sifma

Invested in America

March 5, 2024

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

Re: Consolidated Audit Trail ("CAT") Fee Filings from the Self-Regulatory Organizations ("SROs")

Dear Ms. Countryman:

The Securities Industry and Financial Markets Association ("SIFMA")[1] respectfully submits this comment letter to the U.S. Securities and Exchange Commission (the "Commission") in response to the rule filings by the SROs to establish fees for Industry Members related to certain historical costs of the National Market System Plan Governing the Consolidated Audit Trail (the "CAT NMS Plan" or "Plan") incurred by the SROs prior to January 1, 2022 ("CAT Fee Filings").[2] For the reason set forth below, we believe that the CAT Fee Filings should be disapproved because they do not meet the requirements governing SRO fees in the Securities Exchange Act of 1934 ("Exchange Act"), which requires such fees to be (i) reasonable, (ii) equitably allocated, (iii) not unfairly discriminatory, and (iv) not an undue burden on competition.[3] We strongly agree with the Commission's decision under Section 19(b)(3)(C) to temporarily suspend the CAT Fee Filings and issue orders instituting proceedings ("OIPs") to determine whether to approve or disapprove them under the Exchange Act.

---

[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, e.g., Release No. 34-99363 (January 17, 2024), 89 FR 10850 (February 13, 2024) (SR-FINRA-2024-002). This comment letter also applies to the other CAT Fee Filings by the SROs: SR-BOX-2024-03, SR-CboeBYX-2024-002, SR-CboeBZX-2024-004, SR-C2-2024-002, SR-CboeEDGA-2024-002, SR-CboeEDGX-2024-005, SR-CBOE-2024-003, SR-IEX-2024-01, SR-LTSE-2024-02, SR-MEMX-2024-01, SR-EMERALD-2024-01, SR-PEARL-2024-02, SR-BX-2024-002, SR-GEMX-2024-02, SR-ISE-2024-02, SR-MRX-2024-01, SR-Phlx-2024-01, SR-NASDAQ-2024-001, SR-NYSE-2024-03, SR-NYSEARCA-2024-02, SR-NYSEAMER-2024-02, SR-NYSECHX-2024-02, and SR-NYSENAT-2024-01.

[3] See Sections 6 and 15A of the Exchange Act.

The CAT Fee Filings follow the Commission's approval in September 2023 of the SROs' revised funding model for the CAT ("CAT Funding Model"),[4] which created the framework for the SROs as the CAT NMS Plan Participants ("Participants") to establish and collect fees from Industry Members to cover both historical and future CAT costs incurred by the Participants. The fees imposed under CAT Fee Filings would be payable to Consolidated Audit Trail, LLC starting in April 2024 based on March 2024 trading activity. The Participants refer to the fees as "Historical CAT Assessment 1" and as noted, they are designed to recoup CAT costs incurred by the Participants prior to January 1, 2022. This would include costs incurred by the Participants during the period from June 22, 2020 to December 31, 2021 in which they were subject to the Commission-imposed financial accountability milestones ("FAMs") 1 through 3 related to completion of the CAT.[5] The Commission imposed the FAMs on the Participants in May 2020 to increase "the Participants' financial accountability for the timely completion of the consolidated audit trail."[6]

As a threshold matter, we continue to believe the CAT Funding Model is not consistent with the Exchange Act and the CAT Fee Filings are further evidence of this. In the CAT Funding Model, the Commission approved and committed to a process in which the reasonableness of CAT fees and their satisfaction of the other Exchange Act fee requirements would be evaluated through rule filings submitted by the SROs under Section 19(b) of the Exchange Act. [7] Yet the process created by the CAT Funding Model is one in which the SROs are allowed to file CAT fees for immediate effectiveness under Section 19(b)(3)(A) of the Exchange Act without any requirement that the Commission affirmatively determine that the fees meet these Exchange Act requirements.[8] Unless the Commission suspends the CAT fees and institutes proceedings, there will be no Commission finding in any current or future CAT fee filings that the fees are reasonable, equitably allocated and otherwise meet Exchange Act fee requirements.

