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Invested in America

October 7, 2022

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: ***Joint Industry Plan; Notice of Filing of Amendment to the National Market System Plan Governing the Consolidated Audit Trail; File No. 4-698***

Dear Ms. Countryman:

On behalf of its members firms, the Securities Industry and Financial Markets Association ("SIFMA")[1] respectfully submits this supplemental comment letter to the U.S. Securities and Exchange Commission (the "Commission") in response to the Commission's order ("Order") to extend its time for consideration of the amendment to the National Market System Plan Governing the Consolidated Audit Trail (the "CAT NMS Plan") by the self-regulatory organizations ("SROs") as the participants in the CAT NMS Plan ("Participants") to implement a revised funding model ("Executed Share Model")[2] for the consolidated audit trail ("CAT") and to establish a fee schedule for the participants in the CAT NMS Plan in accordance with the Executed Share Model.[3] As discussed extensively in our first comment letter on the proposal and further supplemented in this letter, the Participants have not demonstrated that the proposal meets the relevant standards under the Securities Exchange Act of 1934 ("Exchange Act") governing SRO fees.

We appreciate the opportunity to submit this supplemental comment letter on the proposed Executed Share Model and continue to reiterate our comments from our initial June 22,

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[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's one million employees, we advocate on legislation, regulation and business policy affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] See Exchange Act Release No. 95634 (August 30, 2022), 87 FR 54558 (September 6, 2022) (Order extended the time for Commission consideration of the Executed Share Model); See Exchange Act Release No. 94984 (May 25, 2022), 87 FR 33226 (June 1, 2022) (Proposal to establish the Executed Share Model).

[3] Capitalized terms not otherwise defined in this letter have the same meanings as they do in the CAT NMS Plan. For instance, "CAT Data" is defined in Article I, Section 1.1 of the CAT NMS Plan. CAT Data is defined as "data derived from Participant Data, Industry Member Data, SIP Data, and such other data as the Operating Committee may designate as 'CAT Data' from time to time."

2022 comment letter ("June 22 Letter") on the proposal.[4] In this supplemental comment letter, we focus on certain items related to the proposed Executed Share Model on which the Commission in its Order has requested additional comment. We believe for the reasons set forth below, as well as in our June 22 Letter, that the Commission should disapprove the proposed Executed Share Model as the Participants have not met their burden under the Exchange Act of demonstrating that the proposal (1) provides "for the equitable allocation of reasonable dues, fees, and other charges," (2) is "not designed to permit unfair discrimination between customers, issuers, brokers or dealers," and (3) does not "impose any burden on competition not necessary or appropriate in furtherance of the purposes" of the Exchange Act. As further described below, we believe that the Executed Share Model fails these standards based on its unfair and inequitable treatment of the Financial Industry Regulatory Authority, Inc. ("FINRA") by assessing it the highest portion of Participants fees and failing to account for Industry Member funding of it, the model's unfair and inequitable treatment of clearing brokers, particularly related to the collection of Past CAT Costs, and the model's the lack of detail regarding current CAT costs and the SRO fee process related to Industry Members' share of those costs.

We also reiterate our call for the Participants to work with SIFMA and the industry in a collaborative manner to establish a viable CAT funding model. We continue to believe that the best approach is for the SROs and Industry Members to work together to develop a model that ultimately is approvable by the Commission. In our experience in dealing the Executed Share Model, as well as the prior two proposed CAT funding models, it is extremely challenging to work collaboratively with the SROs on a CAT funding model, and for them to establish a viable model, when they are unable to agree among themselves on an appropriate model. With regard to the Executed Share Model, we note that FINRA submitted a comment letter objecting to the model.[5]

Accordingly, in addition to our specific comments below on the Executed Share Model, we would suggest based on the continuing inability of the Participants to achieve consensus regarding a CAT funding model, that the Commission consider issuing an order soliciting comment on whether the CAT Operating Committee should be reorganized to provide for a governance structure consistent with the new, single NMS plan for the distribution of equity market data, the CT Plan.[6] We believe such a governance structure for the CAT would help facilitate a fairer structure for the views of the SROs and industry to be heard and incorporated into any further CAT funding proposal by reducing the ability of the largest exchange groups to dictate the terms of any CAT funding proposal over the objections of other SRO Participants and the industry.

[4] See (https://www.sec.gov/comments/4-698/4698-20132695-303187.pdf).

[5] See (https://www.sec.gov/comments/4-698/4698-20132717-303208.pdf).

[6] See Exchange Act Release No. 92586 (August 6, 2021), 86 FR 44142 (August 11, 2021) (order approving the CT Plan).

