer, various members of the Legal Department, and other group leaders. The Exchange reviewed each individual expense to determine if such expense was related to the Proposed Access Fees. Once the expenses were identified, the Exchange department heads, with the assistance of our internal finance department, reviewed such expenses holistically on an Exchange-wide level to determine what portion of that expense supports providing access services for the Proposed Access Fees. The sum of all such portions of expenses represents the total cost to the Exchange to provide access services associated with the Proposed Access Fees. For the avoidance of doubt, no expense amount was allocated twice.

The internal cost analysis conducted by the Exchange is a proprietary process that is designed to make a fair and reasonable assessment of costs and resources allocated to support the provision of access services associated with the Proposed Access Fees. The Exchange

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<sup>32</sup> A description of the Exchange's methodology for determining the portion (or percentage) of each expense to allocate to the Proposed Access Fees is being provide in response to comments from SIG and SIFMA. See SIG Letter 3 and SIFMA Letter, supra note 9.

acknowledges that this assessment can only capture a moment in time and that costs and resource allocations may change. That is why the Exchange has historically, and on an ongoing basis, periodically revisits its costs and resource allocations to ensure it is appropriately allocating resources to properly provide services to the Exchange's constituents. Any requirement that an exchange should conduct a periodic re-evaluation on a set timeline of its cost justification and amend its fees accordingly should be established by the Commission holistically, applied to all exchanges and not just through pending fee proposals, such as this filing. In order to be fairly applied, such a mandate should be applied to existing access fees as well.

In accordance with the Guidance, the Exchange has provided sufficient detail to support a finding that the proposed fees are consistent with the Exchange Act. The proposal includes a detailed description of the Exchange's costs and how the Exchange determined to allocate those costs related to the proposed fees. In fact, the detail and analysis provided in this proposed rule change far exceed the level of disclosure provided in other exchange fee filings that have not been suspended by the Commission during its 60-day suspension period. A finding that this proposed rule change is inconsistent with the Exchange Act would run contrary to the Commission Staff's treatment of other recent exchange fee proposals that have not been suspended and remain in effect today.<sup>33</sup> For example, a proposed fee filing that closely

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<sup>33</sup> See, e.g., Securities Exchange Act Release Nos. 91339 (March 17, 2021), 86 FR 15524 (March 23, 2021) (SR-CboeBZX-2021-020) (increasing fees for a market data product while not providing a cost based justification for the increase); 93293 (October 21, 2021), 86 FR 57716 (October 18, 2021) (SR-PHLX-2021-058) (increasing fees for historical market data while not providing a cost based justification for the increase); 92970 (September 14, 2021), 86 FR 52261 (September 20, 2021) (SR-CboeBZX-2021-047) (adopting fees for a market data related product while not providing a cost based justification for the fees); and 89826 (September 10, 2021), 85 FR 57900 (September 16, 2021) (SR-CBOE-2020-086) (increasing connectivity fees without including a cost based justification).

resembles the Exchange’s current filing was submitted in 2020 by the Cboe Exchange, Inc. (“Cboe”) and increased fees for Cboe’s 10Gb connections.<sup>34</sup> This filing was submitted on September 2, 2020, nearly 15 months after the Staff’s Guidance was issued. In that filing, the Cboe stated that the “proposed changes were not designed with the objective to generate an overall increase in access fee revenue.”<sup>35</sup> This filing provided no cost based data to support its assertion that the proposal was intended to be revenue neutral. Among other things, Cboe did not provide a description of the costs underlying its provision of 10Gb connections to show that this particular fee did not generate a supra-competitive profit or describe how any potential profit may be offset by increased costs associated with another fee included in its proposal. This filing, nonetheless, was not suspended by the Commission and remains in effect today.

The Exchange believes exchanges, like all businesses, should be provided flexibility when allocating costs and resources they deem necessary to operate their business, including providing market data and access services. The Exchange notes that costs and resource allocations may vary from business to business and, likewise, costs and resource allocations may differ from exchange to exchange when it comes to providing market data and access services. It is a business decision that must be evaluated by each exchange as to how to allocate internal resources and what costs to incur internally or via third parties that it may deem necessary to support its business and its provision of market data and access services to market participants.

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<sup>34</sup> See Securities Exchange Act Release No. 89826 (September 10, 2020), 85 FR 57900 (September 16, 2020) (SR-CBOE-2020-086) (increasing connectivity fees without including a cost based justification).

<sup>35</sup> See *id.* at 57909.

An exchange's costs may also vary based on fees charged by third parties and periodic increases to those fees that may be outside of the control of an exchange.<sup>36</sup>

To determine the Exchange's projected revenue associated with the Proposed Access Fees, the Exchange analyzed the number of Members and non-Members currently utilizing the 10Gb ULL fiber connection and used a recent monthly billing cycle representative of 2021 monthly revenue. The Exchange also provided its baseline by analyzing July 2021, the monthly billing cycle prior to the Proposed Access Fees going into effect, and compared it to its expenses for that month.<sup>37</sup> As discussed below, the Exchange does not believe it is appropriate to factor into its analysis future revenue growth or decline into its projections for purposes of these calculations, given the uncertainty of such projections due to the continually changing access needs of market participants and potential increase in internal and third party expenses. The Exchange is presenting its revenue and expense associated with the Proposed Access Fees in this filing in a manner that is consistent with how the Exchange presents its revenue and expense in its Audited Unconsolidated Financial Statements. The Exchange's most recent Audited Unconsolidated Financial Statement is for 2020. However, since the revenue and expense associated with the Proposed Access Fees were not in place in 2020 or for the first seven months of 2021, the Exchange believes its 2020 Audited Unconsolidated Financial Statement is not representative of its current total annualized revenue and costs associated with the Proposed Access Fees. Accordingly, the Exchange believes it is more appropriate to analyze the Proposed Access Fees utilizing its 2021 revenue and costs, as described herein, which utilize the same presentation methodology as set forth in the Exchange's previously-issued Audited

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<sup>36</sup> See supra note 32.

<sup>37</sup> Id.

Unconsolidated Financial Statements. Based on this analysis, the Exchange believes that the Proposed Access Fees are reasonable because they will allow the Exchange to recover its costs associated with providing access services related to the Proposed Access Fees and not result in excessive pricing or supra-competitive profit.

As outlined in more detail below, the Exchange and MIAX project that the final annualized expense for 2021 to provide all network connectivity services (that is, the shared network connectivity of all connectivity alternatives of the Exchange and MIAX, but excluding MIAX Emerald) to be approximately \$15.9 million per annum or an average of \$1,325,000 per month. The Exchange implemented the Proposed Access Fees on August 1, 2021 in the First Proposed Rule Change. For July 2021, prior to the Proposed Access Fees, the Exchange and MIAX Members and non-Members purchased a total of 156 10Gb ULL connections for which the Exchange and MIAX charged a total of approximately \$1,547,620 (this includes MIAX Pearl Options and MIAX Members and non-Members dropping or adding connections mid-month, resulting a pro-rated charge at times). This resulted in a profit of \$222,620 for that month (a profit margin of 14.4%). For the month of October 2021, which includes the tiered rates for 10Gb ULL connectivity for the Proposed Access Fees, MIAX Pearl Options and MIAX Exchange Members and non-Members purchased a total of 154 10Gb ULL connections for which the Exchange and MIAX charged a total of approximately \$1,684,000 for that month (also including pro-rated connection charges). This resulted in a profit of \$359,000 for that month for a profit margin of 21.3% (a modest 6.9% profit margin increase from July 2021 to October 2021 from 14.4% to 21.3%). The Exchange believes that the Proposed Access Fees are reasonable because they only generate an additional 6.9% of profit margin per-month



(reflecting a 21.3% profit margin).<sup>38</sup> The Exchange cautions that this profit margin is likely to fluctuate from month to month based on the uncertainty of predicting how many connections may be purchased from month to month as Members and non-Members are able to add and drop connections at any time based on their own business decisions. This profit margin may also decrease due to the significant inflationary pressure on capital items that the Exchange needs to purchase to maintain the Exchange’s technology and systems.<sup>39</sup>

The Exchange and MIAX have been subject to price increases upwards of 30% during the past year on network equipment due to supply chain shortages. This, in turn, results in higher overall costs for ongoing system maintenance, but also to purchase the items necessary to ensure ongoing system resiliency, performance, and determinism. These costs are expected to continue to go up as the U.S. economy continues to struggle with supply chain and inflation related issues.

As mentioned above, the Exchange and MIAX project that the annualized expense for 2021 to provide network connectivity services (all connectivity alternatives) to be approximately \$15.9 million per annum or an average of \$1,325,000 per month and that these costs are expected to increase not only due to anticipated significant inflationary pressure, but

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<sup>38</sup> The Exchange notes that this profit margin differs from the First and Second Proposed Rule Changes because the Exchange now has the benefit of using a more recent billing cycle under the Proposed Access Fees (October 2021) and comparing it to a baseline month (July 2021) from before the Proposed Access Fees were in effect.

<sup>39</sup> See “Supply chain chaos is already hitting global growth. And it’s about to get worse”, by Holly Ellyatt, CNBC, available at <https://www.cnbc.com/2021/10/18/supply-chain-chaos-is-hitting-global-growth-and-could-get-worse.html> (October 18, 2021); and “There will be things that people can’t get, at Christmas, White House warns” by Jarrett Renshaw and Trevor Hunnicutt, Reuters, available at <https://www.reuters.com/world/us/americans-may-not-get-some-christmas-treats-white-house-officials-warn-2021-10-12/> (October 12, 2021).

also periodic fee increases by third parties.<sup>40</sup> The Exchange notes that there are material costs associated with providing the infrastructure and headcount to fully-support access to the Exchange. The Exchange incurs technology expense related to establishing and maintaining Information Security services, enhanced network monitoring and customer reporting, as well as Regulation SCI mandated processes, associated with its network technology. While some of the expense is fixed, much of the expense is not fixed, and thus increases the cost to the Exchange to provide access services associated with the Proposed Access Fees. For example, new Members to the Exchange may require the purchase of additional hardware to support those Members as well as enhanced monitoring and reporting of customer performance that the Exchange and its affiliates provide. Further, as the total number Members increases, the Exchange and its affiliates may need to increase their data center footprint and consume more power, resulting in increased costs charged by their third-party data center provider. Accordingly, the cost to the Exchange and its affiliates to provide access to its Members is not fixed. The Exchange believes the Proposed Access Fees are a reasonable attempt to offset a portion of the costs to the Exchange associated with providing access to its network infrastructure.

