



June 19, 2015

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 15-13 (“Notice”); Proposed Exemptions to the Trading Activity Fee (“TAF”) for Proprietary Trading Firms.

Dear Ms. Asquith,

The Security Traders Association (“STA”) is pleased to offer comment on FINRA Regulatory Notice 15-13 which proposes exemptions to the TAF for proprietary trading firms. The STA is comprised of 24 affiliate organizations¹ in North America, whose membership is comprised of individuals employed in the financial services industry. The STA relies on its Trading Issue Advisory Committees for input on its comment letters. For this particular comment letter the STA relied predominately on its Listed Options Committee which is comprised of liquidity providers, characterized as option market makers and proprietary trading firms,² and representatives from exchanges and retail brokerage firms.

STA believes that in the aftermath of the 2007 financial crisis certain regulatory actions have increased costs for all trading centers. In addition, there have been unique regulatory events with corresponding costs specific to liquidity providers in the listed options market with acute impacts to varying subsets.³ These regulatory costs, while not the only factor,

¹ STA is a trade organization founded in 1934 for individual professionals in the securities industry. STA is comprised of 24 Affiliate organizations with 4,200 individual professionals, most of who are engaged in the buying, selling and trading of securities. The STA is committed to promoting goodwill and fostering high standards of integrity in accord with the Association’s founding principle, Dictum Meum Pactum – “My Word is My Bond”

² These requirements are based largely on existing exchange definitions of proprietary trading firms. See, e.g., NYSE Rule 7410(p); CBOE Rule 3.6A, Interpretation .07

³ *Basel III Capital Rules and risk-weighted assets (“RWA”)* A sub-set of former and current listed option market makers are subsidiaries of U.S. banking organizations that are required to maintain capital based, in part, on their RWA adopted under Basel III Capital Rules. Changes in calculating RWA have increased the capital costs of maintaining portfolios of hedged transactions in facilitating investor trades.

Options Clearing Corporation, (“OCC”); Systemically Important Financial Market Utility, (“SIFMU”) in response to being designated a SIFMU in March 2014; the OCC was required, among other things, to increase its minimum regulatory capital. In February 2015, the OCC filed its capital raising plan which is a combination of capital contribution from the options exchanges who are shareholders in OCC with commitments from them for additional capital. In return, OCC will pay out dividends to these shareholders which will be financed through higher clearing rates. Firms, many of whom are market makers, who are not able to be shareholders in OCC, are not able to offset their costs.

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have contributed greatly to the decrease in the overall number of liquidity providers and their make-up as measured by percentage changes in market makers and proprietary trading firms.

Furthermore, there exists foreseeable regulatory events and associated costs that if implemented could exacerbate the trend toward fewer liquidity providers from both of these groups. The Notice identifies one such event: the Securities and Exchange Commission (“SEC”) proposed amendments to Rule 15b9-1 under the Securities Exchange Act of 1934 filed on March 25, 2015 (“SEC Amendment”).

As explained in the Notice, the SEC Amendment:

“If adopted, the amendments generally would require a proprietary trading firm relying on the current exemption to register with FINRA if the firm continues to engage in over-the-counter trading or trading on an exchange of which it is not a member. FINRA membership would, among other things, subject these firms to the existing FINRA fee structure, including the TAF”.

In addition, the Notice states that it has been the assessment of the SEC that having proprietary firms as FINRA members will:

“...lead to more comprehensive surveillance and uniform regulation of trading activity by proprietary trading firms. As a result, investors and intermediaries would likely benefit from the increased regulatory oversight.”

Regarding anticipated reactions from those proprietary firms affected should the SEC Amendment and FINRA Notice be adopted, FINRA states such firms may:

- Alter their activities;
- Choose to exit from or limit their trading activities to exchanges of which they are members;
- Elect to become a member of every SRO where they transact directly or indirectly;
- Become a member of FINRA.