I. Discussion

FINRA Allocation

We continue to believe that the Executed Share Model does not satisfy the Exchange Act fee standards based on the way it allocates CAT costs to FINRA and its lack of consideration of Industry Member funding of FINRA. On this point, it is telling that FINRA submitted a comment letter objecting to the proposal.[7] In that letter, FINRA notes that:

> the Proposal does not disclose that the increase in Participants' share is disproportionately allocated to FINRA rather than equitably allocated amongst the Participants. In fact, under the Proposal, the exchange Participants' share of total costs would remain almost the same as under the previous proposal. Notably, using trade volumes from 2021, FINRA would pay roughly $19 million per year under the Proposal, which is $4 million more than all the options exchanges combined.

Similarly, as we noted in our June 22 Letter, we believe that the proposal is flawed because it fails to appropriately consider that Industry Members pay the full costs of operating FINRA. In their response to comments on the Executed Share Model, the Participants generally assert that this argument related to industry funding of FINRA inappropriately focuses on how a fee is paid for rather than the fee itself, that the proposed fees under the Executed Share Model are the same regardless of whether a transaction is executed on or off an exchange, and that each exchange is an SRO with regulatory responsibilities under the Exchange Act.

There are several flaws with the exchange Participants' response. Most significantly, the exchange Participants should not be able pick and choose whether to treat FINRA as a market center for purposes of an NMS Plan based on the outcome that leads to the greatest financial benefit to the exchanges, especially given FINRA's regulatory role in the marketplace. In the Executed Share Model, the exchange Participants are effectively choosing to treat FINRA as a market center responsible for all Participant fees for off-exchange transactions. In contrast, they have chosen to not treat FINRA as a market center for purposes of the CT Plan, stating that FINRA is not considered a market center under the CT Plan solely by virtue of facilitating trades through any trade reporting facility FINRA operates in affiliation with a national securities exchange designed to report transactions otherwise than on an exchange.[8] The result of this decision in the CT Plan is that the exchange Participants have limited FINRA to only one vote for purposes of governance of the CT Plan, thus limiting FINRA's ability to determine how to allocate the lucrative market data revenue to be distributed under the plan. These two conflicting decisions by the exchange Participants demonstrate that they will choose to treat FINRA for purposes of NMS plans involving money in the way that is most financially beneficial to them and without regard to FINRA's critical role in the marketplace. These decisions also show the inherent conflicts of interest that for-profit exchanges have in operating as SROs, where their incentive is to make decisions that benefit them financially as for-profit entities, regardless of the impact to the market.

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[7] See supra note 5.

[8] See supra note 6.

We further note that the exchange Participants' argument dismissing consideration of how fees are paid ignores prior precedent. In the past, the exchanges have certainly considered how fees are paid in other contexts when seeking to change them. For instance, the options exchanges discarded their registered representative fees in favor of the options regulatory fee ("ORF") due to the expansion of on-line brokers with fewer registered representatives and the ability of firms to reduce their registered representative fee burdens by restructuring their businesses.[9] The exchanges decided to institute the ORF to make up for this lost fee revenue, and there was a clear consideration by the exchanges of how the fee was being paid by members in making this decision.

Finally, in making the argument about each exchange being an SRO like FINRA, the exchange Participants fail to acknowledge that even though they are legally SROs, many of them exercise little to no regulatory authority. Instead, many of them have completely outsourced their regulatory responsibilities to FINRA.[10] Given this dynamic and the unique role that FINRA currently plays as the not-for-profit self-regulator for the entire brokerage industry, it makes sense in the context of CAT funding to treat FINRA differently from the exchange Participants and to consider FINRA funding by Industry Members in connection this decision.

While we have not yet fully considered all the ways FINRA could be treated differently than the exchange Participants in the context of CAT funding, we do believe that such a different treatment is justifiable under the Exchange Act fee standards given the factors discussed above, including its treatment as not being a market center in the CT Plan and its broad regulatory role for the brokerage industry. For example, consistent with FINRA's treatment in the CT Plan as not being a market center, one approach would be to exclude FINRA entirely from the allocation of CAT cost to Participants and assess FINRA a nominal regulatory user fee to access CAT Data to perform its regulatory role, which includes performing regulatory duties for most of the exchanges. In this regard, we raised the concept of Participant user fees in our June 22 Letter as a mechanism to help pay CAT costs, which is an area that we believe has not been explored fully enough as part of CAT funding. Although the Participants dismissed this concept in their response to comments, perhaps a hybrid approach in which the exchange Participants continue to be treated as market centers responsible for their share of total CAT costs, with FINRA being charged a nominal regulatory user fee from the costs that would otherwise be assigned to Industry Members, could help serve as a path forward on establishing a viable funding model.

