

**SUPPORTING STATEMENT**  
**for the Paperwork Reduction Act Information Collection Submission for**  
**Rule 15b9-1 – Exemption for Certain Exchange Members**

This submission is being made pursuant to the Paperwork Reduction Act of 1995, 44 U.S.C. Section 3501 et seq.

**A. JUSTIFICATION**

**1. Necessity for the Information Collection**

Rule 15b9-1 (“Rule”) provides an exemption for certain broker-dealers from the Securities Exchange Act of 1934 (“Exchange Act”) requirement to become a member of a national securities association (“Association”). However, the equities markets have undergone a substantial transformation since the U.S. Securities and Commission (“Commission”) previously considered the Rule. Over time, active, cross-market proprietary trading firms began relying on the Rule 15b9-1 exemption in ways that were not envisioned when the Rule was adopted or amended. The Commission, on March 25, 2015, voted to propose certain amendments<sup>1</sup> to Rule 15b9-1 to better align the scope of its exemption, in light of today’s market activity, with Section 15(b)(8) of the Exchange Act and the Commission’s purposes underlying the adoption of Rule 15b9-1.

Section 15(b)(9) of the Exchange Act,<sup>2</sup> provides the Commission with authority to exempt any broker-dealer from the requirements of Section 15(b)(8), if that exemption is consistent with the public interest and the protection of investors. Pursuant to that authority, the Commission adopted Rule 15b9-1,<sup>3</sup> which was last substantively updated in 1983.<sup>4</sup> The equities markets have undergone a substantial transformation since the Commission previously considered Rule 15b9-1, evolving from markets with both manual and automated features and trading volumes concentrated on the primary listing exchanges, to a highly electronic, decentralized market with substantial competition among a large number and great variety of trading venues.<sup>5</sup> New types of proprietary trading firms have emerged, including those that

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<sup>1</sup> See Exemption for Certain Exchange Members; Securities Exchange Act Release No. 74581 (March 25, 2015), 80 FR 18035 (April 2, 2015).

<sup>2</sup> “The Commission by rule or order, as it deems consistent with the public interest and the protection of investors, may conditionally or unconditionally exempt from paragraph (8) of this subsection any broker or dealer or class of brokers or dealers specified in such rule or order.” 15 U.S.C. 78o(b)(9); Pub. L. No. 98-38, 97 Stat. 205 (1983).

<sup>3</sup> 17 CFR 240.15b9-1.

<sup>4</sup> See SECO Programs; Direct Regulation of Certain Broker-Dealers; Elimination, Exchange Act Release No. 20409 (November 22, 1983), 48 FR 53688 (November 29, 1983) (“SECO Programs Release”).

<sup>5</sup> See Concept Release Concerning Equity Market Structure, Exchange Act Release No. 61358 (January 14, 2010), 75 FR 3594, 3594-3596 (January 21, 2010) (“Concept Release”) (discussing the evolution from “a market structure with primarily manual trading to a market structure with pri-

engage in so-called high-frequency trading strategies. These firms tend to effect transactions across the full range of exchange and off-exchange markets, including alternative trading systems (“ATSs”). They also tend to use complex electronic trading strategies and sophisticated technology to generate a large volume of orders and transactions throughout the national market system.

The Commission proposed to amend Rule 15b9-1 to better align the scope of its exemption, in light of today’s market activity, with Section 15(b)(8) of the Exchange Act and the Commission’s original purpose in adopting Rule 15b9-1, which was to accommodate broker-dealer activities ancillary to a floor-based business while preserving the traditional role of the exchange as the entity best suited to regulate member conduct on the exchange.<sup>6</sup> A broker-dealer that conducts off-exchange transactions outside the limited scope of Rule 15b9-1, as proposed to be amended, would be required to become a member of an Association. Consequently, such a broker-dealer would be subject, with respect to its off-exchange transactions, to the oversight and rules of an Association, the category of self-regulatory organization (“SRO”) primarily responsible for regulating trading in the off-exchange market in accordance with Section 15(b)(8).<sup>7</sup> Further, as a result of the proposal, a broker-dealer that does not trade off-exchange but that trades indirectly on multiple exchanges would be required in accordance with Section 15(b)(8), to become a member of an Association, or alternatively, a member of each exchange where it effects transactions other than transactions to hedge the risks of its floor-based activities.