---

[4] See Release No. 34-98290 (September 6, 2023), 88 FR 62628 (September 12, 2023). Capitalized terms not otherwise defined in this letter have the same meanings as they do in the CAT NMS Plan and/or the CAT Funding Model.

[5] In May 2020, the Commission amended the CAT NMS Plan ("May 2020 Amendments") to include financial accountability milestones to incentivize the Participants to complete the CAT in a timely manner. See Release No. 34-88890 (May 15, 2020), 85 FR 31322 (May 22, 2020).

[6] Id.

[7] In this regard, for example, the Commission noted in its CAT Funding Model approval order that "[o]nce the proposed Section 19(b) fee filings are filed by the Participants, the Commission will review them for consistency with the Exchange Act and the CAT NMS Plan." See CAT Funding Model at 62663. The Commission also noted that "[e]ven if the Participants decide to pass-through the costs of CAT to Industry Members, however, in our view, the rule filing process under Section 19(b) and Rule 19b-4 will still incentivize the Participants to control costs. Any effort to pass-through costs will be subject to that process and, if the Participants fail to control costs, their ability to demonstrate that a proposed fee is reasonable and consistent with the Exchange Act may be compromised." See CAT Funding Model at 62636.

[8] This is the completely opposite approach to the one the Commission recently took in amending Rule 608 of Regulation NMS, in which the Commission eliminated the ability of NMS plan participants to file fee changes for fees charged under the plans for immediate effectiveness. See Release No. 34-89618 (August 19, 2020), 85 FR 65470 (October 15, 2020). Now, such fee filings must be published for comment and approved by the Commission before they can become effective.

The CAT Fee Filings directly demonstrate these flaws with the CAT Funding Model. As permitted under the model, the Participants submitted the filings for immediate effectiveness at the beginning of January 2024, seeking to force Industry Members to build entirely new systems and processes to validate and pay CAT fees by March 1, 2024. In the filings, the Participants are seeking to pass along to Industry Members virtually all historical costs incurred by them through the proposed CAT fees regardless of the reasonableness of passing along such costs. Absent the Commission's intervention here, Industry Members would have been faced with the impossible task of building new systems and processes to pay such fees in two months without any Commission evaluation of the reasonableness of the fee collection process or the fees themselves.

As described below, the Commission should disapprove the CAT Fee Filings because they do not meet the Exchange Act fee requirements as well as the requirement in Section 11.1 of the CAT NMS Plan that CAT costs be fairly and reasonably shared among the Participants and Industry Members. In particular, the Participants through the CAT Fee Filings:

- Seek to establish an unreasonable fee collection process under which Industry Members are not afforded sufficient time to verify the accuracy and completeness of the CAT billing data, build new systems and processes to validate and pay CAT fees, or evaluate whether the fees meet the Exchange Act fee standards, including whether the fees are reasonable and equitably allocated;

- Seek to impose unreasonable fees on Industry Members by allocating to them inappropriate CAT costs that were (and continue to be) unconstrained by any controls or limits; and

- Have not demonstrated that they have met FAMs 1 through 3, as the Participants are required to do under the CAT Funding Model and CAT NMS Plan prior to collecting any fees for historical CAT costs. Therefore, under the terms of the FAMs, they are not entitled to recover 100% of the costs incurred during the period covered from FAMs 1 through 3.

Each of these points is discussed in more detail below.

A number of these flaws with the CAT Funding Model, as evidenced by the CAT Fee Filings, are subject to litigation in which certain affected groups are challenging the Commission's approval of the CAT Funding Model in the Eleventh Circuit.[9] In SIFMA's amicus brief in support of vacating the Commission's approval, we include arguments that the Commission's imposition of uncontrolled CAT costs on broker-dealers and investors through the approval of the CAT Funding Model is unlawful.[10] Given the Eleventh Circuit's review of the CAT Funding Model on which the CAT Fee Filings are based, SIFMA urges the Commission to halt the process for consideration of the CAT Fee Filings until the fate of the funding model is clear.