The Exchange only has four primary sources of revenue and cost recovery mechanisms to fund all of its operations: transaction fees, access fees (which includes the Proposed Access Fees), regulatory fees, and market data fees. Accordingly, the Exchange must cover all of its

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<sup>40</sup> For example, on October 20, 2021, ICE Data Services announced a 3.5% price increase effective January 1, 2022 for most services. The price increase by ICE Data Services includes their SFTI network, which is relied on by a majority of market participants, including the Exchange. See email from ICE Data Services to the Exchange, dated October 20, 2021. The Exchange further notes that on October 22, 2019, the Exchange was notified by ICE Data Services that it was raising its fees charged to the Exchange by approximately 11% for the SFTI network.

expenses from these four primary sources of revenue and cost recovery mechanisms. Until recently, the Exchange has operated at a cumulative net annual loss since it launched operations in 2017.<sup>41</sup> This is a result of providing a low cost alternative to attract order flow and encourage market participants to experience the high determinism and resiliency of the Exchange's trading Systems.<sup>42</sup> To do so, the Exchange chose to waive the fees for some non-transaction related services or provide them at a very marginal cost, which was not profitable to the Exchange. This resulted in the Exchange forgoing revenue it could have generated from assessing higher fees.

The Exchange believes that the Proposed Access Fees are fair and reasonable because they will not result in excessive pricing or supra-competitive profit, when comparing the total annual expense that the Exchange projects to incur in connection with providing these access services versus the total annual revenue that the Exchange projects to collect in connection with services associated with the Proposed Access Fees. As mentioned above, for 2021,<sup>43</sup> the total annual expense for MIAX Pearl Options and MIAX for providing the access services associated with the Proposed Access Fees is projected to be approximately \$15.9 million, or approximately \$1,325,000 per month. This projected total annual expense is comprised of the following, all of which are directly related to the access services associated with the Proposed Access Fees: (1) third-party expense, relating to fees paid by the Exchange to third-parties for

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<sup>41</sup> The Exchange has incurred a cumulative loss of \$86 million since its inception in 2017 to 2020, the last year for which the Exchange's Form 1 data is available. See Exchange's Form 1/A, Application for Registration or Exemption from Registration as a National Securities Exchange, filed July 28, 2021, available at <https://www.sec.gov/Archives/edgar/vpr/2100/21000461.pdf>.

<sup>42</sup> The term "System" means the automated trading system used by the Exchange for the trading of securities. See Exchange Rule 100.

<sup>43</sup> The Exchange has not yet finalized its 2021 year end results.

certain products and services; and (2) internal expense, relating to the internal costs of the Exchange to provide the services associated with the Proposed Access Fees.<sup>44</sup> As noted above, the Exchange believes it is more appropriate to analyze the Proposed Access Fees utilizing its 2021 revenue and costs, which utilize the same presentation methodology as set forth in the Exchange’s previously-issued Audited Unconsolidated Financial Statements.<sup>45</sup> The \$15.9 million projected total annual expense is directly related to the access services associated with the Proposed Access Fees, and not any other product or service offered by the Exchange or MIAX. It does not include general costs of operating matching engines and other trading technology. No expense amount was allocated twice. Further, the Exchange notes that, with respect to the MIAX Pearl Options’ expenses included herein, those expenses only cover the MIAX Pearl options market; expenses associated with MIAX Pearl Equities are accounted for separately and are not included within the scope of this filing.

As discussed above, the Exchange conducted an extensive cost review in which the Exchange analyzed nearly every expense item in the Exchange’s general expense ledger (this includes over 150 separate and distinct expense items) to determine whether each such expense relates to the access services associated with the Proposed Access Fees, and, if such expense

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<sup>44</sup> The percentage allocations used in this proposed rule change may differ from past filings from the Exchange or its affiliates due to, among other things, changes in expenses charged by third-parties, adjustments to internal resource allocations, and different system architecture of the Exchange as compared to its affiliates.

<sup>45</sup> For example, the Exchange previously noted that all third-party expense described in its prior fee filing was contained in the information technology and communication costs line item under the section titled “Operating Expenses Incurred Directly or Allocated From Parent,” in the Exchange’s 2019 Form 1 Amendment containing its financial statements for 2018. See Securities Exchange Act Release No. 87876 (December 31, 2019), 85 FR 757 (January 7, 2020) (SR-PEARL-2019-36). Accordingly, the third-party expense described in this filing is attributed to the same line item for the Exchange’s 2021 Form 1 Amendment, which will be filed in 2022.

did so relate, what portion (or percentage) of such expense actually supports those services, and thus bears a relationship that is, “in nature and closeness,” directly related to those services. In performing this calculation, the Exchange considered other services and to which the expense may be applied and how much of the expense is directly and/or indirectly utilized in providing those other services. The sum of all such portions of expenses represents the total cost of the Exchange to provide access services associated with the Proposed Access Fees.

#### External Expense Allocations

For 2021, expenses relating to fees paid by the Exchange and MIAX to third-parties for products and services necessary to provide the access services associated with the Proposed Access Fees is projected to be \$3.9 million. This includes, but is not limited to, a portion of the fees paid to: (1) Equinix for data center services, including for the primary, secondary, and disaster recovery locations of the Exchange’s trading system infrastructure; (2) Zayo Group Holdings, Inc. (“Zayo”) for network services (fiber and bandwidth products and services) linking the Exchange’s and its affiliates’ office locations in Princeton, New Jersey and Miami, Florida, to all data center locations; (3) Secure Financial Transaction Infrastructure (“SFTI”),<sup>46</sup> which supports connectivity and feeds for the entire U.S. options industry; (4) various other services providers (including Thompson Reuters, NYSE, Nasdaq, and Internap), which provide content, connectivity services, and infrastructure services for critical components of options connectivity and network services; and (5) various other hardware and software providers (including Dell and Cisco, which support the production environment in which Members connect to the network to trade, receive market data, etc.).

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<sup>46</sup> See supra note 40.

For clarity, the Exchange took a conservative approach in determining the expense and the percentage of that expense to be allocated to providing access services in connection with the Proposed Access Fees. Only a portion of all fees paid to such third-parties is included in the third-party expenses described herein, and no expense amount is allocated twice. Accordingly, the Exchange does not allocate its entire information technology and communication costs to the access services associated with the Proposed Access Fees. This may result in the Exchange under allocating an expense to the provision of access services in connection with the Proposed Access Fees and such expenses may actually be higher or increase above what the Exchange utilizes within this proposal. Further, the Exchange notes that expenses associated with its affiliate, MIAX Emerald, are accounted for separately and are not included within the scope of this filing. Further, as part its ongoing assessment of costs and expenses (described above), the Exchange recently conducted a periodic thorough review of its expenses and resource allocations which, in turn, resulted in revised percentage allocations in this filing. Therefore, the percentage allocations used in this proposed rule change may differ from past filings from the Exchange or its affiliates due to, among other things, changes in expenses charged by third-parties, adjustments to internal resource allocations, and different system architecture of the Exchange as compared to its affiliates.

The Exchange believes it is reasonable to allocate such third-party expense described above towards the total cost to the Exchange and MIAX to provide the access services associated with the Proposed Access Fees. In particular, the Exchange believes it is reasonable to allocate the identified portion of the Equinix expense because Equinix operates the data centers (primary, secondary, and disaster recovery) that host the Exchange's network infrastructure. This includes, among other things, the necessary storage space, which continues

to expand and increase in cost, power to operate the network infrastructure, and cooling apparatuses to ensure the Exchange's network infrastructure maintains stability. Without these services from Equinix, the Exchange would not be able to operate and support the network and provide the access services associated with the Proposed Access Fees to its Members and their customers. The Exchange did not allocate all of the Equinix expense toward the cost of providing the access services associated with the Proposed Access Fees, only that portion which the Exchange identified as being specifically mapped to providing the access services associated with the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 62% of the total applicable Equinix expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable because it represents the Exchange's actual cost to provide the access services associated with the Proposed Access Fees, and not any other service, as supported by its cost review.<sup>47</sup>

The Exchange believes it is reasonable to allocate the identified portion of the Zayo expense because Zayo provides the internet, fiber and bandwidth connections with respect to the network, linking the Exchange with its affiliates, MIAX and MIAX Emerald, as well as the data center and disaster recovery locations. As such, all of the trade data, including the billions of messages each day per exchange, flow through Zayo's infrastructure over the Exchange's network. Without these services from Zayo, the Exchange would not be able to operate and

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<sup>47</sup> As noted above, the percentage allocations used in this proposed rule change may differ from past filings from the Exchange or its affiliates due to, among other things, changes in expenses charged by third-parties, adjustments to internal resource allocations, and different system architecture of the Exchange as compared to its affiliates. Again, as part its ongoing assessment of costs and expenses, the Exchange recently conducted a periodic thorough review of its expenses and resource allocations which, in turn, resulted in a revised percentage allocations in this filing.

support the network and provide the access services associated with the Proposed Access Fees. The Exchange did not allocate all of the Zayo expense toward the cost of providing the access services associated with the Proposed Access Fees, only the portion which the Exchange identified as being specifically mapped to providing the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 62% of the total applicable Zayo expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable because it represents the Exchange's actual cost to provide the access services associated with the Proposed Access Fees, and not any other service, as supported by its cost review.<sup>48</sup>

The Exchange believes it is reasonable to allocate the identified portions of the SFTI expense and various other service providers' (including Thompson Reuters, NYSE, Nasdaq, and Internap) expense because those entities provide connectivity and feeds for the entire U.S. options industry, as well as the content, connectivity services, and infrastructure services for critical components of the network. Without these services from SFTI and various other service providers, the Exchange would not be able to operate and support the network and provide access to its Members and their customers. The Exchange did not allocate all of the SFTI and other service providers' expense toward the cost of providing the access services associated with the Proposed Access Fees, only the portions which the Exchange identified as being specifically mapped to providing the access services associated with the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 75% of the total applicable SFTI and other service providers' expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable

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<sup>48</sup> Id.



because it represents the Exchange's actual cost to provide the access services associated with the Proposed Access Fees.<sup>49</sup>

The Exchange believes it is reasonable to allocate the identified portion of the other hardware and software provider expense because this includes costs for dedicated hardware licenses for switches and servers, as well as dedicated software licenses for security monitoring and reporting across the network. Without this hardware and software, the Exchange would not be able to operate and support the network and provide access to its Members and their customers. The Exchange did not allocate all of the hardware and software provider expense toward the cost of providing the access services associated with the Proposed Access Fees, only the portions which the Exchange identified as being specifically mapped to providing the access services associated with the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 51% of the total applicable hardware and software provider expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable because it represents the Exchange's actual cost to provide the access services associated with the Proposed Access Fees.<sup>50</sup>

#### Internal Expense Allocations

For 2021, total projected internal expenses relating to the Exchange and MIAX providing the access services associated with the Proposed Access Fees are projected to be approximately \$12 million. This includes, but is not limited to, costs associated with: (1) employee compensation and benefits for full-time employees that support the access services associated with the Proposed Access Fees, including staff in network operations, trading

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<sup>49</sup> Id. See also supra note 40 (regarding SFTI's announced fee increases).