As part of the proposed amendments to Rule 15b9-1, the Commission proposed to eliminate the de minimis allowance in its entirety and replace the allowance with an exemption from Association membership for exchange member broker-dealers that operate on the floor of the exchange, to the extent they effect transactions off-exchange solely for the purpose of hedging the risks of their floor-based activities. The Commission proposed that the hedging exemption be limited to firms that trade on the floor of a national securities exchange, as the

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marily automated trading”).

<sup>6</sup> In adopting Rule 15b8-1, the Commission stated: “Among the broker-dealers that are not members of a registered national securities association are several specialists and other floor members of national securities exchanges, some of whom introduce accounts to other members. The over-the-counter business of these broker-dealers may be limited to receipt of a portion of the commissions paid on occasional over-the-counter transactions in these introduced accounts, and to certain other transactions incidental to their activities as specialists. In most cases, the income derived from these activities is nominal.” See Qualifications and Fees Release, supra note 12, at 11675.

<sup>7</sup> See Pub. L. No. 75-719, 52 Stat. 1070 (1938) (The Maloney Act, which established the concept of and framework for Associations, states in its preamble that its purpose was “[t]o provide for the establishment of a mechanism of regulation [Associations] among over-the-counter brokers and dealers operating in interstate and foreign commerce or through the mails, to prevent acts and practices inconsistent with just and equitable principles of trade, and for other purposes”). See also infra notes 26, 28-33 and accompanying text (describing the early history of the Maloney Act).

Commission understands that currently, broker-dealers that trade exclusively on a single exchange do so on a physical exchange floor. A dealer seeking to rely on this exception would have to establish, maintain and enforce written policies and procedures reasonably designed to ensure and demonstrate that such hedging transactions reduce or otherwise mitigate the risks of the financial exposure the dealer incurs as a result of its floor-based activity. The dealer would also be required to preserve a copy of its policies and procedures in a manner consistent with 17 CFR 240.17a-4 until three years after the date the policies and procedures are replaced with updated policies and procedures.”

## **2. Purpose of the Information Collection**

The Commission preliminarily believes that requiring written policies and procedures would facilitate SRO supervision of broker-dealers relying on the proposed hedging exemption, as it would provide an efficient and effective way for regulators to assess compliance with the proposed exemption. The determination of whether an off-exchange transaction by a floor-based dealer reduces or otherwise mitigates the risk of the financial exposure incurred as a result of the dealer’s floor-based business may vary depending on the nature of the business of the floor-based dealer, its financial position, and the particular transactions effected. Consequently, the Commission preliminarily believes that requiring floor-based dealers to develop written policies and procedures will provide sufficient flexibility to accommodate the varying business models of floor-based dealers and appropriate hedging activities.

## **3. Role of Improved Information Technology**

The policies and procedures required by the proposed amendments to Rule 15b9-1 do not directly utilize information technology in the collection of information. However, the Commission anticipates that dealers relying on the exemption will utilize information technology when enforcing the policies and procedures required by the rule.

## **4. Efforts to Identify Duplication**

The proposed rule amendments would allow certain dealers to avoid membership in an Association. As a result, dealers complying with the proposed rule would be able to avoid potentially duplicative regulation by various SROs.

## **5. Effect on Small Entities**

In preparing the proposed amendments, the Commission examined recent FOCUS data for the 125 Non-Member Firms and concluded that at most 11 of the affected entities have net capital of \$500,000 or less, and some of those might not be small entities because they might be affiliates of larger organizations. Although the Commission lacks the data to quantify these firms’ off-exchange activity, it does have FOCUS information on the firms’ disclosed activities. Based on this disclosure, the Commission preliminarily believes that many of these firms may be able to trade off-exchange under the proposed floor member hedging exemption for a number of reasons. As a result, the Commission preliminarily believes that the proposed amendments to

Rule 15b9-1 would not, if adopted, have a significant economic impact on a substantial number of small entities.

## **6. Consequences of Less Frequent Collection**

The Commission preliminarily believes that collecting the information on a less frequent basis would frustrate both the ability of the SRO to supervise those broker-dealers relying on the proposed hedging exemption and the ability of broker-dealers subject to the proposed rule to ensure that their hedging activities continue to comply with the requirements of the proposed rule.