[9] Am. Sec. Ass'n v. SEC, No. 23-13396 (11th Cir.) (filed Oct. 17, 2023).

[10] Dkt. 61, Am. Sec. Ass'n v. SEC, No. 23-13396 (11th Cir.) (filed Feb. 15, 2024).

I. The CAT Fee Filings Seek to Establish an Unreasonable Fee Collection Process

The Participants through the CAT Fee Filings seek to establish an unreasonable fee collection process under which Industry Members are not provided with sufficient time to build new systems and processes to validate and pay CAT fees or to evaluate whether those fees meet the Exchange Act fee standards. As noted, we greatly appreciate the Commission's issuance of the OIPs to determine whether to approve or disapprove the CAT Fee Filings. Under the OIP process, the Commission has up to 240 days to make such a decision.[11] We fully expect that during these proceedings, Industry Members will be given sufficient time to create new systems and processes to handle CAT billing.

Since the submission of the CAT Fee Filings (and even before), Industry Members have been grappling with a number of challenges that need to be adequately addressed for them to be ready to handle CAT billing. One such challenge relates to the Participants' decision under the CAT Funding Model to only assess CAT fees on broker-dealers defined as Executing Brokers. Even though these firms often execute orders for other broker-dealers, they are named in the CAT transaction reports and thus are the only firms assessed CAT fees under the CAT Funding Model. One effect of this Participant decision is that such firms need to evaluate whether and how they might pass through CAT fees to other broker-dealers that sent orders to them. In addition to the Exchange Act requirement that SRO fees be equitably allocated, the CAT NMS Plan provides that CAT "fees, costs and expenses shall be fairly and reasonably shared among the Participants and Industry Members."[12] Consistent with these requirements, Executing Brokers should be provided with sufficient time to build systems and processes to handle CAT billing, including whether and how they might pass through CAT fees to other broker-dealers.

Another challenge that Executing Brokers and other Industry Members are grappling with in connection with preparing for CAT billing is their need to build new systems and processes to be in a position to pay CAT bills. Particularly for Executing Brokers, this includes establishing reconciliation processes to ensure that they are being billed the correct amounts. It is important to keep in mind that Executing Brokers and other Industry Members are subject to their own obligations as broker-dealers to make sure they maintain accurate books and records, including GAAP requirements under the SEC's net capital rule (Exchange Act Rule 15c3-1) and audits subject to the standards of the Public Company Accounting Oversight Board. In addition, certain Executing Brokers and other Industry Members are public companies subject to the various accounting and disclosure requirements under the federal securities laws.

Despite Participants' assertions to the contrary, the CAT invoices and fees are entirely different from the regulatory bills Industry Members receive and pay currently. For instance, CAT fees are assessed on both the buyer and seller in a transaction, unlike Section 31 fees that are assessed only on the seller. In addition, CAT fees are assessed on the executed equivalent share volume in a transaction, which includes a special adjustment for listed options and OTC equity transactions. This is entirely different than the Section 31 methodology, which is based

[11] See Exchange Act Section 19(b)(2)(B).

[12] See Section 11.1(c) of the CAT NMS Plan.

on the notional amount of the transaction. Thus, Industry Members are faced with the task of building new systems and processes to handle CAT billing. For some Executing Brokers, this includes establishing reconciliation processes that look at their own trading data, determine whether and on which trades they expect to be billed CAT fees, and then comparing that data to the FINRA CAT data provided in the sample invoices. Building, testing, and troubleshooting these new systems and processes takes time.

The inability of Executing Brokers to reconcile their order and trade data with the FINRA CAT data has made this undertaking even more difficult and lengthy. Since the sample invoices were provided to Executing Brokers during the last week of December 2023, Executing Brokers have been carefully reviewing them and comparing them with their own data to confirm that they are accurate. Such firms have noted high mismatch rates between their data and the FINRA CAT data, with one firm indicating that the mismatch rate in January 2024 was approximately 40%, meaning that the firm is only seeing an approximately 60% match rate between the trades on which it expected CAT fees and the trades that are being assessed CAT fee in the FINRA CAT December 2023 sample invoices. These material discrepancies need to be resolved prior to CAT billing going live. We direct the Commission to the comment letter from the Financial Information Forum for a detailed discussion of the current reconciliation challenges Industry Members are facing.

