



SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-97798; File No. SR-FINRA-2023-009]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend FINRA’s Trading Activity Fee

June 26, 2023.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 23, 2023, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as “establishing or changing a due, fee or other charge” under Section 19(b)(3)(A)(ii) of the Act³ and Rule 19b-4(f)(2) thereunder,⁴ which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

FINRA is proposing to amend Section 1(b) of Schedule A to the FINRA By-Laws to exempt from the Trading Activity Fee (“TAF”) any transaction by a proprietary trading firm that occurs on an exchange of which the proprietary trading firm is a member.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(ii).

⁴ 17 CFR 240.19b-4(f)(2).

The text of the proposed rule change is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

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

In its filing with the Commission, FINRA 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 below. FINRA 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

As a general matter, the most significant sources of FINRA’s funding are three core regulatory fees: the Gross Income Assessment; the TAF; and the Personnel Assessment.⁵ These regulatory fees are used to substantially fund FINRA’s regulatory activities, including examinations, financial monitoring, and FINRA’s policymaking, rulemaking, and enforcement activities.⁶ As discussed in FINRA’s prior Regulatory Notices, FINRA is proposing an exemption from one of FINRA’s regulatory fees—the TAF—for transactions by “proprietary trading firms,” which FINRA understands would include firms currently operating in compliance with existing SEA Rule 15b9-1 and that would be required to become FINRA members in light of the SEC’s proposed amendments to SEA Rule 15b9-1, as further discussed below.⁷ In this

⁵ See FINRA By-Laws, Schedule A, Section 1.

⁶ See Securities Exchange Act Release No. 90176 (October 14, 2020), 85 FR 66592 (October 20, 2020) (Notice of Filing and Immediate Effectiveness of File No. SR-FINRA-2020-032).

⁷ FINRA believes that proprietary trading firms currently operating in compliance with existing SEA Rule 15b9-1 that would join FINRA due to the SEC’s proposed amendments to SEA Rule 15b9-1 would meet the proposed definition of “proprietary trading firm” and would qualify for the proposed exemption (assuming no changes to their business models that would alter their eligibility), as well as current FINRA members that meet the proposed definition. See also infra notes 37 and 39.

regard, FINRA proposes to define “proprietary trading firm” as a member that (i) trades exclusively its own capital; (ii) does not have “customers,” which shall include any person, other than a broker or dealer, with whom the member engages, or within the past six months has engaged, in securities activities; and (iii) conducts all trading through the firm’s accounts by traders that are owners of, employees of, or contractors to the firm, or employees of an affiliate of the firm.

Under the Exchange Act, a registered broker-dealer must become a member of a national securities association (currently, FINRA is the sole national securities association) unless the broker-dealer effects transactions in securities solely on a national securities exchange of which it is a member.⁸ SEA Rule 15b9-1 provides an exemption to the requirement that a broker-dealer become a member of a national securities association if the broker-dealer (i) is a member of a national securities exchange, (ii) carries no customer accounts, and (iii) has annual gross income derived from purchases and sales of securities otherwise than on a national securities exchange of which it is a member in an amount no greater than \$1,000 (the \$1,000 limitation is known as the “de minimis allowance”).⁹ The \$1,000 gross income limitation does not apply to income derived from transactions for the dealer’s own account with or through another registered broker or dealer. Thus, for example, income derived from over-the-counter trades through an alternative trading system does not count toward the \$1,000 threshold. On July 29, 2022, the SEC proposed amendments to SEA Rule 15b9-1 to narrow the exemption from association membership.¹⁰

As discussed in the Proposing Release, the securities markets have evolved dramatically since the adoption of SEA Rule 15b9-1 and, today, the de minimis allowance is relied upon by

⁸ 15 U.S.C. 78q(b)(8).

⁹ 17 CFR 240.15b9-1.

