



July 28, 2017

[Via Electronic Mail- rule-comments@sec.gov](mailto:rule-comments@sec.gov)

Mr. Brent J. Fields
Secretary, Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File Nos. SR-BatsBYX-2017-11; SR-BatsBZX-2017-38; SR-BatsEDGA-2017-13; SR-BatsEDGX-2017-22; SR-BOX-2017-16; SR-BX-2017-023; SR-C2-2017-017; SR-CBOE-2017-040; SR-CHX-2017-08; SR-FINRA-2017-011; SR-GEMX-2017-17; SR-IEX-2017-16; SR-ISE-2017-45; SR-MIAX-2017-18; SR-MRX-2017-04; SR-NASDAQ-2017-046; SR-NYSE-2017-22; SR-NYSEArca-2017-52; SR-NYSEMKT-2017-26; SR-PEARL-2017-20; or SR-PHLX-2017-37, Regarding Suspension of Consolidated Audit Trail Funding and Request for Comment on Proposed Rule Changes to Establish Fees for Industry Members.

Dear Mr. Fields,

This letter is being submitted in response to the Securities and Exchange Commission's ("SEC" or "Commission") July 7th, 2017 request for additional comments regarding the proposed funding structure for the Consolidate Audit Trail ("CAT") proposed by the Plan Participants. Belvedere Trading would like to comment on a variety of issues regarding the structure of the proposed fee schedule, the potential hardships and hazards it creates for certain market participants, and suggest a different, more efficient fee structure that would promote efficiency in implementation, and incentivize exchanges to build and operate the CAT in a manner that passes costs along to market participants more equitable manner.

A. A Fee Structure Based Purely on Messaging Tiers is Anti-Competitive and Will Unduly Impact Options Liquidity Providers Thereby Exacerbating the Current Environment of Decreasing Options Market Liquidity

As a significant provider of market-making liquidity across a variety of US option exchanges, Belvedere shares the concerns voiced in FIA's June 22, 2017 letter regarding the funding structure of the CAT. Put most simply, by focusing purely on messaging volume the CAT plan unfairly penalizes market making firms that provide liquidity through messaging-intensive quoting and trading, while offering outsized benefits (e.g. reduced regulatory processes and costs associated with the elimination of OATS reporting requirements) to larger firms that trade less frequently and fall into lower fee tiers. As a result of this disparity, the current fee structure proposal unduly penalizes market-makers relative to other market participants.

In addition, given the recent contraction in the number of market makers actively providing liquidity across the options markets, proposing to fund the CAT in a manner that levies an outsize burden on options market-making firms will likely have a chilling effect on market-maker activity. We also note from experience that, to compete in the options market making space, messaging at a Tier 1 level as defined by the CAT proposal is essentially a fixed overhead cost regardless of firm size or revenue, thereby creating an additional barrier to entry for new market makers and significantly increasing costs for smaller firms.

As discussed in Part C of this Comment, Belvedere believes that a more flexible fee structure which encourages competition and efficiency among exchanges is more in line with the SEC's guiding principles, particularly that "our rules and operations [must] reflect the realities of our capital markets", as emphasized by Chairman Clayton during his remarks to the Economic Club of New York on July 12, 2017.

B. The Proposed 75%/25% Split of CAT Funding is Wholly Out of Proportion to the Benefits Derived by Different Parties

As codified in 17 CFR 242.613(b), the language regarding the operation and administration of the CAT focuses almost exclusively on the "plan sponsors" (the Participants), and instructs them primarily to allocate costs to both current and future sponsors of the plan, without mentioning either broker-dealers or other customers of those plan sponsors. While 613 does mention broker-dealers and members of exchanges, it only mentions allocating any portion of costs to "members of the plan sponsors" once, and does not at any point instruct Participants to directly charge broker-dealers with funding the CAT.