One of the most troubling issues Executing Brokers have discovered during this process of preparing for CAT billing is that certain options exchanges are reporting to CAT the "give up" clearing firm as the Executing Broker for certain trades such as floor transactions, even though the clearing firms was not involved in executing the transaction at all (other than clearing it). Not only is this causing reconciliation issues, but it also calls into question the validity and consistency of the data exchanges are reporting to CAT and the regulatory utility of that data.[13] Given the CAT's regulatory purpose of being an audit trail for order and trading activity in equities and listed options, it is unclear why a clearing firm that had nothing to do with executing an options transaction would be reported to CAT as the Executing Broker.[14] As they have done with other issues they have discovered in preparing for CAT billing, Industry Members have reported this issue to FINRA CAT.

Ultimately, Executing Brokers' current inability to reconcile their data with the FINRA CAT data is preventing them from understanding whether they are being billed the correct amount by FINRA CAT and the Participants. To the extent that Executing Brokers may pass on their assessed CAT fees to other Industry Members that initiated the orders, these reconciliation challenges are preventing such Executing Brokers from setting up processes to do so and to provide fee estimates to such Industry Members. Most significantly, these challenges are

[13] This further validates our points in our comment letters on the CAT Funding Model that the term "executing broker" does not have a universally agreed-upon meaning within the industry. See, e.g., (https://www.sec.gov/comments/4-698/4698-199319-399182.pdf).

[14] We also question what sort of oversight the Commission is exercising over the SROs to ensure that they are properly reporting to the CAT. Industry Members are subject to close oversight regarding their CAT reporting by FINRA, as well as regulatory actions by FINRA if they have failures related to such reporting. This does not appear to be the case with regard to SRO reporting to the CAT, which is overseen by the Commission.

preventing Industry Members as a group from understanding whether the CAT fees are consistent with the Exchange Act fee standards.

These reconciliation challenges are further evidence of the Participants' misguided decision to assess CAT fees solely on Industry Members defined as "CAT Executing Brokers" in the CAT Funding Model. Despite repeated warnings from SIFMA and others about the challenges such firms would face in creating new systems and processes to pay such CAT fees, the Participants disregarded these concerns and went ahead with the approach.[15] Unfortunately, the Commission compounded the problem by approving the CAT Funding Model, including the assessment of CAT fees solely on Executing Brokers, based on the Participants' stipulations that the FINRA CAT would be able to provide the industry with billing files that can be used for reconciliation. However, it was not until over two months after the SEC approved the funding model that FINRA CAT was able to provide the industry with an initial set of billing files. Based on this data, it is now apparent that there are substantive impediments to using these files for reconciliation purposes:

- partly because of the flawed model of basing bills on only the Executing Broker;
- partly because the bills are not produced directly from Industry Member CAT data, but rather are based on indirect reports of Industry Member activity by the Participants providing such information to CAT;
- partly because of missing or irreconcilable identifiers; and
- partly because in certain cases it seems that for quite some time certain Participants may not have been sending fully correct data to FINRA CAT.

After the sample invoices were provided, the challenges with the Participants' decision to assess only Executing Broker in the CAT Funding Model have become very apparent.

Now that the Commission and industry have learned of the significance of these challenges, SIFMA believes that further consideration should be given to amending the CAT NMS Plan to assess CAT fees on the broker-dealer that originated the order (i.e., the originating broker) rather than the Executing Broker. Among other things, the Participants and FINRA CAT noted in response to the comments about billing the originating broker that such an undertaking would involve multiple steps at FINRA CAT to find the originating broker. However, given the much better understood challenges and costs Industry Members are facing with the Executing Broker approach, it seems even more prudent and cost-effective to have FINRA CAT perform this function rather than having hundreds and perhaps even thousands of Industry Members perform it.

