

MEMORANDUM

TO: File No. S7-11-10

FROM: Cristie L. March

DATE: May 8, 2013

SUBJECT: Meeting with Security Traders Association (STA) and Financial Information Forum (FIF)

On May 7, 2013, Commissioner Walter and Cristie March met with Jim Toes (President and CEO, STA), Tom Jordan (Advisory Committee Chair, FIF), and Manisha Kimmel (Executive Director, FIF) to discuss the consolidated audit trail.

Attachment



FIF – SEC Rule 613/CAT NMS Plan Discussion

April 18, 2013



Agenda



- FIF/SEC CAT Background/Meeting Objective
- View of SRO/FIF Interactions to date
- Discussion of Key Rule 613/CAT NMS Plan Implementation Issues:
 - Implementation Timelines
 - Broker Dealer Reporting of Options Market Maker Quotes
 - Clarification of Customer Definitions
 - Error Correction Process
- 2013 Outlook

FIF/SEC CAT Background/Meeting Objective



FIF focuses on providing an industry view of concerns/issues on the implementation of major initiatives. At this meeting, our objective is to have an interactive dialogue on the progress of the initiative and key implementation issues.

FIF/SEC CAT Activities to Date

- August 12, 2010 – Comment letter to SEC
- February 29, 2012 – Meeting with SEC
- March 2, 2012 – Comment letter to SEC
- Subsequent conversations with SEC staff

Previous topics covered:

- Industry participation in CAT definition and implementation
- RFP Process, Phased Implementation and Timeline
- Customer, Reporter and Order Identifiers
- Real-time Data Submission
- Clock Synchronization
- Elimination of overlapping regulatory rules/systems

SRO/FIF Interactions



Discussion of CAT reporting requirements:

- Customer definition scenarios and need to account for current institutional firm processes
- Allocation model – availability of information and ability to link
- Complex trading scenarios to address, including representative orders
- Need to address significant details (protocols, approach to elimination of rules/systems, risk mitigation, etc.) as early as possible

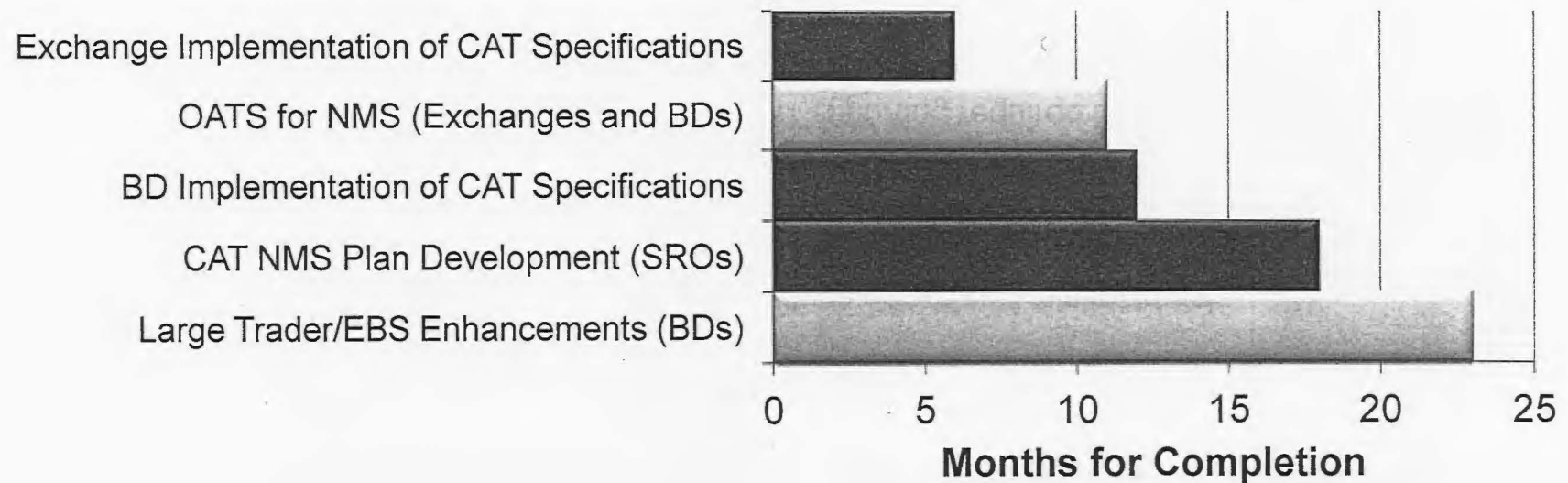
FIF Review/Activity to date:

- Provided comments to all SRO publications, identifying significant implementation issues
- SROs joined FIF calls to listen to member discussion of issues
- FIF provided additional detail as requested by SROs to clarify issues
 - Survey on Representative Orders
 - Customer ID Walk-thru scenarios

FIF participating in SRO Development Advisory Group (DAG).