¹⁰ See Securities Exchange Act Release No. 95388 (July 29, 2022), 87 FR 49930 (August 12, 2022) (“Proposing Release”). The SEC previously proposed to amend SEA Rule 15b9-1 in 2015. See Securities Exchange Act Release No. 74581 (March 25, 2015), 80 FR 18036 (April 2, 2015) (File No. S7-05-15) (“2015 Proposal”).

proprietary trading firms that, in some cases, engage in substantial cross-exchange and off-exchange trading activity, yet they are not subject to FINRA oversight.¹¹ The SEC therefore proposed to eliminate the de minimis allowance and instead provide that a broker-dealer may effect transactions otherwise than on a national securities exchange of which it is a member in only two narrow circumstances: (i) transactions that result solely from orders routed by the exchange of which the firm is a member to prevent trade-throughs consistent with Rule 611 of Regulation NMS or the Options Order Protection and Locked/Cross Market Plan; and (ii) transactions that are solely for the purpose of executing the stock leg of a stock-option order, subject to specified conditions.¹²

The SEC estimates that the proposed amendments to SEA Rule 15b9-1 would impact approximately 65 broker dealers that are not currently FINRA members.¹³ Thus, if adopted, the proposed amendments to SEA Rule 15b9-1 would require additional broker-dealers to become a member of FINRA (unless they limit their activities to the contours of the amended exemption from membership in a national securities association), and such member firms would become subject to FINRA regulatory fees, among other requirements.

Proprietary trading firms that potentially could become members of FINRA have expressed concern about the TAF in particular. FINRA notes that there currently are several exemptions from the TAF, including for transactions by floor brokers and for market making transactions subject to Section 11(a) of the Act.¹⁴ However, proprietary trading firms do not function as floor brokers and may only be registered market makers in some, but not all, of the securities that they trade. As a result, if the proposed amendments to SEA Rule 15b9-1 are adopted by the SEC, those proprietary trading firms that would become FINRA members would be subject to the TAF for much of their trading activity, including transactions on exchanges of

¹¹ See Proposing Release, supra note 10, 87 FR 49930, 49931.

¹² See Proposing Release, supra note 10.

¹³ See Proposing Release, supra note 10, 87 FR 49930, 49954.

¹⁴ FINRA By-Laws, Schedule A, Section 1(b)(2)(F) and (G).

which they are a member. The SEC noted specifically when proposing the amendments to SEA Rule 15b9-1 that FINRA may want to “evaluate its TAF to ensure that it appropriately reflects the activities of, and regulatory responsibilities towards, broker-dealer proprietary trading firms that would be required to join FINRA if the proposed amendments to [SEA] Rule 15b9-1 are adopted.”¹⁵ In light of the SEC’s proposed amendments to SEA Rule 15b9-1, FINRA has considered the application and potential impact of the TAF to proprietary trading firms and has concluded that it is appropriate to provide an exemption from the TAF for all proprietary trading firms for transactions executed on an exchange of which the proprietary trading firm is a member.¹⁶ As FINRA regularly evaluates its fees to ensure appropriate funding for its regulatory mission, FINRA expects to evaluate the TAF—including with respect to proprietary trading firms—more broadly in the future.

FINRA has filed the proposed rule change for immediate effectiveness. FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice. The implementation date will be no earlier than the date of adoption of the Commission’s amendments to SEA Rule 15b9-1 eliminating the de minimis allowance and no later than the effective date of any such amendments.¹⁷

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(5) of the Act,¹⁸ which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and

¹⁵ See Proposing Release, supra note 10, 87 FR 49930, 49943. In the 2015 Proposal, the SEC made a similar comment: “FINRA may need to consider reassessing the structure of its fees, including its Trading Activity Fee, in order to assure that it is fairly and equitably applied to many of the [non-FINRA member firms] that, as a result of the amendments to [SEA] Rule 15b9-1, may join FINRA.” See 2015 Proposal, supra note 10, 80 FR 18036, 18044 n.95.

¹⁶ FINRA notes that, in addition to any other applicable FINRA fees, proprietary trading firms would incur a TAF obligation on transactions executed otherwise than on an exchange and on transactions executed on an exchange of which the firm is not a member. These transactions would be subject to the TAF under the existing fee structure and at existing rates.

¹⁷ See supra note 10.

¹⁸ 15 U.S.C. 78o-3(b)(5).

other persons using any facility or system that FINRA operates or controls. FINRA believes that the proposed TAF exemption will result in an equitable allocation of fees to proprietary trading firms in accord with their activities and the regulatory resources to oversee them with respect to their trading activity on an exchange of which they are a member.