[15] Various groups commented on these challenges and attempted to meet with the CAT Operating Committee in groups and individually to discuss it, urging the urged the Participants to bill the broker-dealer that originated the order rather than the Executing Broker. Id. The Operating Committee and individual exchanges refused to entertain such a change.

II. The CAT Fee Filings Seek to Impose Unreasonable Fees on Industry Members

In contravention of the Exchange Act fee requirements, the Participants through the CAT Fee Filings are seeking to impose unreasonable fees on Industry Members by allocating inappropriate CAT costs to them. While SIFMA members have only had a few weeks to review the cost items described in the CAT Fee Filings that would be passed on to them, and the filings themselves lack necessary detail, they have initially identified several CAT costs items incurred by the Participants that are inappropriate to be allocated to Industry Members. Several of these CAT cost items are described below. As SIFMA members review more closely the cost items in the CAT fee filings that would be passed on to them, they may also raise other cost items with the Commission that would result in unreasonable fees being imposed on Industry Members. We are concerned that under the paradigm established by the Commission-approved CAT Funding Model, Commission decisions about the reasonableness of the pass-through of certain historical costs will establish precedent for the Participants to try to recoup such costs down the road in future fee filings. This dynamic further demonstrates the problems with the CAT Funding Model, which is a badly flawed mechanism to pay for the CAT.

1. The Participants' Legal Costs Related to CAT Liability

Perhaps the most egregious CAT cost item that the Participants are seeking to pass on to Industry Members through the CAT Fee Filings are the legal bills from Pillsbury Winthrop Shaw Pittman LLP ("Pillsbury") and Covington & Burling LLP ("Covington") incurred by them when they unsuccessfully sought to limit their liability in connection with owning and operating the CAT by seeking to pass on their liability to Industry Members. The Participants initially sought to accomplish this limitation of liability by trying to force Industry Members to sign CAT Reporter Agreements that limited the Participants' liability in connection with a CAT data breach or loss. Through SIFMA-led litigation before the Commission, SIFMA members successfully stopped that Participant effort and incurred significant legal expenses in doing so.[16]

Subsequently, the Participants unsuccessfully sought to amend the CAT NMS Plan to limit their liability, which the Commission disapproved in October 2021, finding among other things that "for situations where regulatory immunity may not be applicable (e.g., commercial use or intentional misconduct), the Participants have not met their burden to justify a nearly complete elimination of liability to Industry Members as consistent with the Exchange Act and the rules and regulations as required by Rule 608 of Regulation NMS."[17] Under these circumstances, it is completely inappropriate for Industry Members to be responsible for any costs related to these unsuccessful Participant efforts, which were solely designed to advance the Participants' position at the expense of Industry Members. Consistent with our comment above about the CAT Fee Filings lacking necessary detail, the Participants have not broken out the costs incurred from Pillsbury and Covington in the filings, but rather have lumped all of their legal expenses together in the filings. Nonetheless, all legal fees from Pillsbury and Covington,

[16] In the Matter of the Application of Securities Industry and Financial Markets Association for Review of Action Taken by CAT LLC and Certain Self-Regulatory Organizations in Violation of Exchange Act Sections 19(d) and 19(f), Admin. Proc. File No. 3-19766 (SEC filed Apr. 22, 2020)

[17] See Release No. 34-93484 (October 29, 2021), 86 FR 60933 (November 4, 2021).

who represented the Participants in these failed efforts, should be excluded from being passed on to Industry Members and the CAT Fee Filings should be amended to reflect this.[18] The filings also should be amended to provide greater transparency regarding the services provided by the law firms used by the Participants because, as discussed below, these services likely include ones for which Industry Members should not be assessed costs.

