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July 28, 2017

Brent J. Fields  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-0609

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

Dear Mr. Fields:

The FIA Principal Traders Group (“FIA PTG”)<sup>1</sup> appreciates the opportunity to further comment on the above-captioned proposed rule changes (the “Proposals”). In our First Letter on the Proposals<sup>2</sup> we expressed our concern with the lack of collaboration with the impacted industry participants in the design of the Consolidated Audit Trail (“CAT”) funding model. We remain concerned about the lack of inclusion in the approach taken by the Plan Participants, but applaud the U.S. Securities and Exchange Commission (“the Commission”) for suspending the Proposals and allowing for broad industry input, albeit quite late, through this comment process. Whether the CAT as designed is the optimal data collection model is a debate best left for another day – FIA PTG supports data-driven decision making and accordingly is supportive of providing regulators, including self-regulatory organizations (“SROs”) like the Plan Participants, with the

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<sup>1</sup> FIA PTG is an association of more than 20 firms, many of whom are broker-dealers, who trade their own capital on exchanges in futures, options and equities markets worldwide. FIA PTG members engage in manual, automated and hybrid methods of trading, and they are active in a wide variety of asset classes, including equities, fixed income, foreign exchange and commodities. FIA PTG member firms serve as a critical source of liquidity, allowing those who use the markets, including individual investors, to manage their risks and invest effectively. The presence of competitive professional traders contributing to price discovery and the provision of liquidity is a hallmark of well-functioning markets. FIA PTG advocates for open access to markets, transparency and data-driven policy and has previously made recommendations about a variety of equity market structure issues, including Regulation NMS (See <https://ptg.fia.org/keywords/equity-market-structure>).

<sup>2</sup> <https://www.sec.gov/comments/sr-cboe-2017-040/cboe2017040-1819670-154195.pdf>. “First Letter” Except as may be modified in this letter, we reaffirm and incorporate herein by reference our previous comments on the Proposals.

data they need to ensure our markets operate efficiently and effectively for the market participants that use them. That being said, we continue to have concerns with many specific aspects of the Proposals including: the cost allocation methodology, the use of inconsistent metrics, the disproportionate impact on options market-makers, the lack of transparency, conflicts of interest, and the governance of the CAT NMS, LLC (“the Company”). The remainder of this letter expands on these concerns.

### **Proposed Cost Allocation Methodology is Fundamentally Flawed**

As we noted in our First Letter, there are existing electronic audit trails in place, the most predominant being FINRA’s Order Audit Trail System (“OATS”). Under the OATS cost allocation model, the costs of managing the SRO portion of the system are incurred by the SRO and then allocated out to market participants as they see fit. One way to address the inherent conflicts of interest in the Proposals, would be to apply the OATS cost allocation model to the CAT. The use of this model would allow the Company the flexibility to divvy up 100% of the costs across its ownership (the Plan Participants) in whatever manner it deems appropriate. In turn each Plan Participant could determine how those costs would be passed on to market participants trading on their venue. Not only would this type of methodology obviate the need to resolve the current 75/25 debate, but it would incentivize the Plan Participants to manage the costs of the CAT. In addition, it would encourage each Plan Participant to look for efficient and creative ways to manage their individual cost allocation and might even facilitate Plan Participants competing with each other on how these costs are passed on to market participants.

### **The Use of Inconsistent Metrics is Discriminatory**

Plan Participants have recognized that message traffic is an inequitable metric to drive cost allocations, yet the Proposals use message volume as the sole apportionment metric for applying fees to market participants. While we have concerns with using message traffic to determine fees, we believe that whatever metric is used should be applied across the board when determining cost allocations. In their June 29, 2017 letter,<sup>3</sup> the Plan Participants state that larger broker-dealers generate more message traffic, whereas “the Participants believe that equity exchanges produce similar volumes of message traffic regardless of their size, and similarly, that options exchanges produce similar volumes of message traffic regardless of their size. Therefore, if exchange Execution Venues were charged based on message traffic, large and small exchanges would pay comparable fees, thus making the fee structure inequitable.”<sup>4</sup>

Further to our First Letter, if the biggest driver of the cost of the CAT is indeed the processing and storing of messages, then we fail to see why this point, even if true, is relevant. The Proposals address cost allocation, not size of market participant or exchange, and if message traffic is what generates the costs, then all participants – both Plan Participants and market participants – should be assessed based on the same metric. Unfortunately, what is good for the goose does not appear to be good for the gander and the inconsistent approach is inherently discriminatory. Please see below for how this approach disproportionately impacts options market-makers.