FINRA believes it is reasonable to propose this amendment in view of the fact that regulatory costs for firms that do not have customers are expected to be less than the cost to oversee the activity of firms with customers. FINRA also believes that it is appropriate to proceed with an exemption for proprietary trading firms with respect to their transactions on an exchange of which they are a member because FINRA anticipates that regulatory costs largely will relate to overseeing such firms' activity over the counter or across exchanges.

Under the proposal, proprietary trading firms (as defined in the proposed rule) that are current FINRA members would experience a reduction in their TAF assessments to the extent they conduct non-market making transactions executed on exchanges of which they are members. Proprietary trading firms that become FINRA members would incur a smaller TAF assessment than they otherwise would pay absent the proposal. Finally, FINRA believes that the proposal is reasonable in that the proposed exemption is clear, simple, and cost effective for firms to implement.

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

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

Economic Impact Assessment

1. Regulatory Need

As discussed above, the SEC is proposing to amend SEA Rule 15b9-1 to narrow the scope of the exemption from FINRA membership. The proposed amendments to SEA Rule

15b9-1, if adopted, would generally require proprietary trading firms to become FINRA members if they engage in trading otherwise than on exchanges of which they are members.¹⁹

2. Economic Baseline

The economic baseline for FINRA's proposed rule change consists of the regulatory framework under the SEC's proposed amendments to SEA Rule 15b9-1, if adopted, as well as FINRA's current TAF. In the Proposing Release, the SEC notes that, under the amended rule, a non-FINRA member firm that trades equities, options or fixed income securities off-exchange, or on exchanges of which it is not a member, can comply in four ways. One option is to join FINRA. The other options are to cease any off-exchange trading and either trade solely upon the exchanges of which the firm is already a member, or join additional exchanges, or cease trading securities altogether.²⁰ The discussion below briefly considers the benefits, costs and other economic impacts of the SEC proposed amendments to SEA Rule 15b9-1, as discussed by the SEC, to facilitate the consideration of the economic impacts of FINRA's proposed rule change to the TAF.

FINRA expects that some firms that are not currently FINRA members will apply for FINRA membership due to the SEC's modifications to SEA Rule 15b9-1, if adopted. These firms would maintain the ability to effect securities transactions on the same on and off exchange venues on which they currently effect such transactions. These firms would incur the one-time and ongoing costs of FINRA membership, including the TAF and other regulatory fees. The TAF would increase these firms' variable costs to trade, and the SEC notes that this may lead certain firms to reduce their trading both on-exchange and off-exchange.²¹ These firms may, however, mitigate some of the disincentive that comes from being liable for the TAF for trading on exchanges by registering as market makers.²² Membership by these firms in FINRA would

¹⁹ See *supra* notes 10-12 and accompanying text.

²⁰ See Proposing Release, *supra* note 10, 87 FR 49930, 49958.

²¹ See Proposing Release, *supra* note 10, 87 FR 49930, 49958-60, 49965.

²² See Proposing Release, *supra* note 10, 87 FR 49930, 49960, 49965.

provide more stable and uniform FINRA surveillance of off-exchange and cross-exchange trading activity than currently occurs.²³

Other non-FINRA member firms may choose to cease their off-exchange activity rather than join FINRA. Some of these firms may adjust their business models to trade solely upon the exchanges of which they are already a member or join additional exchanges upon which they wish to trade. However, since these firms may currently trade on exchanges of which they are not members, they may also cease trading on some of those exchanges.²⁴

The SEC also discusses how the changes non-FINRA member firms make to their business models to comply with the proposed amendments to SEA Rule 15b9-1 may affect other activities, including competition in the equity and U.S. Treasury securities markets, particularly for off-exchange liquidity provision.²⁵ As discussed above, non-FINRA member firms that join FINRA may reduce trading off-exchange and those that do not join FINRA will cease trading off-exchange, with similar impacts on their provision of off-exchange liquidity. Non-FINRA member firms may also reduce trading and liquidity provision on exchanges, whether or not they join FINRA.²⁶ A loss in liquidity provision may impose costs on investors in the form of higher trading costs than they would otherwise realize.²⁷ However, current member firms may increase their activity and offset some of these impacts, both on and off-exchange.²⁸ The ultimate impact on liquidity, execution quality and trading volume for particular assets and trading venues is generally not determinate. Regarding the overall provision of liquidity to financial markets, however, the SEC argues that the effect of the proposed rule is not likely to be significant.²⁹

²³ See Proposing Release, supra note 10, 87 FR 49930, 49962.