Despite this, the nineteen exchange Participants have developed a unified implementation plan, and their exclusive control over this process has led to a proposed funding model that passes the majority of the costs directly to broker dealers. These additional costs, on top of the estimated direct implementation cost to broker-dealers of more than \$3.1 billion, and estimated annual maintenance costs for broker-dealers of roughly \$3 billion, make for an inequitable distribution of the overall funding burden for a project with questionable value and immense cost.

Furthermore, Participants themselves estimate a \$10.6 million minimum aggregate savings based on the retirement of legacy systems (not to mention the acknowledged additional cost savings made possible by the replacement systems). Participants have taken full control over the project, have chosen the plan processor, structured the CAT's entire corporate organization, and will allegedly reap both cost savings and greater efficiency in their duties as self-regulatory organizations. Choosing only to provide a quarter of the direct funding for the CAT is inconsistent with level of responsibility encapsulated in Rule 613 and alleged benefit to the Participants, especially given the multi-billion-dollar operational and compliance burden imposed on broker dealers under CAT's reporting obligations.

C. Abandon the Current Fee Structure and Require Participants to Directly Fund the CAT

Given that the Participants have exercised near total control over governance, organization, and implementation of the CAT, they are also best-situated to ensure that it is built and maintained in the most cost-effective manner. However, their current plan to shift three-quarters of the direct costs on to broker-dealers significantly reduces their incentive to carefully monitor and scrutinize the cost of the CAT.

Belvedere anticipates significant additional reporting costs from complying with the CAT, but we will manage our own internal costs of CAT compliance effectively through careful decision-making and leveraging our internal knowledge and staff abilities. Market participants however, despite bearing three-quarters of CAT funding, have no power over the implementation of the CAT, and cannot ensure that their fees are expended efficiently during the process. Without a significant voice in the process (as noted by SIFMA and FIA), the proposed fee structure effectively insulates the Participants from full accountability for their management decisions.

Belvedere believes that this issue can be resolved at a stroke by requiring the Participants to be directly responsible for the funding of the CAT. Given that broker-dealers like Belvedere trade primarily at the Participant's various exchanges, we anticipate that exchanges will then pass along the additional CAT-related costs to their membership in a form and manner tailored by exchange as they see fit. Thus, ultimately broker-dealers and other trading participants will still effectively fund the creation of the CAT, but Participants will be responsible for self-allocating their share of costs from the CAT.

This funding structure has a variety of advantages. First, as the Participants have noted in previous correspondence with the SEC, there is significant competition on pricing across the different exchanges. Given that Participants will want to remain competitive, they will thus be incentivized to manage CAT implementation in more cost-effective manner. Similarly, it will streamline overall billing costs by eliminating the need to calculate message volume and individual billing for each of the approximately 4400 broker-dealers in the US.

Second, allowing each of the Participants to individually decide how to "bake in" the costs of CAT implementation on an individualized basis gives Participants the discretion currently lacking from the proposed tier-based messaging volume criteria. Options market-makers will have greater freedom to choose how manage their messaging, and competition in pricing among the Participant's will promote a more appropriate allocation CAT costs.

Finally, Belvedere's proposed pricing structure would assuage market participant's concerns over potential conflicts of interest mentioned in the FIA's June 22, 2017 comment letter. If Participants instead absorb all CAT costs directly and individually pass them on to broker-dealers as they see fit, the potential conflicts of interest that are apparent in the proposed fee structure will be mitigated.

In conclusion, Belvedere urges the SEC to reconsider the proposed fee structure for CAT funding. A reshaped structure that places the funding burden on the Participants, and provides them with the flexibility to recover the costs as they see fit would undoubtedly promote a more effective and efficient CAT implementation in addition to a far more equitable distribution of costs.

Sincerely,

A handwritten signature in black ink, appearing to read "Kevin Coleman". The signature is written in a cursive style with a large initial "K" and a long, sweeping underline.

Kevin Coleman
General Counsel & Chief Compliance Officer
Belvedere Trading LLC