## **7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)**

5 CFR 1320.5(d)(2) requires an agency to demonstrate, in its submission for OMB clearance, that the reporting of information more often than quarterly is necessary to satisfy statutory requirements or other substantial need. The proposed amendments to Rule 15b9-1 would require the dealer to establish, maintain and enforce written policies and procedures reasonably designed to ensure and demonstrate that such hedging transactions reduce or otherwise mitigate the risks of the financial exposure the dealer incurs as a result of its floor-based activity. The proposed rules do not require the dealer to report information more often than quarterly. As a result, there are no special circumstances. This collection under the proposed amendments to Rule 15b9-1 is consistent with the guidelines of 5 CFR 1320.5(d)(2).

## **8. Consultation Outside the Agency**

The Commission has not consulted with entities outside the agency about the proposed amendments to Rule 15b9-1. “The Commission has issued a release soliciting comment on the new “collection of information” requirements and associated paperwork burdens. A copy of the release is attached. Comments on Commission releases are generally received from registrants, investors, and other market participants. In addition, the Commission and staff participate in ongoing dialogue with representatives of various market participants through public conferences, meetings and informal exchanges. Any comments received on this proposed rulemaking will be posted on the Commission’s public website, and made available through <http://www.sec.gov/rules/proposed.shtml>. The Commission will consider all comments received prior to publishing the final rule, and will explain in any adopting release how the final rule responds to such comments, in accordance with 5 C.F.R. 1320.11(f).”

## **9. Payment or Gift to Respondents**

Not applicable.

## **10. Assurance of Confidentiality**

The information collected pursuant to the proposed amendments to Rule 15b9-1 will not be widely available as it is information related to the internal operations of those dealers complying with the exemption. To the extent that the Commission receives confidential

information pursuant to Rule 15b9-1, such information will be kept confidential, subject to the provisions of the Freedom of Information Act.

## **11. Sensitive Questions**

Not applicable. The collection of information will not include Personally Identifiable Information.<sup>8</sup>

## **12. Estimate of Burden**

The Commission estimates that up to 100 dealers may wish to take advantage of the exemption provided for under the proposed amendments to Rule 15b9-1. The total recordkeeping burden for those dealers is approximately 1,600 hours initially and 9,600 hours annually thereafter. This burden is broken down in more detail below.

The Commission estimates that the one-time, initial burden for a dealer to establish written policies and procedures as required under Rule 15b9-1 would be approximately 16 hours.<sup>9</sup> This figure is based on the estimated number of hours to develop a set of written policies and procedures, including review and approval by appropriate legal personnel. The Commission notes that the policies and procedures required by the proposed Rule are limited to hedging transactions that reduce or otherwise mitigate the risks of the financial exposure the dealer incurs as a result of its floor-based activity.

In addition, the Commission estimates the annual burden of maintaining and enforcing such policies and procedures, including a review of such policies at least annually, would be approximately 96 hours for each dealer.<sup>10</sup> This figure includes an estimate of hours related to reviewing existing policies and procedures, making necessary updates, conducting ongoing training, maintaining relevant systems and internal controls, performing necessary testing and monitoring of off-exchange hedging transactions as they relate to the broker-dealer's floor-based activities and maintaining copies of the policies and procedures for the period of time required by the proposed rule.

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<sup>8</sup> The term "Personally Identifiable Information" refers to information which can be used to distinguish or trace an individual's identity, such as their name, social security number, biometric records, etc. alone, or when combined with other personal or identifying information which is linked or linkable to a specific individual, such as date and place of birth, mother's maiden name, etc.

<sup>9</sup> This figure is based on the following: (Compliance Manager at 10 hours) + (Compliance Attorney at 5 hours) + (Director of Compliance at 1 hour) = 16 burden hours per dealer.

<sup>10</sup> This figure is based on the following: (Compliance Manager at 60 hours) + (Compliance Attorney at 24 hours) + (Director of Compliance at 12 hours) = 96 burden hours per dealer.