²⁴ See Proposing Release, supra note 10, 87 FR 49930, 49967.

²⁵ See Proposing Release, supra note 10, 87 FR 49930, 49958.

²⁶ See Proposing Release, supra note 10, 87 FR 49930, 49959-60.

²⁷ See Proposing Release, supra note 10, 87 FR 49930, 49959. The SEC also states that the removal of liquidity from the market could either improve or degrade execution quality on off-exchange markets and reduced liquidity on exchanges can result in higher spreads and increased liquidity. Id. at 49960.

²⁸ See Proposing Release, supra note 10, 87 FR 49930, 49960.

²⁹ See supra note 28.

Current FINRA members, including proprietary trading firms, would not be directly affected by the SEC proposal.³⁰ However, to the extent that member firms currently compete with non-member firms that must become FINRA members or change their historical trading activities to avoid FINRA membership, the current members may benefit from having more uniform regulatory requirements among similarly situated competitors.

The SEC has estimated that there are approximately 65 broker-dealers registered with the Commission and exchange members that are not FINRA members. Each of these non-FINRA member firms will assess the costs and benefits of the options permitted by the amendments the SEC may make to SEA Rule 15b9-1. FINRA cannot determine the number of firms that may choose to become FINRA members or the likelihood or magnitude of any anticipated changes in trading behavior because of the proposed SEC rule amendments.³¹

FINRA estimates that approximately 66 member firms derive all or most of their revenue from proprietary trading, although not all of these firms would meet the proposed definition of “proprietary trading firm” based on their current business models.³² FINRA understands that, of the 66 firms that clear their own trades, the TAF accounts for over 85% of the regulatory fees paid by these firms (GIA, PA and TAF). However, most of the 66 firms do not clear their own trades and so do not pay TAF directly to FINRA.³³ Whether these firms conduct trades subject to TAF and whether they reimburse their clearing firm for the TAF, is not known to FINRA. Overall, between 2015 and 2022, TAF as a proportion of regulatory fees received by FINRA ranged from 41% to 56%. For the member firms that are proprietary trading firms and conduct

³⁰ See Proposing Release, *supra* note 10, 87 FR 49930, 49963.

³¹ FINRA notes that the SEC Proposal also discusses difficulties related to predicting changes in trading behavior and associated competitive impacts. See Proposing Release, *supra* note 10, 87 FR 49930, 49960.

³² Some of these 66 member firms may need to adjust their business models if they seek to qualify for the proposed TAF exemption. Whether these firms would eliminate disqualifying activity, move it into a separate entity or decline to take the TAF exemption depends on the value of this activity and the extent to which the loss of scale economies in conducting the activity in a separate entity would affect the cost.

³³ See Trading Activity Fee Frequently Asked Questions, <https://www.finra.org/rules-guidance/guidance/faqs/trading-activity-fee> (“Data should be submitted as monthly aggregates at the clearing firm level” A100.6).

trades subject to TAF, this may be a closer approximation to the maximum share of their regulatory fees that would be subject to the proposed TAF exemption.

3. Economic Impacts

FINRA is proposing to amend the TAF to exempt all transactions by a FINRA member proprietary trading firm executed on an exchange of which it is a member.³⁴ The proposed rule change would directly impact member proprietary trading firms by providing them an exemption from the TAF for such transactions. These member proprietary trading firms include current FINRA members as well as those that would join FINRA due to the SEC's proposed amendments to SEA Rule 15b9-1. The FINRA proposed rule change may also impact the number of non-member proprietary trading firms that choose to apply for FINRA membership rather than use one of the other options for compliance (as described above). All comparisons below are relative to the baseline, and therefore assume that SEA Rule 15b9-1 is amended as proposed and that, notionally, firms have adjusted their business conduct taking into account the SEC proposed rule and market conditions, as described above.

a. Anticipated Benefits

FINRA believes that the proposed TAF exemption is clear and simple for firms to implement. In addition, the proposed TAF exemption will likely dampen potential competitive effects and other market impacts as participants determine how to respond to proprietary trading firms' change in trading behaviors in response to the amendments to SEA Rule 15b9-1, while continuing to assess fees in a manner that is fair, reasonable, and equitably allocated among FINRA member firms. FINRA anticipates that, by reducing the fees associated with FINRA membership, the proposed TAF exemption may result in more proprietary trading firms joining FINRA. FINRA membership would allow these firms increased flexibility in where and how they trade.