Clearing Broker Impact

We also share the concerns raised by the Commission's questions in the Order that the Executed Share Model fails the Exchange Act fee standards with regard to its treatment of clearing brokers in connection with Past CAT Cost. Regarding these Past CAT Costs, clearing brokers that seek to pass on these costs to their clearing clients would have tremendous difficulty in doing so. For instance, as we understand it, the Past CAT Costs Fee Rate would be based on

[9] See, e.g., Exchange Act Release No. 58817 (October 20, 2008), 73 FR 63744 (October 27, 2008) (https://www.sec.gov/rules/sro/cboe/2008/34-58817.pdf).

[10] See e.g., (https://www.finra.org/media-center/speeches-testimony/equity-market-surveillance-today-and-path-ahead).

current volumes as opposed to volumes that existed at the time the Past CAT Costs were incurred. This would create a very difficult exercise for clearing brokers in trying to devise a mechanism to assess these Past CAT Costs on existing clearing clients. This exercise would be made even more difficult due to the fact that new clearing clients have entered and old clients have left the business since these Past CAT Costs were incurred. It also could lead clearing brokers to choose different methodologies to assess Past CAT Costs on their clearing clients, leading to industry and end-customer confusion – the exact opposite of fair, predictable and stable CAT funding model. Rather than go through this complicated exercise if it is even possible, clearing brokers may be unfairly placed in a position of having to pay these Past CAT Costs themselves, thus shouldering an unfair burden of CAT costs on behalf of the industry and SROs. Such an outcome is inconsistent with the Exchange Act Fee standards.

We would also expect under the Executed Share Model that clearing brokers would be saddled with most of the implementation costs related to collecting Industry Member fees due to their role under the model. In this regard, the Executed Share Model takes a step backwards from the prior CAT funding model by changing the collection model process, switching it from the executing broker to the clearing broker. We therefore recommend that the Participants go back to the drawing board with regard to their decision to place the burden of collecting and paying the Industry Members' portion of CAT fees under the Executed Share Model on the clearing brokers.

We further recommend that the proposed approach of assessing Past CAT Costs through a transaction fee under the Executed Share Model be reassessed due to difficulty of using current volumes and trading activity by individual Industry Members as a mechanism for assessing costs incurred in the past where the trading volumes and individual Industry Member trading activity likely were different. The Participants themselves recognize the limitations of their proposed approach by discussing their decision to effectively ignore the impact on the model of firms that are no longer in business. The Participants also have not provided any data analysis regarding different alternatives for collecting Past CAT Costs, such as one based on historical volumes, as well as the costs associated with the current approach versus any potential alternative approaches. This type of data is needed to help demonstrate that any proposed collection mechanism regarding Past CAT Costs meets the Exchange Act fee standards. While we have not delved deeply into the issue of how to allocate Past CAT Costs in a manner that is consistent with the Exchange Act fee standards, we believe that this is an area that would benefit greatly from a dialogue between Industry Members and the Participants given that the amount of Past CAT Costs is approaching upwards of $400 million.

Cost Detail and Fee Setting Process

As we noted in our June 22 Letter, we continue to have significant concerns about the lack of an independent cost control mechanism for the CAT operating budget, as well as the lack of a reconciliation process for the CAT budget if actual costs exceed or are less than the budgeted CAT costs. The Commission in its Order similarly highlights certain process issues related to the Executed Share Model, asking for example for commenters' views on "whether it is necessary or appropriate in the public interest for the Proposed Amendment to permit the Fee Rate to potentially remain in effect even if the budget or projected executed equivalent share

volume changes (both would be used to calculate the Fee Rate under the Executed Share Model) or if the Fee Rate should sunset after a year."

We continue to strongly believe that the CAT needs an independent review mechanism of proposed CAT expenditures to help ensure that the process fosters appropriate and cost-effective CAT spending. In the absence of adding Industry Member representation to the CAT Operating Committee, this could be facilitated through public disclosure of detailed CAT costs that provides the industry and public with greater transparency into the actual costs, and not high-level categories of costs, so that the industry and public can actually evaluate and understand the spending choices made by the Participants, particularly those choices that relate to technology spending.

