Reginald M. Browne
Senior Managing Director – ETF Trading

January 29, 2018

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street, N.W.
Washington, D.C. 20006-1506

Re: Retrospective Rule Review; Effectiveness and Efficiency of Payments for Market Making Regulatory Notice 17-41

Dear Ms. Mitchell:

On behalf of Cantor Fitzgerald & Co. ("Cantor Fitzgerald"), we welcome the opportunity to submit this letter in response to FINRA's Regulatory Notice 17-41 relating to a *Retrospective Rule Review of Its Payment for Market Making Rule* ("Rule 5250"), and appreciate FINRA's ongoing commitment to modernizing its rules to reflect the realities of today's marketplace. As discussed more fully below, Cantor Fitzgerald supports a revision to Rule 5250 to permit issuers or sponsors of exchange-traded funds ("ETFs") to make *direct* payments to market makers.[1] The restrictions of Rule 5250, however, should continue to apply to single stock corporate issuers.

Background

Cantor Fitzgerald was formed in 1945 as an investment bank and brokerage business. Today, Cantor Fitzgerald, along with its affiliates, is a premier global financial services firm and is recognized for its strengths in *the* equity and fixed income capital markets. Cantor Fitzgerald operates trading desks in every major financial center in the world, with offices in over 30 locations around the world. Cantor Fitzgerald's Senior Managing Director and Global co-Head of its ETF group has been in senior leadership roles for the last 15 years at different broker-dealers and has played a direct role in helping to bring to market over 1,000 ETFs in the United States and Europe.

Exchange-traded products ("ETPs"), and in particular ETFs, play an important role in both institutional and retail investor portfolios. The number of ETPs has grown significantly over the last decade in the U.S. and globally. Assets invested in ETFs now stand at well over $3 trillion in the U.S. versus less than $300 billion only 10 years ago.

---

[1] Cantor Fitzgerald supports many of the recommendations made in the comment letters submitted by the Security Traders Association (STA), dated January 22, 2018 ("STA Letter"); SIFMA, dated January 29, 2018; Virtu Financial Inc., dated January 3, 2018; and, Cboe Global Markets, Inc., dated November 27, 2017.

FINRA Rule 5250

Rule 5250 explicitly prohibits broker-dealers from accepting payment or other consideration from an issuer for market making activities. The rule excepts from this prohibition (i) payment for services, including, investment banking services; (ii) reimbursement of any payment for registration imposed by the SEC or state regulatory authorities and for listing fees imposed by a self-regulatory organization; and (iii) any payment expressly provided for under the rules of a national securities exchange that have been approved by the SEC.

The main purpose of Rule 5250 has been to address perceived conflicts of interests between market makers and issuers, helping to ensure that market makers act independently and that their quoting activities were not influenced by issuer payments.[2] FINRA amended Rule 5250 to allow exchanges to develop programs for issuers of ETPs to pay market makers indirectly to incentivize liquidity.[3] Although well-intentioned, Cantor Fitzgerald believes that the exchange programs are ineffective for new and thinly-traded ETFs. These programs are driven by performance metrics and tailored toward volume discounts and/or time at the NBBO. New and less liquid ETFs need time and market maker capital to ramp-up before natural market forces can materialize, thus enabling an active market and competitive forces to drive quotations.

ETP issuers and direct payments to market makers

As noted by the other commenters, ETP issuers should be permitted to make *direct* payments to market makers. The concerns which formed the basis of Rule 5250 (i.e., a perceived conflict of interest which could influence how a market maker quotes a security) are not present when quoting an ETP.

As noted in the STA letter, "*the derivative nature of ETPs provide an efficient arbitrage mechanism which ensures ETP prices align with the market values of the underlying securities.*"[4] This is precisely the point that vitiates any conflict, perceived or otherwise, and ensures that the investor protection intent under Rule 5250 is not compromised. The prices of ETPs are derived from their respective underlying basket of securities; those prices are effectively driven by the quotations of securities for which the market maker has no relationship. Any dislocation in pricing between the ETPs and its component securities is quickly corrected, as happens each and every trading day, through arbitrage trading.

To ensure transparency in the payments, ETP issuers should be required to disclose the terms of any payment arrangements they make with broker-dealers to act as market makers. These disclosures can be made in the prospectus, ETP website, or other prominent location to ensure investors have ready access to this information.

---

[2] *See* FINRA Notice to Members 75-16 (February 20, 1975).

[3] Order Approving a Proposed Rule Change by Financial Industry Regulatory Authority, Inc. Relating to FINRA Rule 5250 (Payments for Market Making), Exchange Act Release No. 69398, 78 Fed. Reg. 24,261 (Apr. 18, 2013).

[4] *See*, STA letter, *supra*.

Conclusion

Cantor Fitzgerald joins with its industry colleagues in expressing its appreciation for FINRA taking on this important issue. Amending Rule 5250 to permit ETP issuers to make direct payments to market makers would increase competition, as well as create more liquidity and efficiency in the market. This benefit to the market is balanced against concerns related to potential conflicts such payments might create, which are effectively eliminated by the independent and competitive pricing mechanism for the underlying components of the ETPs.

We would be happy to answer any questions, and look forward to FINRA's continued initiatives to improve market efficiency.

Sincerely,

Cantor Fitzgerald & Co.
Reginald M. Browne
Senior Managing Director

cc: Racquel Russell, Associate General Counsel, FINRA Office of the General Counsel
Cara Rosen, Counsel, FINRA Office of the General Counsel
Shawn O'Donoghue, Economist, FINRA Office of the Chief Economist