<sup>50</sup> See supra note 47.

operations, development, system operations, business, as well as staff in general corporate departments (such as legal, regulatory, and finance) that support those employees and functions (including an increase as a result of the higher determinism project); (2) depreciation and amortization of hardware and software used to provide the access services associated with the Proposed Access Fees, including equipment, servers, cabling, purchased software and internally developed software used in the production environment to support the network for trading; and (3) occupancy costs for leased office space for staff that provide the access services associated with the Proposed Access Fees. The breakdown of these costs is more fully-described below.

For clarity, and as stated above, the Exchange took a conservative approach in determining the expense and the percentage of that expense to be allocated to providing access services in connection with the Proposed Access Fees. Only a portion of all such internal expenses are included in the internal expense herein, and no expense amount is allocated twice. Accordingly, the Exchange does not allocate its entire costs contained in those items to the access services associated with the Proposed Access Fees. This may result in the Exchange under allocating an expense to the provision of access services in connection with the Proposed Access Fees and such expenses may actually be higher or increase above what the Exchange utilizes within this proposal. Further, as part its ongoing assessment of costs and expenses (described above), the Exchange recently conducted a periodic thorough review of its expenses and resource allocations which, in turn, resulted in a revised percentage allocations in this filing.

The Exchange believes it is reasonable to allocate such internal expense described above towards the total cost to the Exchange and MIAA to provide the access services

associated with the Proposed Access Fees. In particular, the Exchange's and MIAX's combined employee compensation and benefits expense relating to providing the access services associated with the Proposed Access Fees is projected to be \$6.1 million, which is only a portion of the approximately \$12.6 million (for MIAX) and \$9.2 million (for MIAX Pearl Options) total projected expense for employee compensation and benefits. The Exchange believes it is reasonable to allocate the identified portion of such expense because this includes the time spent by employees of several departments, including Technology, Back Office, Systems Operations, Networking, Business Strategy Development (who create the business requirement documents that the Technology staff use to develop network features and enhancements), Trade Operations, Finance (who provide billing and accounting services relating to the network), and Legal (who provide legal services relating to the network, such as rule filings and various license agreements and other contracts). As part of the extensive cost review conducted by the Exchange, the Exchange reviewed the amount of time spent by employees on matters relating to the provision of access services associated with the Proposed Access Fees. Without these employees, the Exchange would not be able to provide the access services associated with the Proposed Access Fees to its Members and their customers. The Exchange did not allocate all of the employee compensation and benefits expense toward the cost of the access services associated with the Proposed Access Fees, only the portions which the Exchange identified as being specifically mapped to providing the access services associated with the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 28% of the total applicable employee compensation and benefits expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable because it represents the Exchange's actual cost

to provide the access services associated with the Proposed Access Fees, and not any other service, as supported by its cost review.<sup>51</sup>

The Exchange's and MIAX's depreciation and amortization expense relating to providing the services associated with the Proposed Access Fees is projected to be \$5.3 million, which is only a portion of the \$4.8 million (for MIAX) and \$2.9 million (for MIAX Pearl Options) total projected expense for depreciation and amortization. The Exchange believes it is reasonable to allocate the identified portion of such expense because such expense includes the actual cost of the computer equipment, such as dedicated servers, computers, laptops, monitors, information security appliances and storage, and network switching infrastructure equipment, including switches and taps that were purchased to operate and support the network and provide the access services associated with the Proposed Access Fees. Without this equipment, the Exchange would not be able to operate the network and provide the access services associated with the Proposed Access Fees to its Members and their customers. The Exchange did not allocate all of the depreciation and amortization expense toward the cost of providing the access services associated with the Proposed Access Fees, only the portion which the Exchange identified as being specifically mapped to providing the access services associated with the Proposed Access Fees. According to the Exchange's calculations, it allocated approximately 70% of the total applicable depreciation and amortization expense to providing the access services associated with the Proposed Access Fees, as these access services would not be possible without relying on such. The Exchange believes this allocation is reasonable

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<sup>51</sup> Id.

because it represents the Exchange's actual cost to provide the access services associated with the Proposed Access Fees, and not any other service, as supported by its cost review.<sup>52</sup>

The Exchange's and MIAX's occupancy expense relating to providing the services associated with the Proposed Access Fees is projected to be approximately \$0.6 million, which is only a portion of the \$0.6 million (for MIAX) and \$0.5 million (for MIAX Pearl Options) total projected expense for occupancy. The Exchange believes it is reasonable to allocate the identified portion of such expense because such expense represents the portion of the Exchange's cost to rent and maintain a physical location for the Exchange's staff who operate and support the network, including providing the access services associated with the Proposed Access Fees. This amount consists primarily of rent for the Exchange's Princeton, New Jersey office, as well as various related costs, such as physical security, property management fees, property taxes, and utilities. The Exchange operates its Network Operations Center ("NOC") and Security Operations Center ("SOC") from its Princeton, New Jersey office location. A centralized office space is required to house the staff that operates and supports the network. The Exchange currently has approximately 200 employees. Approximately two-thirds of the Exchange's staff are in the Technology department, and the majority of those staff have some role in the operation and performance of the access services associated with the Proposed Access Fees. Accordingly, the Exchange believes it is reasonable to allocate the identified portion of its occupancy expense because such amount represents the Exchange's actual cost to house the equipment and personnel who operate and support the Exchange's network infrastructure and the access services associated with the Proposed Access Fees. The Exchange did not allocate all of the occupancy expense toward the cost of providing the access services

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<sup>52</sup> Id.

associated with the Proposed Access Fees, only the portion which the Exchange identified as being specifically mapped to operating and supporting the network. According to the Exchange's calculations, it allocated approximately 53% of the total applicable occupancy expense to providing the access services associated with the Proposed Access Fees. The Exchange believes this allocation is reasonable because it represents the Exchange's cost to provide the access services associated with the Proposed Access Fees, and not any other service, as supported by its cost review.<sup>53</sup>

The Exchange notes that a material portion of its total overall expense is allocated to the provision of access services (including connectivity, ports, and trading permits). The Exchange believes this is reasonable and in line, as the Exchange operates a technology-based business that differentiates itself from its competitors based on its more deterministic and resilient trading systems that rely on access to a high performance network, resulting in significant technology expense. Over two-thirds of Exchange staff are technology-related employees. The majority of the Exchange's expense is technology-based. As described above, the Exchange and MIAX have only four primary sources of fees to recover their costs; thus, the Exchange believes it is reasonable to allocate a material portion of its total overall expense towards access fees.

Based on the above, the Exchange believes that its provision of access services associated with the Proposed Access Fees will not result in excessive pricing or supra-competitive profit. As discussed above, the Exchange projects that its annualized expense for 2021 to provide network connectivity services (all connectivity alternatives) to be approximately \$15.9 million per annum or an average of \$1,325,000 per month. The Exchange

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<sup>53</sup> Id.

implemented the Proposed Access Fees on August 1, 2021. For July 2021, prior to the Proposed Access Fees, Exchange Members and non-Members purchased a total of 156 10Gb ULL connections for which the Exchange and MIAX charged approximately \$1,547,620. This resulted in a profit of \$222,620 (a profit margin of 14.4%) for that month (including pro-rated charges). For the month of October 2021, which includes the tiered 10Gb ULL connectivity fees pursuant to the Proposed Access Fees, the Exchange and MIAX had Members and non-Members purchasing a total of 154 10Gb ULL connections for which the Exchange and MIAX charged a total of approximately \$1,684,000 (including pro-rated charges). This resulted in a profit of \$359,000 for that month for a profit margin of 21.3% (a modest 6.9% profit margin increase from July 2021 to October 2021 from 14.4% to 21.3%). The Exchange believes that the Proposed Access Fees are reasonable because they only generate an additional 6.9% of profit margin per month (reflecting a 21.3% profit margin).<sup>54</sup> The Exchange believes this modest increase in profit margin will allow it to continue to recoup its expenses and continue to invest in its technology infrastructure. Therefore, the Exchange also believes that this proposed profit margin increase is reasonable because it represents a reasonable rate of return.

Again, the Exchange cautions that this profit margin may fluctuate from month to month based in the uncertainty of predicting how many connections may be purchased from month to month as Members and non-Members are free to add and drop connections at any time based on their own business decisions. Notwithstanding that the revenue (and profit margin) may vary from month to month due to changes in connections and to changes to the Exchange's expenses, the number of connections has not materially changed over the prior months. Consequently, the Exchange believes that the months it has used as a baseline to

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<sup>54</sup> See supra note 31.

perform its assessment are representative of reasonably anticipated costs and expenses. This profit margin may also decrease due to the significant inflationary pressure on capital items that it needs to purchase to maintain the Exchange's technology and systems.<sup>55</sup> Accordingly, the Exchange believes its total projected revenue for the providing the access services associated with the Proposed Access Fees will not result in excessive pricing or supra-competitive profit.

The Exchange believes that conducting the above analysis on a per month basis is reasonable as the revenue generated from access services subject to the proposed fee generally remains static from month to month. The Exchange also conducted the above analysis on a per month basis to comply with the Commission Staff's Guidance, which requires a baseline analysis to assist in determining whether the proposal generates a supra-competitive profit. This monthly analysis was also provided in response to comment received on prior submissions of this proposed rule change.

The Exchange reiterates that it only has four primary sources of revenue and cost recovery mechanisms: transaction fees, access fees (which includes the Proposed Access Fees), regulatory fees, and market data fees. Accordingly, the Exchange must cover all of its expenses from these four primary sources of revenue and cost recovery mechanisms. As a result, each of these fees cannot be "flat" and cover only the expenses directly related to the fee that is charged. The above revenue and associated profit margin therefore are not solely intended to cover the costs associated with providing access services subject to the Proposed Access Fees.

The Exchange believes it is reasonable, equitable and not unfairly discriminatory to allocate the respective percentages of each expense category described above towards the total

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<sup>55</sup> See supra note 39.



cost to the Exchange of operating and supporting the network, including providing the access services associated with the Proposed Access Fees because the Exchange performed a line-by-line item analysis of nearly every expense of the Exchange, and has determined the expenses that directly relate to providing access to the Exchange. Further, the Exchange notes that, without the specific third-party and internal expense items listed above, the Exchange would not be able to provide the access services associated with the Proposed Access Fees to its Members and their customers. Each of these expense items, including physical hardware, software, employee compensation and benefits, occupancy costs, and the depreciation and amortization of equipment, have been identified through a line-by-line item analysis to be integral to providing access services. The Proposed Access Fees are intended to recover the costs of providing access to the Exchange's System. Accordingly, the Exchange believes that the Proposed Access Fees are fair and reasonable because they do not result in excessive pricing or supra-competitive profit, when comparing the actual costs to the Exchange versus the projected annual revenue from the Proposed Access Fees.