³⁴ As noted above, the TAF currently provides an exemption for proprietary transactions by a member firm effected on an exchange of which it is a member in its capacity as a specialist or market maker in the security on that exchange.

Proprietary trading firms that are current FINRA members would experience a reduction in their TAF assessments to the extent they conduct non-market making transactions executed on exchanges of which they are members. Under the proposed TAF exemption, proprietary trading firms that become FINRA members would incur a smaller TAF assessment than they otherwise would pay absent the proposal. FINRA cannot determine the number of firms for which the proposed TAF exemption will have an impact on their determination of whether to become FINRA members and the likelihood or magnitude of any anticipated changes in trading behavior. There is significant diversity in the business models of proprietary trading firms. FINRA expects that the impacts of the exemption would depend on the level of trading activities proprietary trading firms conduct other than on the exchanges of which they are members. The impacts may also vary with the proportion of TAF to their overall FINRA membership costs. When TAF is expected to be a significant component of their membership costs, the proposed exemption is more likely to affect the firm's decision to become a FINRA member under the baseline.

b. Anticipated Costs

As discussed above, FINRA anticipates that the proposed TAF exemption may increase the number of proprietary trading firms that choose to become FINRA members relative to the baseline. The costs to these firms, like the benefits to these firms discussed above, are qualitatively the same as those incurred by proprietary trading firms that would choose to become FINRA members absent the proposed TAF exemption. These firms presumably choose to become FINRA members because the overall financial outcome is superior to that which would occur without joining FINRA and complying with the SEC proposed rule by restricting their trades to exchanges of which they are members.

4. Other Economic Effects

Effects on Trading Activities

Proprietary trading firms that are current FINRA members may alter their trading strategies to take advantage of the proposed TAF exemption, which may impact the amount and

allocation of trading activity among exchange and off-exchange trading venues from the baseline. Likewise, the existence of the TAF exemption may impact non-FINRA member firms' decision whether to become FINRA members, and thus also may impact the amount and allocation of trading activity among exchange and off-exchange trading venues from the baseline.

These potential changes in trading activity of proprietary trading firms may affect liquidity, execution quality and trading volume on the various trading venues. However, the extent and direction of the effect is generally not determinate and depends on how other market participants, including non-proprietary trading firms, respond to proprietary firms' actions.³⁵ To the extent the TAF exemption dampens a decrease in liquidity that may otherwise result as trading firms adjust to the amendments to SEA Rule 15b9-1, such an impact could help improve outcomes for investors seeking to trade, including lowering transaction costs or providing greater immediacy in trading relative to the baseline.

Effects on Competition

FINRA members that are proprietary trading firms may compete to provide liquidity with other FINRA members. Since the proposed TAF exemption is only available for proprietary trading firms, it could provide those firms with a competitive advantage over other members that engage in similar trading activity but do not qualify as proprietary trading firms by changing the relative costs of trading. However, this advantage would not be greater than what non-FINRA member proprietary trading firms currently experience (prior to the potential amendments of SEA Rule 15b9-1).

In addition, to the extent the proposed rule change leads to more proprietary trading firms joining FINRA, the proposed rule change may increase competition by having a more level playing field in terms of the costs associated with FINRA membership and regulatory

³⁵ See Proposing Release, supra note 10, 87 FR 49930, 49959.

requirements. As discussed in the SEC Proposal, competition in liquidity provision may be distorted by inequalities in regulatory requirements.³⁶ With more uniform regulatory requirements and oversight due to the potential increase in FINRA membership, proprietary trading firms could compete more equitably to supply liquidity both on and off-exchange.