This could be further facilitated by creating a Commission review mechanism for the CAT operating budget, as we noted in our June 22 Letter. On this point, and contrary to the Participants' assertion in their response to comments, NMS plan and SRO fees are subject to Commission review under the Exchange Act. While the Participants appear to contemplate in the Executed Share Model a process in which they would not have to file the CAT budget each year with the Commission, we continue to believe that the Commission, which is charged under Rule 608 of Regulation NMS with reviewing NMS plan fees, would continue to need to be involved in reviewing the CAT operating budgets in a public process as contemplated by the rule. We also believe that specifically including line-item details about which CAT cost will be allocated back to the industry would provide additional discipline and needed transparency into such a process. We recognize the concerns about such a process leading to significant delays in adopting CAT operating budgets, but putting Industry Members in the position of having to wait to object to overall CAT costs when the individual SROs file fee changes to implement the current Fee Rate places Industry Members in the untenable position of trying to voice concerns about CAT spending after an operating budget has already been agreed to and approved if the process envisioned under the current Executed Share Model is approved.

We also agree with the Commission's questions in the Order related to the lack of detail or description by the SROs about how the CAT Fee Rate under the Executed Share Model would be implemented by each SRO to collect from Industry Members their share of the CAT costs. As the Commission indicates in the Order, individual SROs would need to file fee changes to implement the Fee Rate to be able to impose the fees on Industry Members. However, the SROs provide no detail in the Executed Share Model filing regarding this process, including any triggers and/or annual review mechanisms that would result in new fee filings in the future as a result of Fee Rate changes.

Allowing SROs to set a regulatory fee like the one contemplated in the Executed Share Model without some sort of trigger or automatic annual review of the fee is a significant and persistent problem that Industry Members have experienced in other contexts. For example, in the ORF context, this has led the options exchanges to establish fees based on volume numbers that quickly become outdated, leading to vast over-collections of the fees in the future as compared to the amount needed to recover costs. Absent triggers and/or annual review mechanisms that require the SROs to file fee changes each time a new annual Fee Rate is established, we could easily envision a scenario where the SROs choose not to file fee changes in

years where the prior CAT Fee Rate would lead to over-collections of CAT fees. We therefore recommend that the SROs develop an annual reconciliation process that requires the SROs to re-file the fee changes needed to cover the Fee Rate each year, such as a sunset provision as suggested by the Commission, so that the fees collected each year are specifically designed to cover that year's projected CAT costs.

Continued Lack of Support for Executed Share Model

As we note in our June 22 Letter, the Participants have not provided sufficient justifications regarding the Executed Share Model for the Commission to be in a position to approve it under the Exchange Act. For instance, the division of costs under the Executed Share Model, which is premised on the concept of there being three parties to every trade with one-third of the cost allocated to the execution venue Participants and two-thirds allocated to the buyer and seller Industry Members through clearing brokers, is not in a number of scenarios directly related to actual CAT reporting or the processing costs of CAT. For instance, the clearing broker for the buyer and/or seller is not always a party to the trade, but rather the clearer of the trade on behalf of the executing broker(s). In such a scenario, it could be the executing broker that is the CAT reporter(s) for the transaction, even though the clearing broker would be assessed the CAT fee for the transaction under the Executed Share Model. Similarly, the three-party approach under the Executed Share Model ignores activities that result in CAT costs but not in actual trades, such as unexecuted orders.

Similarly, the Participants seek to justify the Executed Share Model by comparing it to Section 31 fees, but then fail to address the significant differences between the proposed approach and the Section 31 fee approach. For instance, unlike the Executed Share Model, Section 31 fees are charged only on the sell side of a transaction and are based on the notional value of a trade. The Participants provide no analysis of why their proposed approach, as opposed to the notional value approach under Section 31, properly treats high-volume trades in low-priced stocks. The Participants also fail to analyze why it is appropriate to assess Industry Member any fees for the Past CAT Costs incurred when only the Participants were reporting to the CAT. The lack of further analysis by the Participants in these and other areas does not provide the Commission with sufficient data to allow it to articulate a satisfactory explanation for its approval of the proposed funding model, including a rational connection between the facts found and the choice made, as required under the D.C. Circuit's opinion in Susquehanna Int'l Grp., LLP v. SEC, 866 F.3d 442, 443 (D.C. Cir. 2017).

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SIFMA greatly appreciates the opportunity to submit this supplemental comment letter on the Executed Share Model. For the reasons discussed above, as well as in our June 22 Letter, we strongly urge the Commission to disapprove the proposed model. If you have any questions or require additional information, please do not hesitate to contact us by calling Ellen Greene at [redacted] or Joe Corcoran at [redacted].

Sincerely,

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SIFMA

Cc: The Hon. Gary Gensler, Chair
The Hon. Hester M. Peirce, Commissioner
The Hon. Caroline A. Crenshaw, Commissioner
The Hon. Mark T. Uyeda
The Hon. Jaime Lizarraga
Mr. Haoxiang Zhu, Director, Division of Trading and Markets