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<sup>3</sup> <https://www.sec.gov/comments/sr-batsbyx-2017-11/batsbyx201711-1832632-154584.pdf> (“Plan Participants Response”)

<sup>4</sup> Plan Participants Response at 6.

### **The Proposals are Particularly Punitive for Options Market-Makers**

Options market-makers, regardless of size, generate high volumes of message traffic in order to meet their obligation to quote thousands of options strikes and series. The Proposals are very prescriptive in allocating the costs of the CAT and allow no flexibility for nonidentical treatment by market participant type. Accordingly it appears that many options market-makers will find themselves in the highest tiers and may incur a disproportionate percentage of the CAT costs. This situation further supports our suggestion that all CAT costs be allocated to the Plan Participants and that how, and to whom, the Plan Participants allocate their costs be left to each venue to determine.

### **The Proposals Lack the Transparency Promised by the Plan Participants**

After review of the Proposals, we are left with more questions than answers about the costs and related fees for the CAT. The Plan Participants responded to criticisms about the creation of a CAT-specific fee in a September 23, 2016 letter.<sup>5</sup> “Moreover, by adopting a CAT-specific fee, the Participants will be fully transparent regarding the costs of the CAT. Charging a general regulatory fee, which would be used to cover CAT costs as well as other regulatory costs, would be less transparent than the proposed approach of charging a fee designated to cover CAT costs only.”<sup>6</sup> After reviewing the Proposals we are struggling to identify the transparency that was promised. The detail required to determine what is actually being paid for via CAT fees and what can be expected in return for the payment of those fees is not available. As such, we are able to comment on the relative fee allocation, but it is an impossible task to opine on whether or not the fees being charged are fair or not.

### **The Plan Participants have a Conflict of Interest**

Further to our First Letter, we continue to believe that the Plan Participants have a conflict of interest when it comes to determining how much of the cost of this endeavor they should bear. The Plan Participants briefly responded to this concern in their June 29, 2017 letter. “The Plan establishes a funding method that operates the CAT NMS, LLC on a break-even basis – that is, the fees imposed and collected would be intended to cover CAT costs and an appropriate reserve for CAT costs. Any surpluses would be treated as an operational reserve to offset fees in future payment.”<sup>7</sup> The Plan Participants have explained that the Company will not generate any profits, however we remain unconvinced that the break-even basis of the venture addresses any potential conflicts. Complete control of the source of the costs remains with the Plan Participants, while 75%+ of the burden of maintaining the “break-even” construct is placed on market participants.

### **Plan Governance does not Incentivize Aggressive Cost Management**

In addition to our concerns with the lack of inclusiveness in the development of the funding model, we are concerned with the lack of industry participation in the oversight of the Company. Based on our understanding of the structure of the Company, the majority of CAT fee payers – the group to which 75%+ of the costs have been allocated – have no role in its governance. What incentive do the Plan Participants have to manage the costs aggressively when by some estimates only 12% of those costs will be borne by the Plan Participants themselves? We fear the answer to that

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<sup>5</sup> <https://www.sec.gov/comments/4-698/4698-32.pdf> (“Plan Participants Response II”).

<sup>6</sup> Plan Participants Response II at 10.

<sup>7</sup> Plan Participants Response at 11.

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question is – none. Absent exiting the business, what recourse do market participants have? Again, we fear the answer is – none.

In summary, the proposed CAT pricing model is fundamentally flawed given the conflicts of interest in its design. It will risk further harm to market structure by encouraging cost inefficiency and discouraging options market-making. For all of the aforementioned reasons, FIA PTG again respectfully urges the Commission not to approve the Proposals. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Joanna Mallers (██████████).

Respectfully,

FIA Principal Traders Group

A handwritten signature in blue ink that reads "Joanna Mallers". The signature is written in a cursive style and is placed on a light yellow rectangular background.

Joanna Mallers  
Secretary

cc: Walter J. Clayton, Chairman  
Michael S. Piwowar, Commissioner  
Kara M. Stein, Commissioner