5. Alternatives Considered

FINRA considered alternatives to the exemption proposed in this proposed rule change. FINRA believes that the proposed TAF exemption is preferable to an exemption from other types of fees and is directly related to the impacts on the provision of liquidity that the SEC discusses in its proposal.

FINRA also considered other alternative changes to the TAF, including adjusting the overall rate of the TAF or implementing a tiered TAF structure based on trading activity or providing caps. However, such alternatives could likely be more costly to implement for both the affected firms and FINRA, compared to the proposed TAF exemption. Accordingly, FINRA believes that the simple structure in this proposed rule change would be more cost effective to implement. FINRA will have more information about the total fees paid by proprietary trading firms, and their impact on FINRA's regulatory programs and fees once these firms become FINRA members.

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

Following the SEC's 2015 Proposal to amend SEA Rule 15b9-1, FINRA published Regulatory Notice 15-13 to solicit comment on a proposal to exclude from FINRA's TAF transactions by a proprietary trading firm on exchanges of which the firm is a member.³⁷ Four comment letters were received in response to the 2015 Notice.³⁸ Following the SEC's re-

³⁶ See Proposing Release, supra note 10, 87 FR 49930, 49960.

³⁷ See Regulatory Notice 15-13 (May 2015) ("2015 Notice").

³⁸ Letter from Mary Ann Burns, Chief Operating Officer, FIA Principal Traders Group ("FIA PTG"), to Marcia E. Asquith, Corporate Secretary, FINRA, dated June 19, 2015 ("FIA PTG 2015 Letter"); Letter from Adam Nunes, Hudson River Trading LLC ("HRT"), to Marcia E. Asquith, Corporate Secretary,

proposal of amendments to SEA Rule 15b9-1 in December 2022, FINRA re-opened the comment period for Regulatory Notice 15-13 by publishing Regulatory Notice 22-30.³⁹ Four additional comment letters were received in response to the 2022 Notice.⁴⁰ A copy of both Regulatory Notices are available on FINRA’s website at <http://www.finra.org>. Copies of the comment letters received in response to both Regulatory Notices are also available on FINRA’s website.

FINRA received four generally supportive comment letters in response to Regulatory Notice 15-13.⁴¹ All of these commenters also suggested expanding the proposed TAF exemption to cover additional proprietary trades. FINRA received three supportive⁴² and one unsupportive⁴³ comment letter in response to Regulatory Notice 22-30.

Supportive Comments

The FIA PTG 2023 Letter, HRT 2023 Letter, and Group One Letter stated that the proposed TAF exemption would help address the significant increase in costs that affected firms would otherwise face in light of the SEC’s proposed amendments. HRT and FIA PTG further stated that the proposed exemption from TAF appropriately recognizes the differences in the activities between proprietary trading businesses and customer businesses, and the

FINRA, dated June 19, 2015 (“HRT 2015 Letter”); Letter from Rory O’Kane, Chairman of the Board & James Toes, President and CEO, Security Traders Association (“STA”), to Marcia E. Asquith, Corporate Secretary, FINRA, dated June 19, 2015 (“STA Letter”); and Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association (“SIFMA”), to Marcia E. Asquith, Corporate Secretary, FINRA, dated June 22, 2015 (“SIFMA Letter”).

³⁹ See Regulatory Notice 22-30 (December 2022) (“2022 Notice”).

⁴⁰ Letter from Adam Nunes, Hudson River Trading LLC, to Jennifer Piorko Mitchell, Office of the Corporate Secretary, FINRA, dated February 13, 2023 (“HRT 2023 Letter”); Letter from Joanna Mallers, Secretary, FIA PTG, to Jennifer Piorko Mitchell, Office of Corporate Secretary, FINRA, dated March 8, 2023 (“FIA PTG 2023 Letter”); Letter from John Kinahan, Chief Executive Officer, Group One Trading, LP (“Group One”), to Jennifer Piorko Mitchell, Office of Corporate Secretary, FINRA, dated March 15, 2023 (“Group One Letter”); and Letter from University of Pittsburgh, School of Law (“Pittsburgh University”) to Jennifer Piorko Mitchell, Office of Corporate Secretary, FINRA, dated March 17, 2023 (“University of Pittsburgh Letter”).

⁴¹ See FIA PTG 2015 Letter; HRT 2015 Letter; SIFMA Letter; and STA Letter.