The Proposed Tiered-Pricing Structure is not Unfairly Discriminatory and Provides for the Equitable Allocation of Fees, Dues, and other Charges

The Exchange believes the proposed tiered-pricing structure is reasonable, fair, equitable, and not unfairly discriminatory because it will apply to all Members and non-Members in the same manner based on the amount of 10Gb ULL connectivity they require based on their own business decisions and usage of Exchange resources. All similarly situated Members and non-Members would be subject to the same fees. The fees do not depend on any distinction between Members and non-Members because they are solely determined by the individual Members' or non-Members' business needs and its impact on Exchange resources.

The proposed tiered-pricing structure is not unfairly discriminatory and provides for the equitable allocation of fees, dues, and other charges because it is designed to encourage Members and non-Members to be more efficient and economical when determining how to connect to the Exchange and the amount of the fees are based on the number of connections a Member or non-Member utilizes. Charging an incrementally higher fee to a Member or non-Member that utilizes numerous connections is directly related to the increased costs the Exchange incurs in providing and maintaining those additional connections. The proposed tiered pricing structure should also enable the Exchange to better monitor and provide access to the Exchange's network to ensure sufficient capacity and headroom in the System.

The Exchange believes that the proposal to move to a tiered-pricing structure for its 10Gb ULL connections is reasonable, equitably allocated and not unfairly discriminatory because the majority of Members and non-Members that purchase 10Gb ULL connections will either save money or pay the same amount after the tiered-pricing structure is implemented. After the effective date of the First Proposed Rule Change on August 1, 2021, approximately 80% of the firms that purchased at least one 10Gb ULL connection experienced a decrease in their monthly connectivity fees while only approximately 20% of firms experienced an increase in their monthly connectivity fees as a result of the proposed tiered-pricing structure when compared to the flat monthly fee structure. To illustrate, firms that purchase only one 10Gb ULL connection per month used to pay the flat rate of \$10,000 per month for that one 10Gb ULL connection. Pursuant to the proposed tiered-pricing structure, these firms now pay \$9,000 per month for that same one 10Gb ULL connection, saving \$1,000 per month or \$12,000 annually. Further, firms that purchase two 10Gb ULL connections per month previously paid a flat rate of \$20,000 per month ( $\$10,000 \times 2$ ) for those two 10Gb ULL connections. Pursuant to the proposed tiered-

pricing structure, these firms now pay \$18,000 per month (\$9,000 x 2) for those two 10Gb ULL connections, saving \$2,000 per month or \$24,000 annually.

To achieve a consistent, premium network performance, the Exchange must build out and continue to maintain a network that has the capacity to handle the message rate requirements of not only firms that consume minimal Exchange connectivity resources, but also those firms that most heavily consume Exchange connectivity resources, network consumers, and purchasers of 10Gb ULL connectivity. 10Gb ULL connectivity is not an unlimited resource as the Exchange needs to purchase additional equipment to satisfy requests for additional connections. The Exchange also needs to provide personnel to set up new connections, service requests related to adding new and/or deleting existing connections, respond to performance queries from, and to maintain those connections on behalf of Members and non-Members. Also, those firms that utilize 10Gb ULL connectivity typically generate a disproportionate amount of messages and order traffic, usually billions per day across the Exchange. These billions of messages per day consume the Exchange's resources and significantly contribute to the overall network connectivity expense for storage and network transport capabilities. The Exchange also has to purchase additional storage capacity on an ongoing basis to ensure it has sufficient capacity to store these messages as part of its surveillance program and to satisfy its record keeping requirements under the Exchange Act.<sup>56</sup> Thus, as the number of connections an entity has increases, certain other costs incurred by the Exchange that are correlated to, though not directly affected by, connection costs (e.g., storage costs, surveillance costs, service expenses) also increase.

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<sup>56</sup> 17 CFR 240.17a-1 (recordkeeping rule for national securities exchanges, national securities associations, registered clearing agencies and the Municipal Securities Rulemaking Board).

The Exchange sought to design the proposed tiered-pricing structure to set the amount of the fees to relate to the number of connections a firm purchases. The more connections purchased by a firm likely results in greater expenditure of Exchange resources and increased cost to the Exchange. With this in mind, the Exchange proposes to decrease the monthly fees for those firms who connect to the Exchange as part of their best execution obligations and generally tend to send the least amount of orders and messages over those connections. The Exchange notes that firms that primarily route orders seeking best execution generally only purchase a limited number of connections. Those firms also generally send fewer orders and messages over those connections, resulting in less strain on Exchange resources. Therefore, the connectivity costs will likely be lower for these firms based on the proposed tiered-pricing structure.

On a similar note, the Exchange proposes to increase the fee for those firms that purchase more connections resulting in greater expenditure of Exchange resources and increased cost to the Exchange. The Exchange notes that these firms that purchase more than two to four 10Gb ULL connections essentially do so for competitive reasons amongst themselves and choose to utilize numerous connections based on their business needs and desire to attempt to access the market quicker by using the connection with the least amount of latency. These firms are generally engaged in sending liquidity removing orders to the Exchange and seek to add more connections so they can access resting liquidity ahead of their competitors. For instance, a Member may have just sent numerous messages and/or orders over one of their 10Gb ULL connections that are in queue to be processed. That same Member then seeks to enter an order to remove liquidity from the Exchange's Book. That Member may choose to send that order over one or more of their other 10Gb ULL connections with less message and/or order traffic to ensure that their liquidity taking order accesses the Exchange quicker because that connection's

queue is shorter. These firms also tend to frequently add and drop connections mid-month to determine which connections have the least latency, which results in increased costs to the Exchange to frequently make changes in the data center and provide the additional technical and personnel support necessary to satisfy these requests.

The firms that engage in the above-described liquidity removing and advanced trading strategies typically require multiple connections and, therefore, generate higher costs by utilizing more of the Exchange's resources. Those firms may also conduct other latency measurements over their connections and drop and simultaneously add connections mid-month based on their own assessment of their performance. This results in Exchange staff processing such requests, potentially purchasing additional equipment, and performing the necessary network engineering to replace those connections in the data center. Therefore, the Exchange believes it is equitable for these firms to experience increased connectivity costs based on their disproportionate pull on Exchange resources to provide the additional connectivity.

In addition, the proposed tiered-pricing structure is equitable because it is designed to encourage Members and non-Members to be more efficient and economical when determining how to connect to the Exchange. Section 6(b)(5) of the Exchange Act requires the Exchange to provide access on terms that are not unfairly discriminatory.<sup>57</sup> As stated above, 10Gb ULL connectivity is not an unlimited resource and the Exchange's network is limited in the amount of connections it can provide. However, the Exchange must accommodate requests for additional connectivity and access to the Exchange's System to ensure that the Exchange is able to provide access on non-discriminatory terms and ensure sufficient capacity and headroom in the System. To accommodate requests for additional connectivity on top of current network capacity

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<sup>57</sup> 15 U.S.C. 78f(b)(5).

constraints, requires that the Exchange purchase additional equipment to satisfy these requests. The Exchange also needs to provide personnel to set up new connections and to maintain those connections on behalf of Members and non-Members. The proposed tiered-pricing structure is equitable because it is designed to encourage Members and non-Members to be more efficient and economical in selecting the amount of connectivity they request while balancing that against the Exchange's increased expenses when expanding its network to accommodate additional connectivity.

#### The Proposed Fees are Reasonable when Compared to The Fees of other Options

##### Exchanges with Similar Market Share

The Exchange does not have visibility into other equities exchanges' costs to provide connectivity or their fee markup over those costs, and therefore cannot use other exchange's connectivity fees as a benchmark to determine a reasonable markup over the costs of providing connectivity. Nevertheless, the Exchange believes the other exchanges' connectivity fees are a useful example of alternative approaches to providing and charging for connectivity. To that end, the Exchange believes the proposed tiered-pricing structure for 10Gb ULL connections is reasonable because the proposed highest tier is still less than fees charged for similar connectivity provided by other options exchanges with comparable market shares. For example, NASDAQ (equity options market share of 8.88% as of November 26, 2021 for the month of November)<sup>58</sup> charges a monthly fee of \$10,000 per 10Gb fiber connection and \$15,000 per 10Gb Ultra fiber connection.<sup>59</sup> The highest tier of the Exchange's proposed fee structure for a 10Gb ULL connection is \$13,000 for the fifth and subsequent connections,

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<sup>58</sup> See "The market at a glance," available at <https://www.miaxoptions.com/> (last visited November 26, 2021).

<sup>59</sup> See NASDAQ Rules, General 8: Connectivity, Section 1. Co-Location Services.

which is \$2,000 per month less than NASDAQ and, unlike NASDAQ, the Exchange does not charge installation fees. For market participants with fewer connections, the difference is even more stark. For a market participant with two connections to the Exchange and two connections to NASDAQ, the difference in connection fees would be \$12,000 per month. The Exchange notes that the same connectivity fees described above for NASDAQ also apply to its affiliates, ISE<sup>60</sup> (equity options market share of 7.96% as of November 26, 2021 for the month of November)<sup>61</sup> and PHLX (equity options market share of 9.31% as of November 26, 2021 for the month of November).<sup>62</sup> Amex (equity options market share of 5.05% as of November 26, 2021 for the month of November)<sup>63</sup> charges \$15,000 per connection initially plus \$22,000 monthly per 10Gb LX LCN circuit connection.<sup>64</sup> Again, the highest tier of the Exchange's proposed fee structure for a 10Gb ULL connection is \$9,000 per month lower than the Amex connectivity fee after the first month.

In the each of the above cases, the Exchange's highest tier in the proposed tiered-pricing structure only applies to the fifth and additional connections and is still significantly lower than that of competing options exchanges with similar market share. Despite proposing lower or similar fees to that of competing options exchanges with similar market share, the Exchange believes that it provides a premium network experience to its Members and non-Members via a highly deterministic System, enhanced network monitoring and customer reporting, and a superior network infrastructure than markets with higher market shares and more expensive

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<sup>60</sup> See ISE Rules, General 8: Connectivity.

<sup>61</sup> See supra note 58.

<sup>62</sup> See id. See also PHLX Rules, General 8: Connectivity.

<sup>63</sup> See supra note 58.