Today there are over 800,000 option series on approximately 4,700 underlying equities, ETFs, and indices. Each option series requires a two-sided quote that is often attributed to a liquidity provider. These conditions create a regime of very low amounts of investor



to investor trading, which in turn requires liquidity providers to buy from or sell to the investor or customer who is seeking liquidity. In 2013, approximately 85% of all customer trades were facilitated with a listed options market maker on the other side.⁴ Given the unique role that market makers and proprietary traders perform as liquidity providers in the listed options market, the STA is concerned this market and the investors it serves will be harmed if the SEC's Amendment is approved in its current draft and the regulatory costs of FINRA membership remain unchanged. Therefore, the STA supports FINRA's Notice to exclude from the TAF transactions by a proprietary trading firm on exchanges of which the firm is a member, although we feel more cost reductions in the form lower TAF rates are needed. We believe a lower TAF will better improve the likelihood that the SEC's desired goal of a more comprehensive surveillance and uniform regulation of trading activity by proprietary trading firms is achieved. In addition, they would ensure that FINRA fulfills its statutory obligation that its rules provide for the equitable allocation of reasonable dues, fees and other charges among its members.⁵ Finally, revenue generated by the TAF from proprietary firms should result in lower unit costs in areas where the fixed costs associated with providing oversight is shared by all FINRA members.

STA is concerned that should there be an over-collection from FINRA of membership fees, attempts to rectify membership fee levels for this group will be too late to offset the permanent harm to the approximately eighty-five (85) non-FINRA member broker dealers who meet the definition of proprietary trading firms as identified in the Notice. We believe that the cost of entry to liquidity providers is so high that any exit of an existing participant will be permanent regardless of any regulatory response associated with the TAF.

To be clear, the STA believes that regulatory authorities require efficient means, processes and rules in order to discharge their responsibilities properly and that adequate funding is needed in order to achieve these goals. However, in this situation we believe that should FINRA identify additional cuts in the TAF for proprietary firms, it can achieve the SEC's goal that registered broker dealers be members of a national securities association and avoid doing permanent harm to liquidity providers without causing itself long-term monetary loss. FINRA is currently the only registered national securities

⁴ [Letter from Craig S. Donahue, Executive Chairman, OCC to Ms Constance M. Horsley Assistant Director, Board of Governors of the Federal Reserve System January 6, 2015](#)

⁵ Securities Exchange Act of 1934, Section 15A(b)(5)



association and it has the ability to raise the TAF at a future date to a level which may more accurately reflect its costs. Since July 2011, the SEC has approved three (3) TAF

rate increases for sales of covered equity securities filed by FINRA.⁶ As such, we recommend that FINRA err on the side of implementing a TAF structure which best achieves the SEC's goals and does no permanent harm to proprietary firms. Specifically, we recommend that FINRA reduce the TAF rates for equity transactions by proprietary firms on over-the-counter and exchanges of which they are not a member.

Conclusion:

The STA compliments FINRA for analyzing the potential impact of the TAF to proprietary firms and for acknowledging that such a regime could result in a:

“significant TAF obligation for these firms that may be disproportionate to FINRA’s anticipated costs associated with the financial monitoring and trading surveillance of these firms, in large part because these firms do not have customers”.

STA encourages FINRA to continue its analysis and recommends a reduction in the TAF be considered in conjunction with exempting certain transactions.

We look forward to working with FINRA and the Commission on this matter and any other market structure issues that may be considered.

Sincerely,

A handwritten signature in black ink, appearing to read "Rory O'Kane".

Rory O’Kane, Chairman of the Board

A handwritten signature in black ink, appearing to read "James Toes".

James Toes, President & CEO

CC:

Mary Jo White, Chair, Securities and Exchange Commission

Luis A. Aguilar, Commissioner, Securities and Exchange Commission

Daniel M. Gallagher, Commissioner, Securities and Exchange Commission

Kara M. Stein, Commissioner, Securities and Exchange Commission

Michael S. Piwowar, Commissioner, Securities and Exchange Commission

Stephen Luparello, Director, Division of Trading & Markets, Securities and Exchange Commission

⁶ FINRA Regulatory Notices; 11-27 effective July 1, 2011; 12-06 effective March 1, 2012; 12-31 effective July 1, 2012