⁴² See FIA PTG 2023 Letter; Group One Letter; and HRT 2023 Letter.

⁴³ See University of Pittsburgh Letter.

accompanying costs related to regulating each type of business.⁴⁴ Group One added that implementing the proposed TAF exemption would support the ability of proprietary trading firms to continue to provide liquidity in the least disruptive manner possible.⁴⁵ HRT, FIA PTG, and Group One also asserted that implementing the TAF exemption would achieve an equitable allocation of fees and be in line with FINRA’s actual cost of regulating its members.⁴⁶ SIFMA also generally supported the proposed TAF exemption and stated that FINRA should not assess TAF on any principal transactions executed on exchanges of which the firm is a member, regardless of the type of firm.⁴⁷

Requests for Modifications

The FIA PTG 2015 Letter and SIFMA Letter requested that the proposed TAF exemption be broadened to include all principal trades done on an exchange of which a firm is a member, rather than just trades by proprietary trading firms.⁴⁸ Similarly, STA recommended 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.”⁴⁹

HRT proposed that all principal trades executed on any exchange be exempt from the TAF, adding that “off-exchange trades, as well as Agency and Riskless Principal trades executed

⁴⁴ See HRT 2023 Letter, at 1-2; FIA PTG 2023 Letter.

⁴⁵ See Group One Letter, at 1.

⁴⁶ See HRT 2023 Letter; FIA PTG 2023 Letter; and Group One Letter.

⁴⁷ See SIFMA Letter, at 2.

⁴⁸ Some comments also addressed the potential restructuring of the TAF as well as issues related to other FINRA fees. For example, STA suggested that FINRA reduce the current TAF rate for equity securities and, in particular, consider reducing the rate for over-the-counter and exchange trades by proprietary trading firms. SIFMA requested that FINRA review its fees more broadly and provide more transparency into how it uses and allocates the revenues it receives from fees and other sources of income. While these comments are not germane to the instant proposal—which seeks to provide an exemption from the TAF for a proprietary trading firm for transactions on an exchange of which it is a member—FINRA notes that it reviews its revenues as part of its budgeting process and revises fees as appropriate, both their application and their rates. In this regard, on October 14, 2020, FINRA amended various regulatory fees to increase the revenues that FINRA, as a not-for-profit self-regulatory organization, relies upon to fund its regulatory mission. The proposed fee increases were designed to better align FINRA’s revenues with its costs while preserving the existing equitable allocation of fees among FINRA members. See Securities Exchange Act Release No. 90176 (October 14, 2020), 85 FR 66592 (October 20, 2020) (Notice of Filing and Immediate Effectiveness of File No. SR-FINRA-2020-032).

⁴⁹ See STA Letter, at 4.

on an exchange, should continue to be charged the TAF.”⁵⁰ HRT stated that, as proposed, the TAF exemption may discourage firms from engaging in customer-based business⁵¹ or, alternatively, could result in such firms operating multiple broker-dealers to avoid the proprietary firm business incurring a TAF obligation on exempt exchange transactions.⁵²

As discussed above, FINRA believes that it is appropriate to proceed with an exemption from TAF for proprietary trading firms with respect to their transactions on an exchange of which they are a member because FINRA anticipates that regulatory costs largely will relate to overseeing such firms’ activity over the counter or across exchanges.

The FIA PTG 2015 Letter requested that, should the TAF exemption be limited to “proprietary trading firms” as proposed, FINRA provide guidance regarding the scope of the term “proprietary trading firm” to clarify: (i) the scope of the term “customer” for purposes of the exemption, and (ii) the requirement that traders be owners of, employees of, or contractors to the firm. Specifically, the FIA PTG 2015 Letter requested that FINRA clarify that the criteria “does not have customers” only applies to customers that are engaged in transactions in securities that are subject to the TAF, and not to “non-securities transactions, fixed-income transactions, and other businesses such as stock-lending and licensing of technology.”⁵³ FIA PTG also asked that FINRA specify what time period is relevant for purposes of determining whether a firm is engaged in a customer business.⁵⁴ Further, FIA PTG requested that FINRA clarify that traders or other associated persons could be employed by an affiliate of the firm (rather than firm itself) without losing the ability to rely on the proposed exemption.⁵⁵ FIA PTG asserted that such employment arrangements are “a common structure” for such firms.⁵⁶

⁵⁰ See HRT 2015 Letter, at 2.