<sup>64</sup> See Amex Fee Schedule, Section IV.

connectivity alternatives. Each of the connectivity rates in place at competing options exchanges were filed with the Commission for immediate effectiveness and remain in place today.

The Exchange further believes that the Proposed Access Fees are reasonable, equitably allocated and not unfairly discriminatory because, for one 10Gb ULL connection, the Exchange provides each Member or non-Member access to all twelve (12) matching engines on MIAX Pearl and a vast majority choose to connect to all twelve (12) matching engines. The Exchange believes that other exchanges require firms to connect to multiple matching engines.<sup>65</sup>

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 that is not necessary or appropriate in furtherance of the purposes of the Act.

With respect to intra-market competition, the Exchange does not believe that the proposed rule change would place certain market participants at the Exchange at a relative disadvantage compared to other market participants or affect the ability of such market participants to compete. As stated above, the Exchange does not believe its proposed pricing will impose a barrier to entry to smaller participants and notes that its proposed connectivity pricing structure for its 10Gb ULL connections is associated with relative usage of the various market participants. Further, the majority of firms that purchase 10Gb ULL connections may

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<sup>65</sup> See Specialized Quote Interface Specification, Nasdaq PHLX, Nasdaq Options Market, Nasdaq BX Options, Version 6.5a, Section 2, Architecture (revised August 16, 2019), available at <http://www.nasdaqtrader.com/content/technicalsupport/specifications/TradingProducts/SQF6.5a-2019-Aug.pdf>. The Exchange notes that it is unclear whether the NASDAQ exchanges include connectivity to each matching engine for the single fee or charge per connection, per matching engine. See also NYSE Technology FAQ and Best Practices: Options, Section 5.1 (How many matching engines are used by each exchange?) (September 2020). The Exchange notes that NYSE provides a link to an Excel file detailing the number of matching engines per options exchange, with Arca and Amex having 19 and 17 matching engines, respectively.



either save money or pay the same amount after the tiered-pricing structure is implemented. While total cost may be increased for market participants with larger capacity needs or for business/technical preferences, such options provide far more capacity and are purchased by those that consume more resources from the network. Accordingly, the proposed tiered-pricing structure does not favor certain categories of market participants in a manner that would impose an undue burden on competition; rather, the allocation reflects the network resources consumed by the various usage of market participants – lowest bandwidth consuming members pay the least, and highest bandwidth consuming members pay the most, particularly since higher bandwidth consumption translates to higher costs to the Exchange.

The Exchange also does not believe that the proposed rule change will result in any burden on inter-market competition that is not necessary or appropriate in furtherance of the purposes of the Act. As discussed above, options market participants are not forced to connect to all options exchanges. The Exchange operates in a highly competitive environment, and as discussed above, its ability to price access and connectivity is constrained by competition among exchanges and third parties. There are other options markets of which market participants may connect to trade options. There is also a possible range of alternative strategies, including routing to the exchange through another participant or market center or accessing the Exchange indirectly. For example, there are 15 other U.S. options exchanges, which the Exchange must consider in its pricing discipline in order to compete for market participants. In this competitive environment, market participants are free to choose which competing exchange or reseller to use to satisfy their business needs. As a result, the Exchange believes this proposed rule change permits fair competition among national securities exchanges. Accordingly, the Exchange does

not believe its proposed fee changes impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

Regrettably, the Exchange believes that the application of the Guidance to date has adversely affected inter-market competition by impeding the ability of smaller, low cost exchanges to adopt or increase fees for their market data and access services (including connectivity and port products and services). Since the adoption of the Guidance, and even more so recently, it has become harder, particularly for smaller, low cost exchanges, to adopt or increase fees to generate revenue necessary to invest in systems, provide innovative trading products and solutions, and improve competitive standing to the benefit of the affected exchanges' market participants. Although the Staff Guidance has served an important policy goal of improving disclosures and requiring exchanges to justify that their market data and access fee proposals are fair and reasonable, it has also negatively impacted exchanges, and particularly many smaller, low cost exchanges, that seek to adopt or increase fees despite providing enhanced disclosures and rationale to support their proposed fee changes.

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

As described above, the Exchange received one comment letter on the First Proposed Rule Change and four comment letters on the Second Proposed Rule Change.<sup>66</sup> The Exchange responded to the comment letters in the Third Proposed Rule Change and repeats its response in its filing. No comment letters were received in response to the Third Proposed Rule Change.

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<sup>66</sup> See supra note 9.

## HMA Letter

The HMA Letter does not raise specific issues with the First or Second Proposed Rule Changes. Instead the HMA Letter is generally critical of the exchange fee filing process contained in Section 19(b)(3)(A)(ii) of the Act,<sup>67</sup> and Rule 19b-4(f)(2) thereunder,<sup>68</sup> and other exchanges' fee filings in recent years. The HMA Letter, however, applauds the level of disclosure the Exchange included in the First and Second Proposed Rule Changes and was supportive of the efforts made by the Exchange and its affiliates to provide transparency and justify their proposed fees. The HMA Letter specifically notes that:

“MIAX has repeatedly filed to change its connectivity fees in a way that will materially lower costs for many users, while increasing the costs for some of its heaviest of users. These filings have been withdrawn and repeatedly refiled. Each time, however, the filings contain significantly greater information about who is impacted and how than other filings that have been permitted to take effect without suspension. For example, MIAX detailed the associated projected revenues generated from the connectivity fees by user class, again in a clear attempt to comply with the SRO Fee Filing Guidance.”<sup>69</sup>

As the HMA Letter notes, the Exchange refiled its same fee proposals to include significantly greater information about who is impacted and how, primarily at the request of the Commission Staff and in response to comments. The Exchange is again refiling its

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<sup>67</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>68</sup> 17 CFR 240.19b-4.

<sup>69</sup> See HMA Letter, supra note 9.

proposal to include more information surrounding the proposed fees and to respond to commenters.

### SIG Letter 2

SIG Letter 2 argues that the Exchange, in withdrawing the First Proposed Rule Change and refiling the Second Proposed Rule Change, “improperly circumvent[ed] the procedural protections embedded in Exchange Act Section 19(b)(3)(C), and subvert[ed] the balance of interests upheld therein.”<sup>70</sup> SIG’s assertion that the Exchange’s entire reason for withdrawing and refiling was to subvert the protections of the Exchange Act are entirely without merit. The Exchange withdrew the First Proposed Rule Change and replaced it with the Second Proposed Rule Change in good faith to provide additional justification and explanation for the proposed fee changes and did so in compliance with the Exchange Act. The same is true in this filing, where the Exchange withdrew the Second Proposed Rule Change and submitted this filing to provide additional justification and explanation for the proposed fee changes and directly responds to certain points raised in SIG Letters 1, 2, and 3, as well as the SIFMA Letter submitted on the First and Second Proposed Rule Changes.

As SIG well knows, exchanges are able to withdraw and refile various proposals (including fee changes and other rule changes) with the Commission for a multitude of reasons, not the least of which is to address feedback and comments from market participants and Commission Staff. The Exchange is well within the bounds of the Act and the rules and regulations thereunder to withdraw a proposed rule change and replace it with a new proposed rule change in good faith and to enhance the filing to ensure it complies with the requirements of the Act.

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<sup>70</sup> See SIG Letter 2, supra note 9.

### SIG Letters 1 and 3

As an initial matter, SIG Letter 1 cites Rule 700(b)(3) of the Commission’s Rules of Fair Practice which places “the burden to demonstrate that a proposed rule change is consistent with the Act on the self-regulatory organization that proposed the rule change” and states that a “mere assertion that the proposed rule change is consistent with those requirements . . . is not sufficient.”<sup>71</sup> SIG Letter 1’s assertion that the Exchange has not met this burden is without merit, especially considering the overwhelming amounts of revenue and cost information the Exchange included in the First and Second Proposed Rule Changes and this filing.

Until recently, the Exchange operated at a net annual loss since it launched operations in 2017.<sup>72</sup> As stated above, the Exchange believes that exchanges in setting fees of all types should meet very high standards of transparency to demonstrate why each new fee or fee increase meets the requirements of the Act that fees be reasonable, equitably allocated, not unfairly discriminatory, and not create an undue burden on competition among market participants. The Exchange believes this high standard is especially important when an exchange imposes various access fees for market participants to access an exchange’s marketplace. The Exchange believes it has achieved this standard in this filing and in the First Proposed Rule Change, Second Proposed Rule Change. Similar justifications for the proposed fee change included in the First and Second Proposed Rule Changes, but also in this filing, were previously included in similar fee changes filed by the Exchange and its affiliates, MIAX Emerald and MIAX, and SIG did not submit a comment letter on those filings.<sup>73</sup> Those filings were not suspended by the Commission

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<sup>71</sup> 17 CFR 201.700(b)(3).

<sup>72</sup> See supra note 41.

<sup>73</sup> See Securities Exchange Act Release Nos. 91858 (May 12, 2021), 86 FR 26967 (May 18, 2021) (SR-PEARL-2021-23) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend the MIAX Pearl Fee Schedule to Remove the Cap on

and continue to remain in effect. The justification included in each of the prior filings was the result of numerous withdrawals and re-filings of the proposals to address comments received from Commission Staff over many months. The Exchange and its affiliates have worked diligently with Commission Staff on ensuring the justification included in past fee filings fully support an assertion that those fee changes are consistent with the Act.<sup>74</sup> The Exchange leveraged its past work with Commission Staff to ensure the justification provided herein and in the First and Second Proposed Rule Changes include the same level of detail (or more) as the

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the Number of Additional Limited Service Ports Available to Market Makers); 91460 (April 2, 2021), 86 FR 18349 (April 8, 2021) (SR-EMERALD-2021-11) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend Its Fee Schedule To Adopt Port Fees, Increase Certain Network Connectivity Fees, and Increase the Number of Additional Limited Service MIAX Emerald Express Interface Ports Available to Market Makers); and 91857 (May 12, 2021), 86 FR 26973 (May 18, 2021) (SR-MIAX-2021-19) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend Its Fee Schedule To Remove the Cap on the Number of Additional Limited Service Ports Available to Market Makers).

