

**RE: Regulatory Notice 25-07**

Dear Ms. Mitchell

The Firm - XR Securities LLC ("XRS") - is a privately held, proprietary-based trading firm located in Chicago, IL (USA). We appreciate the opportunity to add some commentary about a few of the subjects noted seeking clarification as to the applicability of some rules to modern day trading by firm's directly into Exchange systems where no public, brokerage, custody or customer business is applicable. Please see below and thank you for the opportunity for us to comment.

\*\*\*\*\*

FINRA Requests Comment on Modernizing FINRA Rules, Guidance, and Processes for the Organization and Operation of Member Workplaces

**A.2. Should the Supervision Rule's branch office and OSJ definitions, inspection requirements, and designation and registration of offices be modernized to eliminate unnecessary burdens or ambiguities while maintaining investor protection and market integrity? Should the branch office definition be amended in light of the technological advances that have changed how and where individuals work? Is the OSJ definition still relevant in today's environment?**

In 2023, the SEC amended Rule 15b9-1 in a manner that required a number of proprietary trading firms to obtain FINRA membership. Proprietary trading firms ("prop firms") trade exclusively for their own account; they do not conduct customer business in any form. They do not handle customer funds or securities or execute orders on behalf of third parties. Prior to joining FINRA, these firms were subject to the rules the various securities exchanges of which they were members. Cboe was and still remains our DSRO. We request that, in its efforts to modernize its rules, FINRA recognize this new cohort of members, and make an effort to distinguish prop firms from customer-based firms where it is reasonable to do so, and accommodate the fact that many firms who shaped their business models and operations under a different set of regulations over the course of many years now find themselves subject to additional, and in some circumstances unnecessary and non-applicable rules and regulations as a result of their nascent FINRA membership.

FINRA's Branch Office and OSJ definitions are one example of a situation where a prop firm may find itself subject to regulations that were previously inapplicable and unnecessary in relation to its business model. Options exchange rules generally do not require firms that

do not conduct customer business to register locations as Branch Offices or Offices of Supervisory Jurisdiction (OSJ).

Options exchanges generally provide that members (who do not operate a customer business) must inform the exchange of the locations from which they do business. These exchanges include additional obligations to inspect each office or location in a manner reasonably designed to prevent and detect violations of, and achieve compliance with, applicable securities laws and regulations. (For example, PHLX General 9 Sec. 20(g), Cboe 8.16(f)). This approach was sufficient to supervise the activities of prop firms and their associated persons for many years, including the post-pandemic era in which many staff worked in fully remote environments. We request that FINRA grant firms flexibility to determine the locations from which it conducts business and how to supervise and inspect them. Historically prop firms were treated as though they did not and could not have branches. They were not required to, and in fact not able to, amend Form BR in WebCRD. Applying the existing framework to prop firms that have operated under exchange rules for years serves to unnecessarily restrict the locations from which their employees can conduct business and subject the firms to increased filing obligations (and associated fees).

PHLX Options 10 (Doing Business with the Public) Section 5 (Branch Offices) provides that firms “approved to do options business with the public” shall file with the exchange a list of branch offices including each branch’s location and manager; and that each branch shall be supervised by a qualified supervisor. A footnote to this rule (.01) provides a definition of Branch Office identical to that contained in FINRA rules. Given the context of the rule to which the definition is appended, and the title of the chapter in which the rule is contained, it is apparent that these requirements apply only to firms conducting customer business.

A footnote to American Options Rule 922 (Supervision of Accounts) also includes a definition of Branch Office identical to that of FINRA. However, the rule provides that its provisions apply to any firm that “maintains customers’ accounts in which transactions in options on equity or debt securities are effected, that conducts a non-member customer business...”

Cboe C1 Rule 3.40 (c) includes a definition of Branch Office, but similar to the rules mentioned above, the preceding sections of the same rule convey that the rule applies to firms approved to do business with the public.

None of the above-mentioned options exchange rulebooks include or define the term Office of Supervisory Jurisdiction.

FINRA's definition of Branch Office is largely inapplicable to most prop firms with the exception of 3310(f)(2)(B) ("Any location that is responsible for supervising the activities of persons associated with the member at one or more non-branch locations of the member is considered to be a branch office."). We believe FINRA should clarify that the supervisory activities mentioned here apply only to firms that do customer business to provide prop firms with consistent regulation with exchange rules.

As mentioned above, most if not all options exchange rulebooks do not address the concept of an Office of Supervisory Jurisdiction. Again, most of the functions enumerated in the definition of OSJ apply to firms conducting customer business, however, we request clarification of the phrase "**order execution and market making.**" Our perspective of this particular function/definition within the rule verbiage is that it does not apply to Exchange-registered prop firms routing quotes via Exchange protocols. Our understanding is that prop firms that trade electronically on listed exchanges and ATSS do not execute orders, and "market making" in this reference seems to apply to firms that internalize order flow and accept, route, or fill orders on behalf of third parties, not necessarily any firm that posts passive, two-sided displayed interest on an exchange. Again, providing that prop firms are not subject to this definition would provide a regulatory framework consistent with the exchange regulation prop firms operated under for many years.

**A.4. Given members' experience with RSLs as non-branch locations and the Pilot Program, what further revisions or extensions would be helpful, and how would effective supervision be maintained under these revisions? For example, should the conditions and ineligibility criteria be revised based on business attributes such as the size of the member or differences in business models?**

As mentioned in response to A.2 above, many prop firms established their business in a manner that complied with exchange rules. FINRA membership brought a new set of regulations that were primarily written with customer firms in mind. For example, three of five enumerated inspection criteria in Rule 3110(c)((2)(A) are not applicable to Prop firms (safeguarding customer funds and securities; Transmittals of funds or securities from customers to third parties, outside entities, or locations other than the customer's primary residence, or between customers and registered representatives; and changes of customer account information).

As mentioned in A.2 above, we request that FINRA acknowledge the unique situation of prop firms that were mandated to join FINRA due to an SEC rule change. The RSL and remote inspection programs permit some degree of flexibility, however, they too apply

some unnecessary and inefficient provisions to prop firms. Options exchanges generally provide that members must inform the exchange of the locations from which they do business. These exchanges include additional obligations to inspect each “office or location” in a manner reasonably designed to prevent and detect violations of, and achieve compliance with, applicable securities laws and regulations. (For example, PHLX General 9 Sec. 20(g), Cboe 8.16(f)). This approach was sufficient to supervise the activities of prop firms and their associated persons for many years, including the post-pandemic era in which many staff worked in fully remote environments. We request that FINRA grant firms flexibility to determine the locations from which it conducts business and how to supervise and inspect them.

In circumstances where all trading is conducted through firm systems, all communications are logged and subject to surveillance, and books and records stored offsite/backed up to offsite locations, firms should have flexibility to supervise their staff in a manner that makes sense for their size and operations. Guidance for inspection obligations with respect to home offices should allow firms to assess the need for inspections based on the circumstances for each individual, such as disciplinary history, outside business activities, or findings resulting from other routine surveillance (communications, trading surveillance, trading performance).

Respectfully Submitted,

Frank J Vivirito

CCO – XR Securities LLC