⁵¹ See *supra* note 50.

⁵² See *supra* note 50; see also FIA PTG 2015 Letter, at 3.

⁵³ See FIA PTG 2015 Letter, at 4.

⁵⁴ See *supra* note 53.

⁵⁵ See *supra* note 53, at 5.

⁵⁶ See *supra* note 53, at 5.

In response to these comments, FINRA is clarifying that the relevant activities for purposes of the proposed definition of “proprietary trading firm” are securities activities. The term “securities activities” would include transactions in any security (including fixed income) and also would include securities lending transactions. However, the term would not include non-securities activities such as licensing of technology or non-securities transactions. In addition, FINRA is modifying the definition of “proprietary trading firm” to clarify that “customer” would include “any person, other than a broker or dealer, with whom the member engages, or within the past six months has engaged, in securities activities.” FINRA believes that the six-month proposed timeframe will provide additional clarity as to the application of the rule as members’ businesses may evolve over time. Thus, for example, if a member restructures its business such that it ceases engaging in securities activities with customers, the member would be able to avail itself of the proposed proprietary trading firm exemption after a six-month period (assuming that the other conditions of the exemption are met). The six-month timeframe would be assessed on an ongoing basis; therefore, any securities activity with a customer would cause the firm to be ineligible for the exemption for six months from the time the firm ceases to engage in such customer activity. Finally, FINRA is proposing to include within the scope of “proprietary trading firm” a firm that (in addition to the other criteria) conducts all trading through the firm’s accounts by traders that are owners of, employees of, or contractors to the firm “or employees of an affiliate of the firm.”

Unsupportive Comments

Pittsburgh University stated that proprietary trading firms engage in significant trading in the marketplace, which pose a substantial risk to the market, and that there is a related cost for FINRA to supervise and oversee proprietary trading firm activity and that, therefore, FINRA should apply a TAF rate to proprietary trading firms that is proportional to the cost of regulating

such firms.⁵⁷ Pittsburgh University also stated that “[w]hile the cost to regulate proprietary trading firms is less than the cost to regulate firms which trade on behalf of customers, proprietary trading firms should not be entirely exempt from the TAF when trading on an exchange on which they are members.”⁵⁸

FINRA agrees that regulating proprietary trading firm trading activity will involve a cost. For this reason, FINRA is not proposing to exempt proprietary trading firms from the TAF altogether. As discussed above, FINRA believes it is appropriate to exempt proprietary trading firms from the TAF for transactions on an exchange of which they are a member because FINRA anticipates that regulatory costs largely will relate to overseeing such firms’ activity over the counter or across exchanges.

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act⁵⁹ and paragraph (f)(2) of Rule 19b-4 thereunder.⁶⁰ At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

IV. Solicitation of Comments

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

⁵⁷ See University of Pittsburgh Letter, at 6.

⁵⁸ See University of Pittsburgh Letter. Pittsburgh University added that “[t]o exempt proprietary trading firms from TAFs would alter the balance between the TAF and other FINRA fees that fund FINRA’s operations, due to an increased cost in regulation without a similar increase of resources.”

⁵⁹ 15 U.S.C. 78s(b)(3)(A).

⁶⁰ 17 CFR 240.19b-4(f)(2).

Electronic Comments:

- Use the Commission's internet comment form (<https://www.sec.gov/rules/sro.shtml>); or
- Send an email to rule-comments@sec.gov. Please include file number SR-FINRA-2023-009 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-FINRA-2023-009. This file number should be included on the subject line if email 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 (<https://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 a.m. and 3 p.m. Copies of the filing also will be available for inspection and copying at the principal office of FINRA. Do not include personal identifiable information in submissions; you should submit only information that you wish to make available publicly. We may redact in part or withhold entirely from publication submitted material that is obscene or subject to copyright protection.

All submissions should refer to file number SR-FINRA-2023-009 and should be submitted on or before [INSERT DATE 21 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁶¹

J. Lynn Taylor,

Assistant Secretary.

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⁶¹ 17 CFR 200.30-3(a)(12).