<sup>74</sup> See, e.g., Securities Exchange Act Release No. 90196 (October 15, 2020), 85 FR 67064 (October 21, 2020) (SR-EMERALD-2020-11) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend Its Fee Schedule To Adopt One-Time Membership Application Fees and Monthly Trading Permit Fees). See Securities Exchange Act Release Nos. 90601 (December 8, 2020), 85 FR 80864 (December 14, 2020) (SR-EMERALD-2020-18) (re-filing with more detail added in response to Commission Staff's feedback and after withdrawing SR-EMERALD-2020-11); and 91033 (February 1, 2021), 86 FR 8455 (February 5, 2021) (SR-EMERALD-2021-03) (re-filing with more detail added in response to Commission Staff's feedback and after withdrawing SR-EMERALD-2020-18). The Exchange initially filed a proposal to remove the cap on the number of additional Limited Service MEO Ports available to Members on April 9, 2021. See SR-PEARL-2021-17. On April 22, 2021, the Exchange withdrew SR-PEARL-2021-17 and refiled that proposal (without increasing the actual fee amounts) to provide further clarification regarding the Exchange's revenues, costs, and profitability any time more Limited Service MEO Ports become available, in general, (including information regarding the Exchange's methodology for determining the costs and revenues for additional Limited Service MEO Ports). See SR-PEARL-2021-20. On May 3, 2021, the Exchange withdrew SR-PEARL-2021-20 and refiled that proposal to further clarify its cost methodology. See SR-PEARL-2021-22. On May 10, 2021, the Exchange withdrew SR-PEARL-2021-22 and refiled that proposal as SR-PEARL-2021-23. See Securities Exchange Act Release No. 91858 (May 12, 2021), 86 FR 26967 (May 18, 2021) (SR-PEARL-2021-23).

prior fee changes that survived Commission scrutiny. The Exchange’s detailed disclosures in fee filings have also been applauded by one industry group which noted, “[the Exchange’s] filings contain significantly greater information about who is impacted and how than other filings that have been permitted to take effect without suspension.”<sup>75</sup> That same commenter also noted their “worry that the Commission’s process for reviewing and evaluating exchange filings may be inconsistently applied.”<sup>76</sup>

Therefore, a finding by the Commission that the Exchange has not met its burden to show that the proposed fee change is consistent with the Act would be different than the Commission’s treatment of similar past filings, would create further ambiguity regarding the standards exchange fee filings should satisfy, and is not warranted here.

In addition, the arguments in SIG Letter 1 do not support their claim that the Exchange has not met its burden to show the proposed rule change is consistent with the Act. Prior to, and after submitting the First Proposed Rule Change, the Exchange solicited feedback from its Members, including SIG. SIG relayed their concerns regarding the proposed change. The Exchange then sought to work with SIG to address their concerns and gain a better understanding of the access/connectivity/quoting infrastructure of other exchanges. In response, SIG provided no substantive suggestions on how to amend the First Proposed Rule Change to address their concerns and instead chose to submit three comment letters. One could argue that SIG is using the comment letter process not to raise legitimate regulatory concerns regarding the proposal, but to inhibit or delay proposed fee changes by the Exchange.

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<sup>75</sup> See HMA Letter, supra note 9.

<sup>76</sup> Id. (providing examples where non-transaction fee filings by other exchanges have been permitted to remain effective and not suspended by the Commission despite less disclosure and justification).

Nonetheless, the Exchange has enhanced its cost and revenue analysis and data in this Third [sic] Proposed Rule Change to further justify that the Proposed Access Fees are reasonable in accordance with the Commission Staff's Guidance. Among other things, these enhancements include providing baseline information in the form of data from the month before the Proposed Access Fees became effective.

The Exchange now responds to SIG remaining claims below. SIG Letter 3 first summarizes its arguments made in SIG Letters 1 and 2 and incorporates those arguments by reference. The Exchange responded to the arguments in SIG Letter 2 above. SIG Letter 3 incorporates the following arguments from SIG Letter 1, which the Exchange will first respond to in turn, below:

“(1) the prospect that a member may withdraw from the Exchanges if a fee is too costly is not a basis for asserting that the fee is reasonable; (2) profit margin comparisons do not support the Exchanges' claims that they will not realize a supracompetitive profit, the Exchanges' respective profit margins of 30% (for MIAX and Pearl) and 51% (for Emerald) in relation to connectivity fees are high in any event, and comparisons to competing exchanges' overall operating profit margins are an inapt “apples-to-oranges” comparison; (3) the Exchanges provide no support for their claim that their proposed tiered pricing structure is needed to encourage efficiency in connectivity usage; (4) the Exchanges provided no support for their claim that the tiered pricing structure allows them to better monitor connectivity usage, nor that this is an appropriate basis for the pricing structure in any event; (5) the Exchanges' claim that firms who purchase more 10Gb ULL lines generate “higher” costs is misleading, and they offered no



support for this claim in any event; (6) no other exchange has tiered connectivity pricing; (7) the recoupment of investment for exchange infrastructure has no supporting nexus with the claim that the proposed fees are reasonable, equitably allocated, and not unfairly discriminatory; and (8) the recoupment of investment claim belies the Exchanges' claim of encouraging efficiency in connectivity usage."<sup>77</sup>

The Exchange's Examples of Members Terminating Their Exchange Access Shows that Members Have Choice Whether to Connect to an Exchange Based on Fees

SIG asserts that "the prospect that a member may withdraw from the Exchanges if a fee is too costly is not a basis for asserting that the fee is reasonable."<sup>78</sup> SIG misinterprets the Exchange's argument here. The Exchange provided the examples of firms terminating access to certain markets due to fees to support its assertion that firms, including market makers, are not required to connect to all markets and may drop access if fees become too costly for their business models and alternative or substitute forms of connectivity are available to those firms who choose to terminate access. The Commission Staff Guidance also provides that "[a] statement that substitute products or services are available to market participants in the relevant market (e.g., equities or options) can demonstrate competitive forces if supported by evidence that substitute products or services exist."<sup>79</sup> Nonetheless, the Third [sic] Proposed Rule Change no longer makes this assertion as a basis for the proposed fee change and, therefore, the Exchange believes it is not necessary to respond to this portion of SIG Letters 1 and 3.

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<sup>77</sup> See SIG Letter 3, supra note 9.

<sup>78</sup> Id.

<sup>79</sup> See Guidance, supra note 23.

### The Proposed Fees Will Not Result in Excessive Pricing or Supra-Competitive Profit

Next, SIG asserts that the Exchange's "profit margin comparisons do not support the Exchange's claims that they will not realize a supracompetitive profit," that "the Exchanges' respective profit margins of 30% (for MIAX and Pearl) and 51% (for Emerald) in relation to connectivity fees are high in any event," and "comparisons to competing exchanges' overall operating profit margins are an inapt 'apples-to-oranges' comparison."

The Exchange has provided ample data that the proposed fees would not result in excessive pricing or a supra-competitive profit. In this Third [sic] Proposed Rule Change, the Exchange no longer utilizes a comparison of its profit margin to that of other options exchanges as a basis that the Proposed Access Fees are reasonable. Rather, the Exchange has enhanced its cost and revenue analysis and data in this Third [sic] Proposed Rule Change to further justify that the Proposed Access Fees are reasonable in accordance with the Commission Staff's Guidance. Therefore, the Exchange believes it is no longer necessary to respond to this portion of SIG Letters 1 and 3.

### The Proposed Tiered Pricing Structure is Not Unfairly Discriminatory

SIG challenges the proposed fees by arguing that "the Exchange[] provide[s] no support for [its] claim that [the] proposed tiered pricing structure is needed to encourage efficiency in connectivity usage and the Exchange[] provided no support for [the] claim that the tiered pricing structure allows them to better monitor connectivity usage, nor that this is an appropriate basis for the pricing structure in any event." The Exchange provided additional justification to support that the Proposed Access Fees are equitable and not unfairly discriminatory above in response to SIG's assertions.

### Firms that Purchase More 10Gb ULL Generate Higher Exchange Costs

SIG argues that “the Exchanges’ claim that firms who purchase more 10Gb ULL lines generate ‘higher’ costs is misleading,” and that the Exchange has “offered no support for this claim in any event.” As described above, the Exchange sought to design the proposed tiered-pricing structure to set the amount of the fees to relate to the number of connections a firm purchases and the Exchange believes it provided ample justification for the proposed tiered-pricing structure in the First and Second Proposed Rule Changes. Nonetheless, the Exchange provides additional justification to support that the Proposed Access Fees are equitable and not unfairly discriminatory above in response to SIG’s assertions.

### The Proposed Tiered-Pricing Structure for 10Gb ULL Connectivity Will Provide Cost Savings for the Majority of Exchange Members

The SIG Letter incorrectly asserts that no other exchange has tiered connectivity pricing. Numerous other exchanges provide tiered fee structures for various other types of access to their platforms, including trading permits and ports.<sup>80</sup> The Exchange provided adequate evidence that most firms would incur cost savings under the Proposed Access Fees in the First and Second Proposed Rule Changes and this filing. Nonetheless, the Exchange believes it provided

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<sup>80</sup> See Cboe Exchange, Inc. Fee Schedule, Logical Connectivity Fees (\$750 per port per month for the first 5 BOE/FIX Logical Ports and \$800 per port per month for each port over 5; \$1,500 per port per month for the first 5 BOE Bulk Logical Ports, \$2,500 per port per month for ports 6-30, and \$3,000 per port per month for each port over 30); Cboe BXZ Exchange, Inc. Options Fee Schedule, Options Logical Port Fees, Ports with Bulk Quoting Capabilities (\$1,500 per port per month for the first and second ports, \$2,500 per port per month for three or more); Nasdaq Stock Market LLC, Options 7, Pricing Schedule, Section 3 (\$1,500 per port per month for the first 5 SQF ports; \$1,000 per port per month for SQF ports 15-20; and \$500 per port per month for all SQF ports over 21); NYSE American Options Fee Schedule, Section V.A., Port Fees and NYSE Arca Options Fee Schedule, Port Fees (both charging \$450 per port for order/quote entry ports 1-40 and \$150 per port for ports 41 and greater).

additional justification to support that the Proposed Access Fees are equitable and not unfairly discriminatory above in response to SIG’s assertions.

#### Recoupment of Exchange Infrastructure Costs

Nowhere in this proposal or in the First Proposed Rule Change did the Exchange assert that it benefits competition to allow a new exchange entrant to recoup their infrastructure costs. Rather, the Exchange asserts above that its “proposed fees are reasonable, equitably allocated and not unfairly discriminatory because the Exchange, and its affiliates, are still recouping the initial expenditures from building out their systems while the legacy exchanges have already paid for and built their systems.” The Exchange no longer makes this assertion in this filing and, therefore, does not believe it is necessary to respond to SIG’s assertion here.

#### SIFMA Letter

In sum, the SIFMA Letter asserts that the Exchange has failed to demonstrate that the Proposed Access Fees are reasonable for three reasons:

- (i) “The Exchanges’ “platform competition” argument that competition for order flow constrains pricing for market data or other products and services exclusively offered by an exchange does not demonstrate that the fees are reasonable.”
- (ii) “...order flow competition alone between exchanges does not demonstrate that the fees for the products and services subject to the Proposal are reasonable.”
- (iii) “the Exchanges’ argument that the products and services subject to the Proposals are optional does not reflect marketplace reality, nor does it demonstrate that the proposed fees are reasonable.”