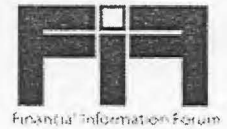
- First topic oriented meeting was April 3, 2013

CAT Implementation Time: Comparative Analysis



- Less time currently allocated for implementation of CAT specifications than for drafting of the NMS Plan
- Implementation schedule established in CAT RFP has exchange specifications released 12 months before broker dealer specifications
- Complexity of CAT implementation far exceeds OATS for NMS and Large Trader/EBS Enhancements
 - OATS for NMS: Specification change after 4 months
 - Large Trader/EBS Enhancements: Specification change after 10.5 months

Risk Mitigation Considerations



- Recommend implementation plans with collaborative design periods, sufficient development time for improved quality, and extensive testing periods.
 - Industry review of selected sections of RFP responses on CAT B/D related interfaces.
 - With early exposure and input into NMS Plan development, impediments to implementation can be identified and resolved with less impact.
 - New concepts included in CAT (e.g., customer definition process and reference data management, middle/back office impact with allocation reporting , options reporting) require broad changes to B/D customer management systems, front /middle/back office systems – a significant implementation effort for B/Ds. Stable specifications will improve the quality of the end products and reduce the implementation costs.
 - Industry-wide testing should be required on all CAT, exchange and B/D functionality.
- Recommend phased implementation plans to reduce errors and minimize risk.
 - Phased implementation by asset class (OTC equity and NMS stock in one phase, followed by options)
 - Incorporate the eliminations of overlapping rules/systems. In CAT roll-out plan. Through identification of the missing elements in CAT reporting required to eliminate systems, initial CAT reporting requirements can be enhanced so that overlapped rules/systems can be eliminated on CAT roll-out.
 - Phased rollout using first test securities, then a small subset of securities, then expansion to all securities within an asset class. Need to also consider phasing in terms of customer roll-out.

Broker Dealer Reporting of Options Market Maker Quotes



FIF believes limiting reporting of Options Market Maker (MM) quotes to exchanges would significantly reduce cost without impairing market surveillance or market reconstruction goals.

- Discussion of regulatory goals achieved by including broker-dealer reported options MM quotes in CAT in addition to exchange reporting of options MM quotes
- Exchanges have same information on quotes as broker dealers except:
 - Quote origination time – the time a MM creates a quote in its internal system.
 - MMs can choose to prioritize quotes internally to optimize bandwidth., resulting in internal queuing of quotes, so the Quote Origination time is of little meaning to external party.
 - There is no intermediary between MM and exchange., so the time a MM takes between origination and sending is of little interest to any external party.
 - Quote sending time – the time a quote is sent by MM to the exchange
 - There is no intermediary between the MM and the exchange so the delta between quote sending and receipt is minimal
 - The time that the quote reaches the exchange is the most relevant time since the market relies upon the exchange version of the book.
- Assume that quote initiations, not exchange-generated quote updates, are reportable by MM.
- The costs to implement essentially dual, duplicative reporting is significant.
 - Implementation and on-going maintenance costs to MM and CAT processor.
 - Significant technical challenges in matching MM and exchange quotes (time-skews, QRM's and in-flight messages, band-width restrictions).
 - Scaling of production, test, development systems to support 2 x 29B quotes/day.
- Discussion of alternate ways to achieve regulatory goals (e.g., could quote sending time be added to quoting protocols?)
- Discussion of next steps.

Clarification of Customer Definitions



Rule 613 - "The term **customer shall mean:**

- The account holder(s) of the account at a registered broker-dealer (originating the order) and ,
- Any person from whom the broker-dealer is authorized to accept trading instructions for such account, if different from the account holder(s)."

Clarification on definitions surrounding customer would be very helpful, and better scope the impact to B/Ds.

- A broker-dealer when routing orders to another firm is excluded from the definition of customer based on SEC 15c3-3.
- Customer refers to firm and not trader within firm (For Large Trader SEC Rule 13h-1, reporting for firm, not employees within firm).
- Customer account information is provided relative to the firm, and not officers of the corporation.

Today, firms maintain different levels of information on "Authorized trader" vs. "Account Holder".

Discussion on next steps, if any.

Experience-Based Error Correction Process



- Data quality is critical to market surveillance and reconstruction. A robust process for the timely identification and correction of errors is essential. To achieve that goal, the following is required:
 - Intelligent (and learning) matching algorithms to not only identify the error but provide direction in correcting the error.
 - Linkage breaks should not cause subsequent events to break.
 - CAT Reporter access to the data submitted so there is no dispute on different data views, plus eliminates CAT Reporter cost of data archive.
 - Continuous error correction process including continual matching as corrections are received and submission of corrections at any time.
- The scope of CAT reporting greatly exceeds current OATS requirements which allow for a 5 day error correction time. Without knowledge of CAT matching algorithms, error detection/correction tool sets, access to CAT data, CAT systems expertise, there is no justification to expect an improved error correction timeframes on initial delivery of system.
- Consider initial period of reporting with relief from enforcement action to gain experience and insight into improving reporting correctness.
- Consider reduction of error correction timeframe as CAT system and reporting mature.
- Discussion of next steps.

2013 Outlook



- SEC insight is invaluable to better understand and interpret Rule 613 and the CAT design and implementation process. Periodic checkpoints with the SEC on CAT would be most helpful to the industry.
- FIF will continue to review all materials available to provide early industry feedback on implementation and costs to help guide the CAT Processor to become an effective and cost-efficient tool for the industry.
- FIF is hopeful that the CAT Development Advisory Group will be a forum to address industry concerns.
- FIF will continue to seek timely dialog with the SROs to help identify and resolve any substantive implementation issues early in the CAT implementation plans to reduce re-work and delays inherent in late problem identification.
- Discussion of next steps.