The Commission estimates that the annualized burden associated with Rule 15b9-1 would be 10,133.33 hours which corresponds to an initial burden of 533.33 hours<sup>11</sup> and an ongoing burden of 9,600 hours.<sup>12</sup>

**In summary, the Commission estimates that, over a three-year period, the total recordkeeping burden associated with Rule 15b9-1 would be approximately 30,400 hours, or 10,133.33 hours per year<sup>13</sup> when annualized over three years. The average estimated burden per dealer would be 304 hours, or 101.33 hours per year<sup>14</sup> when annualized over three years.**

### **13. Estimate of Total Annual Cost Burden**

<sup>11</sup> This figure is based on the following: (Year 1: (16 burden hours per dealer) x (100 dealers)) + (Year 2: (0 burden hours per dealer) x (100 dealers)) + (Year 3: (0 burden hours per dealer) x (100 dealers)) = 1,600 burden hours ÷ 3 = 533.33 hours per year. In estimating these burden hours, the Commission examined the estimated burdens imposed by other rules applicable to broker-dealers. For example, amendments to Regulation SHO adopted in 2010 required broker-dealers to establish, maintain, and enforce written policies and procedures relating to Rule 201(c) and Rule 201(d)(6) to ensure short-sale orders are, among other things, properly marked, are submitted at the proper price, or are properly off-set (in the case of Rule 201(d)(6)). See Exchange Act Release No. 61595 (February 26, 2010) 75 FR 11232, 11286 (March 10, 2010) (“Amendments to Regulation SHO”). The policies and procedures relating to Rule 201(c) and Rule 201(d)(6) required under the Amendments to Regulation SHO estimated an average initial one-time burden of 160 burden hours per broker-dealer and ongoing compliance cost of 60 hours annually to ensure the policies and procedures are up-to-date and remain in compliance as well as an additional 336 hours annual to monitor, surveil, and enforce trading in compliance with Rule 201. *Id.* The Commission preliminarily believes that the policies and procedures under the proposed floor member hedging exemption will be substantially less burdensome than those required by the Amendments to Regulation SHO because those policies and procedures require certain technology and real-time monitoring components. For example, under the Amendments to Regulation SHO described above, broker-dealers’ policies and procedures must be reasonably designed to enable a broker-dealer to monitor, on a real-time basis, the national best bid so as to determine the price at which a broker-dealer may submit a short sale order to a trading center in compliance with Rule 201(c), and off-setting transactions under the riskless principal provision under Rule 201(d)(6) must be allocated to a riskless principal or customer account within 60 seconds of execution. *Id.* at 11284. In contrast, the policies and procedures under the proposed amendments to Rule 15b9-1 do not involve a real-time monitoring or technology component.

<sup>12</sup> This figure is based on the following: (Year 1: (96 burden hours per dealer) x (100 dealers)) + (Year 2: (96 burden hours per dealer) x (100 dealers)) + (Year 3: (96 burden hours per dealer) x (100 dealers)) = 28,800 burden hours ÷ 3 = 9,600 hours per year. In estimating these burden hours, the Commission also examined the estimated initial and ongoing burden hours imposed on registered security-based swap dealers under Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information. See Exchange Act Release No. 74244 (February 11, 2015) 80

The Commission preliminarily does not believe there are any costs related to the proposed amendments that have not been accounted for in the burdens discussed above.

**14. Estimate of Cost to the Federal Government**

The Commission does not believe there are any costs to the Federal Government related to the proposed amendments to Rule 15b9-1.

**15. Explanation of Changes in Burden**

Not applicable.

**16. Information Collection Planned for Statistical Purposes**

Not applicable.

**17. Approval to not Display Expiration Date**

Not applicable.

**18. Exceptions to Certification Statement**

Not applicable.

**B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

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FR 14564, 14683 (March 19, 2015) (“Regulation SBSR”). Regulation SBSR requires registered security-based swap dealers to establish, maintain, and enforce written policies and procedures that are reasonably designed to ensure compliance with any security-based swap transaction reporting obligations. *Id.* The estimated initial and ongoing compliance burden on registered security-based swap dealers under Regulation SBSR were 216 burden hours and 120 burden hours respectively. *Id.* The Commission preliminarily believes that the initial and ongoing burden hours under the proposed floor member hedging exemption will be substantially less than for registered security-based swap dealers under Regulation SBSR, because the policies and procedures under Regulation SBSR require programming certain systems for transaction reporting and performing testing of such systems. *Id.* In contrast, the proposed floor member hedging exemption would not necessarily require programming or testing of certain systems and is a much more discrete set of policies and procedures as compared to the more comprehensive policies and procedures required by Regulation SBSR, which cover, among other things, the full scope of reporting security-based swap transactions by registered security-based swap dealers and others.

<sup>13</sup> 30,400 hours ÷ 3 = 10,133.33 hours per year.

<sup>14</sup> 30,400 hours ÷ 100 (estimated number of dealers) = 304 ÷ 3 = 101.33 hours per respondent.

This collection does not involve statistical methods.