Subject: File No. S7-15-18
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We respectfully submit comments on behalf of Bluefin Trading, LLC (the Firm) to summarize our position on the new purposed rule change for ETF sponsors. For 17 years the Firm has been a registered market maker in, among other products, ETF and ETF derivatives. Specifically, our main concerns and comments are in regard to how the proposed rule would impact the creation and redemption process. Our comments are outlined below.

From the Firms perspective, adding flexibility to the creation and redemption process is generally viewed as positive for the industry. Due to the uniqueness and idiosyncratic risks associated with the underlying assets of ETFs, they become, at times, very difficult, and occasionally impossible to transact in. This in turn prevents both parties (the ETF sponsor and Market Maker) from being able to reasonably engage in transactions via the creation and redemption process. Limiting this engagement leads to higher premiums/discounts, lower volume and high volatility, which undoubtedly damages ETF end users. The current environment which provides exemptive relief for custom creations and redemptions to only a select group of ETF sponsors unfairly favors and advantages those sponsors by allowing their products to be easier to create, redeem and make markets.
While added flexibility would certainly be welcomed by industry participants, equally or even more important is the ultimate adoption of mandated standards for creations and particularly redemptions. We believe this is in the best interest of protecting the rights of fund shareholders. Specifically, in the case of Fixed Income ETFs, we believe there should be a requirement for an in-kind, pro rata fund distribution upon a redemption. Generally, the flexibility of custom creation and redemption baskets enables greater ETF liquidity. However, there are market conditions in which only allowing custom creations or redemptions can lead to greater price volatility and dislocation from NAV. ETF shareholders have pro-rata exposure to the funds total holdings, and by that logic, should have a right to request a pro-rata distribution of those holdings in the event of a redeem. This would mean that any ETF sponsor at any time would be required to honor a pro-rata redemption of its fund in any creation/redemption unit size multiple amounts, subject to some defined amount of flexibility (e.g., for a fixed income ETF, rounding each bond to the nearest 1000 bonds or minimum tradable amount.) or to exclude securities that are undergoing corporate actions or for some other reason cannot be settled or transferred. While adding flexibility would allow for more competitive markets under normal conditions, requiring the basic in-kind pro rata redeem feature in ETFs would greatly improve the effectiveness of markets in high volatility or fast moving markets.

An example may better illustrate how liquidity would be reduced if there is no option or right to an in-kind, pro-rata redeem basket available to a fixed income ETF fund. In the event of heightened market volatility or outflows from ETFs, as customers are selling their shares, market makers step in to buy in order to provide liquidity and to arbitrage the ETF vs. the underlying bond basket, thereby keeping the ETF shares trading close to their NAV. If the Fund sponsor only makes a custom redeem basket available for redemptions with a large concentration of a ticker or sector that has negative news, or a redeem basket (e.g. with a large concentration of energy bonds when oil is down 5% on the day), liquidity in that subset of bonds on the day may effectively evaporate and will prevent market makers from effecting a simple arbitrage or require a higher discount in the ETF to do so. As a Market Maker, knowing that you always have an option to transact in a full in-kind, pro-rata redeem instead of a concentrated basket greatly increases the pool of underlying liquidity and reduces concentration risk. This feature would give market makers more confidence to be able to provide continuous and deeper liquidity in the ETF shares and keep them closer in line with the NAV they are meant to track. In conclusion, these additional redemption (and possibly creation) options will provide for more liquid and continuous markets, as well as less dislocations of ETF share price from NAV.

Our second concern is it appears there exists some form of prioritized or special treatment between certain Authorized Participants (APs) and ETF sponsors as allowed or interpreted by the ETF sponsors respective exemptive relief. While we firmly believe that such prioritized or special treatment should not exist, we would welcome guidance from the Commission on this issue. We respectfully submit that there is a need for direction from Commission staff on the fair and equitable treatment of market makers acting through Authorized Participants to create or redeem shares of a fund. To be clear, if sponsors are allowed to favor certain market makers over others, certain market makers will be priced out or significantly disadvantaged. It is our opinion this practice is counterproductive to the main goal of generalizing ETFs exemptive reliefs, namely, it will lead to higher premiums/discount, lower volume and higher volatility.

It is our belief that the aforementioned comments are extremely important when considering new rules dealing with ETF exemptive relief. Failing to address these issues could be detrimental to our markets and may ultimately lead to larger problems during times of outflows or higher volatility in the fixed income markets. We welcome the opportunity to discuss these issues with Commission staff and are available at your convenience.