The Exchange responds to each of SIFMA’s challenges in turn below.

### The Exchange Never Set Forth a “Platform Competition” Argument

The SIFMA Letter asserts that the Exchange’s “platform competition” argument that competition for order flow constrains pricing for market data or other products and services exclusively offered by an exchange does not demonstrate that the fees are reasonable.”<sup>81</sup> The Exchange does not believe it is necessary to respond to this assertion because it has never set forth a “platform competition”<sup>82</sup> argument to justify the Proposed Access Fees in the First or Second Proposed Rule Change nor does it do so in this filing.

### The Exchange Is Not Arguing that Order Flow Competition Alone Demonstrates that the Proposed Fees are Reasonable

The SIFMA Letter asserts that “order flow competition alone between exchanges does not demonstrate that the fees for the products and services subject to the Proposal are reasonable.”<sup>83</sup> The Exchange never directly asserted in the First or Second Proposed Rule Changes, nor does it do so in this filing, that order flow competition, alone, demonstrated that the Proposed Access Fees are reasonable and has removed any language that could imply this argument from this filing.

### Other SIFMA Assertions

SIFMA also challenges or asserts: (i) the substitutability or optionality of 10Gb ULL connections, (ii) whether the Exchange has shown that the fees are equitable and non-

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<sup>81</sup> See SIFMA Letter, supra note 9.

<sup>82</sup> Pursuant to the Guidance, “platform theory generally asserts that when a business offers facilities that bring together two or more distinct types of customers, it is the overall return of the platform, rather than the return of any particular fees charged to a type of customer, that should be used to assess the competitiveness of the platform’s market.” See Guidance, supra note 23.

<sup>83</sup> See SIFMA Letter, supra note 9.

discriminatory; (iii) that a tiered pricing structure will impose higher cost on all market participants; (iv) that a tiered pricing structure will encourage market participants to be more economical with the usage; (v) greater number of connections use greater Exchange resources; and (vi) that the Exchange has not provided extensive information regarding its cost data and how it determined its cost analysis. The Exchange believes that these assertions by SIFMA basically echo assertions made in SIG Letters 1 and 3 and that it provided a response to these assertions under its response to SIG above or in provided enhanced transparency and justification in this filing.

### III. Suspension of the Proposed Rule Change

Pursuant to Section 19(b)(3)(C) of the Act,<sup>84</sup> at any time within 60 days of the date of filing of a proposed rule change pursuant to Section 19(b)(1) of the Act,<sup>85</sup> the Commission summarily may temporarily suspend the change in the rules of a self-regulatory organization (“SRO”) if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. As discussed below, the Commission believes a temporary suspension of the proposed rule change is necessary and appropriate to allow for additional analysis of the proposed rule change’s consistency with the Act and the rules thereunder.

As the Exchange further details above, the Exchange first filed a proposed rule change proposing fee changes as proposed herein on July 30, 2021, with the proposed fee changes effective beginning August 1, 2021. That proposal, SR-PEARL-2021-36, was published for

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<sup>84</sup> 15 U.S.C. 78s(b)(3)(C).

<sup>85</sup> 15 U.S.C. 78s(b)(1).

comment in the Federal Register on August 17, 2021.<sup>86</sup> On September 24, 2021 the Exchange withdrew SR-PEARL-2021-36 and filed a proposed rule change proposing fee changes as proposed herein. That proposal, SR-PEARL-2021-45, was published for comment in the Federal Register on October 4, 2021.<sup>87</sup> The Commission received four comment letters from three separate commenters on SR-PEARL-2021-45.<sup>88</sup> On November 22, 2021, pursuant to Section 19(b)(3)(C) of the Act, the Commission: (1) temporarily suspended the proposed rule change; and (2) instituted proceedings to determine whether to approve or disapprove the proposed rule change.<sup>89</sup> On December 1, 2021, the Exchange withdrew SR-PEARL-2021-45 and filed a proposed rule change proposing fee changes as proposed herein. That filing, SR-PEARL-2021-57,<sup>90</sup> was published for comment in the Federal Register on December 20, 2021.<sup>91</sup> On January 27, 2022, pursuant to Section 19(b)(3)(C) of the Act, the Commission: (1) temporarily suspended the proposed rule change (SR-PEARL-2021-57) and (2) instituted proceedings to determine whether to approve or disapprove the proposal.<sup>92</sup> On February 1,

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<sup>86</sup> See Securities Exchange Act Release No. 92644 (August 11, 2021), 86 FR 46055 (August 17, 2021) (SR-PEARL-2021-36). The Commission received one comment letter on that proposal. Comment for SR-PEARL-2021-36 can be found at: <https://www.sec.gov/comments/sr-pearl-2021-36/srpearl202136.htm>.

<sup>87</sup> See Securities Exchange Act Release No. 93162 (September 28, 2021), 86 FR 54739 (October 4, 2021) (SR-PEARL-2021-45).

<sup>88</sup> Comment on SR-PEARL-2021-45 can be found at: <https://www.sec.gov/comments/sr-pearl-2021-45/srpearl202145.htm>.

<sup>89</sup> See Securities Exchange Act Release No. 93639 (November 22, 2021), 86 FR 67758 (November 29, 2021).

<sup>90</sup> See text accompanying supra note 12.

<sup>91</sup> See Securities Exchange Act Release No. 93774 (December 14, 2021), 86 FR 71952 (December 20, 2021).

<sup>92</sup> See Securities Exchange Act Release No. 94088 (January 27, 2022), 87 FR 5901 (February 2, 2022).

2022, the Exchange withdrew SR-PEARL-2021-57 and filed the instant filing, which is substantially similar.

When exchanges file their proposed rule changes with the Commission, including fee filings like the Exchange’s present proposal, they are required to provide a statement supporting the proposal’s basis under the Act and the rules and regulations thereunder applicable to the exchange.<sup>93</sup> The instructions to Form 19b-4, on which exchanges file their proposed rule changes, specify that such statement “should be sufficiently detailed and specific to support a finding that the proposed rule change is consistent with [those] requirements.”<sup>94</sup>

Among other things, exchange proposed rule changes are subject to Section 6 of the Act, including Sections 6(b)(4), (5), and (8), which requires the rules of an exchange to: (1) provide for the equitable allocation of reasonable fees among members, issuers, and other persons using the exchange’s facilities;<sup>95</sup> (2) perfect the mechanism of a free and open market and a national market system, protect investors and the public interest, and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers;<sup>96</sup> and (3) not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.<sup>97</sup>

In temporarily suspending the Exchange’s fee change, the Commission intends to further consider whether the proposal to modify fees for certain connectivity options and implement a tiered pricing fee structure is consistent with the statutory requirements applicable to a national

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<sup>93</sup> See 17 CFR 240.19b-4 (Item 3 entitled “Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change”).

<sup>94</sup> Id.

<sup>95</sup> 15 U.S.C. 78f(b)(4).

<sup>96</sup> 15 U.S.C. 78f(b)(5).

<sup>97</sup> 15 U.S.C. 78f(b)(8).



securities exchange under the Act. In particular, the Commission will consider whether the proposed rule change satisfies the standards under the Act and the rules thereunder requiring, among other things, that an exchange's rules provide for the equitable allocation of reasonable fees among members, issuers, and other persons using its facilities; not permit unfair discrimination between customers, issuers, brokers or dealers; and do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.<sup>98</sup>

Therefore, the Commission finds that it is appropriate in the public interest, for the protection of investors, and otherwise in furtherance of the purposes of the Act, to temporarily suspend the proposed rule change.<sup>99</sup>

#### IV. Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change

The Commission is instituting proceedings pursuant to Sections 19(b)(3)(C)<sup>100</sup> and 19(b)(2)(B)<sup>101</sup> of the Act to determine whether the Exchange's proposed rule change should be approved or disapproved. Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described below, the Commission seeks and encourages interested persons

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<sup>98</sup> See 15 U.S.C. 78f(b)(4), (5), and (8), respectively.

<sup>99</sup> For purposes of temporarily suspending the proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>100</sup> 15 U.S.C. 78s(b)(3)(C). Once the Commission temporarily suspends a proposed rule change, Section 19(b)(3)(C) of the Act requires that the Commission institute proceedings under Section 19(b)(2)(B) to determine whether a proposed rule change should be approved or disapproved.

<sup>101</sup> 15 U.S.C. 78s(b)(2)(B).

to provide comments on the proposed rule change to inform the Commission's analysis of whether to approve or disapprove the proposed rule change.

Pursuant to Section 19(b)(2)(B) of the Act,<sup>102</sup> the Commission is providing notice of the grounds for possible disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of whether the Exchange has sufficiently demonstrated how the proposed rule change is consistent with Sections 6(b)(4),<sup>103</sup> 6(b)(5),<sup>104</sup> and 6(b)(8)<sup>105</sup> of the Act. Section 6(b)(4) of the Act requires that the rules of a national securities exchange provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities. Section 6(b)(5) of the Act requires that the rules of a national securities exchange be designed, among other things, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system and, in general, to protect investors and the public interest, and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers. Section 6(b)(8) of the Act requires that the rules of a national securities exchange not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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<sup>102</sup> 15 U.S.C. 78s(b)(2)(B). Section 19(b)(2)(B) of the Act also provides that proceedings to determine whether to disapprove a proposed rule change must be concluded within 180 days of the date of publication of notice of the filing of the proposed rule change. See id. The time for conclusion of the proceedings may be extended for up to 60 days if the Commission finds good cause for such extension and publishes its reasons for so finding, or if the exchange consents to the longer period. See id.

<sup>103</sup> 15 U.S.C. 78f(b)(4).

<sup>104</sup> 15 U.S.C. 78f(b)(5).

<sup>105</sup> 15 U.S.C. 78f(b)(8).

The Commission asks that commenters address the sufficiency of the Exchange’s statements in support of the proposal, in addition to any other comments they may wish to submit about the proposed rule change. In particular, the Commission seeks comment on the following aspects of the proposal and asks commenters to submit data where appropriate to support their views:

1. Cost Estimates and Allocation. The Exchange states that it is not asserting that the Proposed Access Fees are constrained by competitive forces, but rather set forth a “cost-plus model,” employing a “conservative methodology” that “strictly considers only those costs that are most clearly directly related to the provision and maintenance of 10Gb ULL connectivity to estimate such costs.”<sup>106</sup> Setting forth its costs in providing 10Gb ULL connectivity, and as summarized in greater detail above, the Exchange projects \$15.9 million in aggregate (between the Exchange and MIAX) annual estimated costs for 2021 as the sum of: (1) \$3.9 million in third-party expenses paid in total to Equinix (62% of the total applicable expense) for data center services; Zayo Group Holdings, for network services (62% of the total applicable expense); SFTI for connectivity support, Thompson Reuters, NYSE, Nasdaq, and Internap and others (75% of the total applicable expense) for content, connectivity services, and infrastructure services; and various other hardware and software providers (51% of the total applicable expense) supporting the production environment, and (2) \$12 million in internal expenses, allocated to (a) employee compensation and benefit costs (\$6.1 million, approximately 28% of the Exchange’s and MIAX’s total applicable employee compensation and benefits expense); (b)

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<sup>106</sup> See supra Section II.A.2.

depreciation and amortization (\$5.3 million, approximately 70% of the Exchange's and MIAX's total applicable depreciation and amortization expense); and (c) occupancy costs (\$0.6 million, approximately 53% of the Exchange's and MIAX's total applicable occupancy expense). Do commenters believe that the Exchange has provided sufficient detail about how it determined which costs are most clearly directly associated with providing and maintaining 10Gb ULL connectivity? The Exchange describes a "proprietary" process involving all Exchange department heads, including the finance department and numerous meetings between the Exchange's Chief Information Officer, Chief Financial Officer, Head of Strategic Planning and Operations, Chief Technology Officer, various members of the Legal Department, and other group leaders, but do not specify further what principles were applied in making these determinations or arriving at particular allocations. Do commenters believe further explanation is necessary? For employee compensation and benefit costs, for example, the Exchange calculated an allocation of employee time in several departments, including Technology, Back Office, Systems Operations, Networking, Business Strategy Development, Trade Operations, Finance, and Legal, but do not provide the job titles and salaries of persons whose time was accounted for, or explain the methodology used to determine how much of an employee's time is devoted to that specific activity. What are commenters' views on whether the Exchange has provided sufficient detail on the identity and nature of services provided by third parties? Across all of the Exchange's projected costs, what are commenters' views on whether the Exchange has provided sufficient detail on the elements that go into connectivity costs, including how shared costs are allocated and attributed to

connectivity expenses, to permit an independent review and assessment of the reasonableness of purported cost-based fees and the corresponding profit margin thereon? Should the Exchange be required to identify for what services or fees the remaining percentage of un-allocated expenses are attributable to (e.g., what services or fees are associated with the 30% of applicable depreciation and amortization expenses the Exchange does not allocate to the Proposed Access Fees)? Do commenters believe that the costs projected for 2021 are generally representative of expected costs going forward (to the extent commenters consider 2021 to be a typical or atypical year), or should an exchange present an estimated range of costs with an explanation of how profit margins could vary along the range of estimated costs? Should the Exchange use cost projections or actual costs estimated for 2021 in a filing made in 2022, or make cost projections for 2022?

2. Revenue Estimates and Profit Margin Range. The Exchange provides a single monthly revenue figure as the basis for calculating the profit margin of 21.3%. Do commenters believe this is reasonable? If not, why not? The Exchange states that their proposed fee structure is “designed to cover its costs with a limited return in excess of such costs,” and that “revenue and associated profit margin [] are not solely intended to cover the costs associated with providing access services subject to the Proposed Access Fees,” and believes that a 21.3% margin is a limited return over such costs.<sup>107</sup> The profit margin is also dependent on the accuracy of the cost projections which, if inflated (intentionally or unintentionally), may render the projected profit margin meaningless. The Exchange acknowledges that this margin

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<sup>107</sup> See supra Section II.A.2.

may fluctuate from month to month due to changes in the number of connections purchased, and that costs may increase. They also state that the number of connections has not materially changed over the prior months and so the months that the Exchange has used as a baseline to perform its assessment are representative of reasonably anticipated costs and expenses.<sup>108</sup> The Exchange does not account for the possibility of cost decreases, however. What are commenters' views on the extent to which actual costs (or revenues) deviate from projected costs (or revenues)? Do commenters believe that the Exchange's methodology for estimating the profit margin is reasonable? Should the Exchange provide a range of profit margins that they believe are reasonably possible, and the reasons therefor?

3. Reasonable Rate of Return. Do commenters agree with the Exchange that its expected 21.3% profit margin would constitute a reasonable rate of return over cost for 10GB ULL connectivity? If not, what would commenters consider to be a reasonable rate of return and/or what methodology would they consider to be appropriate for determining a reasonable rate of return? What are commenters' views regarding what factors should be considered in determining what constitutes a reasonable rate of return for 10Gb ULL connectivity fees? Do commenters believe it relevant to an assessment of reasonableness that the Exchange's proposed fees for 10Gb ULL connections, even at the highest tier, are lower than those of other options exchanges to which the Exchange has compared the Proposed Access Fees? Should an assessment of reasonable rate of return include consideration of factors other than costs; and if so, what factors should be considered, and why?

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See id.

4. Periodic Reevaluation. The Exchange has addressed whether it believes a material deviation from the anticipated profit margin would warrant the need to make a rule filing pursuant to Section 19(b) of the Act to increase or decrease the fees accordingly, stating that “[a]ny requirement that an exchange should conduct a periodic re-evaluation on a set timeline of its cost justification and amend its fees accordingly should be established by the Commission holistically, applied to all exchanges and not just through pending fee proposals, such as this filing,” and that “[i]n order to be fairly applied, such a mandate should be applied to existing access fees as well.”<sup>109</sup> In light of the impact that the number of subscribers has on connectivity profit margins, and the potential for costs to decrease (or increase) over time, what are commenters’ views on the need for exchanges to commit to reevaluate, on an ongoing and periodic basis, their cost-based connectivity fees to ensure that they stay in line with their stated profitability target and do not become unreasonable over time, for example, by failing to adjust for efficiency gains, cost increases or decreases, and changes in subscribers? How formal should that process be, how often should that reevaluation occur, and what metrics and thresholds should be considered? How soon after a new connectivity fee change is implemented should an exchange assess whether its subscriber estimates were accurate and at what threshold should an exchange commit to file a fee change if its estimates were inaccurate? Should an initial review take place within the first 30 days after a connectivity fee is implemented? 60 days? 90 days? Some other period?

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<sup>109</sup> See supra Section II.A.2.

5. Tiered Structure for 10Gb ULL Connections. The Exchange states that the proposed tiered fee structure is designed to decrease the monthly fees for those firms that connect to the Exchange as part of their best execution obligations and generally tend to send the least amount of orders and messages over those connections, because such firms generally only purchase a limited number of connections, and also “generally send fewer orders and messages over those connections, resulting in less strain on Exchange resources.”<sup>110</sup> According to the Exchange, 80% of firms have not experienced a fee increase as a result of the tiered structure. However, firms that purchase five or more connections will see a 30% increase in their fees for each connection above the fourth. Regarding these firms, the Exchange has not asserted that it is 30% more costly for the Exchange to offer such connections to these firms, but instead argues generally that these firms are “likely” to result in greater expenditure of Exchange resources and increased cost to the Exchange and that as the number of connections an entity has increases, certain other costs incurred by the Exchange that are correlated to, though not directly affected by, connection costs (e.g., storage costs, surveillance costs, service expenses) also increase.<sup>111</sup> Do commenters believe that the price differences between the tiers are supported by the Exchange’s assertions that it set the level of its proposed fees in a manner that it is equitable and not unfairly discriminatory? Do commenters believe the Exchange should demonstrate how the proposed tiered fee levels correlate with tiered costs (e.g., by providing cost information broken down by tier, messaging and order

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<sup>110</sup> See id.

<sup>111</sup> See id.



volumes through the additional 10Gb ULL connections by tier, and/or mid-month add/drop of connection rates by tier)? Do commenters believe that the Exchange should provide more detail about the costs that firms purchasing three or more or five or more 10Gb ULL connections impose on the Exchange, to permit an assessment of the Exchange’s statement that the Proposed Access Fees “do not depend on any distinction between Members and non-Members because they are solely determined by the individual Members’ or non-Members’ business needs and its impact on Exchange resources?”<sup>112</sup>

Under the Commission’s Rules of Practice, the “burden to demonstrate that a proposed rule change is consistent with the Exchange Act and the rules and regulations issued thereunder . . . is on the [SRO] that proposed the rule change.”<sup>113</sup> The description of a proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding,<sup>114</sup> and any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Act and the applicable rules and regulations.<sup>115</sup> Moreover, “unquestioning reliance” on an SRO’s representations in a proposed rule change would not be sufficient to justify Commission approval of a proposed rule change.<sup>116</sup>

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<sup>112</sup> See id.

<sup>113</sup> 17 CFR 201.700(b)(3).

<sup>114</sup> See id.

<sup>115</sup> See id.

<sup>116</sup> See Susquehanna Int’l Group, LLP v. Securities and Exchange Commission, 866 F.3d 442, 446-47 (D.C. Cir. 2017) (rejecting the Commission’s reliance on an SRO’s own determinations without sufficient evidence of the basis for such determinations).

The Commission believes it is appropriate to institute proceedings to allow for additional consideration and comment on the issues raised herein, including as to whether the proposal is consistent with the Act, any potential comments or supplemental information provided by the Exchange, and any additional independent analysis by the Commission.

V. Commission's Solicitation of Comments

The Commission requests written views, data, and arguments with respect to the concerns identified above as well as any other relevant concerns. In particular, the Commission invites the written views of interested persons concerning whether the proposal is consistent with Sections 6(b)(4), 6(b)(5), and 6(b)(8), or any other provision of the Act, or the rules and regulations thereunder. The Commission asks that commenters address the sufficiency and merit of the Exchange's statements in support of the proposal, in addition to any other comments they may wish to submit about the proposed rule change. Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.<sup>117</sup>

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's

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<sup>117</sup> 15 U.S.C. 78s(b)(2). Section 19(b)(2) of the Act grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by an SRO. See Securities Acts Amendments of 1975, Report of the Senate Committee on Banking, Housing and Urban Affairs to Accompany S. 249, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

submission must file that rebuttal by [insert date 35 days from publication in the Federal Register].

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-PEARL-2022-03 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 Number SR-PEARL-2022-03. 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. Persons submitting comments are cautioned that we do not redact or edit personal identifying

information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-PEARL-2022-03 and should be submitted on or before [insert date 21 days from publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from publication in the Federal Register].

VI. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(3)(C) of the Act,<sup>118</sup> that File Numbers SR-PEARL-2022-03 be, and hereby is, temporarily suspended. In addition, the Commission is instituting proceedings to determine whether the proposed rule change should be approved or disapproved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>119</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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<sup>118</sup> 15 U.S.C. 78s(b)(3)(C).

<sup>119</sup> 17 CFR 200.30-3(a)(12), (57) and (58).