2. The Participants' Costs Related to Kingland Systems

The costs related to FINRA CAT's failed decision on behalf of the Participants to hire Kingland Systems ("Kingland") to build the CAT Customer and Account Information System ("CAIS") database (including their management of them during the project) is another inappropriate cost item that the Participants are seeking to pass on to Industry Members though the CAT Fee Filings. Under the CAT NMS Plan, the CAT CAIS database is the repository that will hold all of the equity and listed options customer and account information. It was supposed to be completed by December 31, 2022 in accordance to the Commission's FAM 4 milestone, which requires the Participants to effectively finish building the CAT by that date. It is now more than a year after that date and the CAIS database is still not completed.[19] We also understand that the Participants have terminated Kingland's contract. Like the Participants' failed decision to initially hire Thesys as the Plan Processor, it is completely inappropriate for the Participants to pass along any Kingland-related costs to Industry Members because they had no say in the decision to hire Kingland as a vendor and Kingland has failed to deliver on the task for which it was hired. Based on the CAT Fee Filings, the $9,480,587 in Kingland costs should not be passed on to Industry Members and the CAT Fee Filings should be amended to reflect this.[20] This amount likely will be greater once the Participants provide more detail in the filings regarding legal expenses, as we expect that they have also incurred legal expenses associated with terminating their contract with Kingland.

3. The Participants' Costs Related to Thesys Technologies LLC

Along these lines, the Participants correctly realized in the CAT Funding Model that they should not pass along costs related to their failed decision to initially hire Thesys Technologies LLC ("Thesys") as the Plan Processor (including their management of them during the project). Like Kingland, Industry Members had no say in the decision to hire Thesys and Thesys failed to perform the task for which it was hired. The Participants terminated their contract with Thesys. Despite the failed performance by Thesys, the Participants in the CAT Fee Filings still are seeking to pass along to Industry Members certain costs related to their contract with Thesys. Specifically, even though they had a contract with Thesys from January 17, 2017 through

[18] We note that SIFMA and its members incurred substantial legal bills challenging these inappropriate Participant efforts.

[19] The Participants are requesting exemptive relief from the FAM 4 deadline. See (https://www.catnmsplan.com/sites/default/files/2023-06/05.22.23-Exemption-Request-Regarding-FAM-4.pdf). SIFMA has submitted a letter to the Commission opposing this relief request. See (https://www.sifma.org/resources/submissions/sros-fam-4-exemptive-request/).

[20] Based on the CAT Fee Filings, these Kingland costs consist of $2,072,908 for the Pre-FAM period, $254,998 for the FAM Period 1, $1,590,298 for the FAM Period 2, and $5,562,383 for FAM Period 3, which totals to $9,480,587 in Kingland costs.

January 30, 2019, the Participants are seeking to exclude from being passed along to Industry Members only to those Thesys-related costs they incurred from November 15, 2017 through November 15, 2018 ("Thesys Exclusion Period"). In other words, the Participants are seeking to pass along Thesys-related costs incurred before and after the Thesys Exclusion Period to Industry Members. However, the Participants in the CAT Fee Filings do not adequately support why it is appropriate for them to exclude only those costs incurred in the Thesys Exclusion Period, particularly since Thesys was engaged for nearly two years. The Participants should provide more detail about the costs incurred and work performed by Thesys in the two and half month period from November 16, 2018 through January 30, 2019 for which they claim costs should be recovered. Detailed information about the work performed during that period is essential for the Commission and the Industry Members to assess the Participant's assertion that those costs are recoverable.

While it is difficult to piece together based on the CAT Fee Filings, the Participants appear to have incurred $71,475,941 in Thesys-related costs during the Participants' contract with them. Despite Thesys's failed performance and countless hours of Industry Members' time, the Participants in the filings are seeking to exclude only $48,874,937 of these Thesys-related costs incurred during the Thesys Exclusion Period from being passed along to Industry Members.[21] However, it is not clear from the filings why any Thesys-related costs should be passed along to Industry Members, especially since the Participants have already made the determination in the CAT Funding Model and CAT Fee Filings that certain of these costs - the ones incurred during the Thesys Exclusion Period - should be excluded. Moreover, there is no acknowledgment of the indirect costs Thesys imposed on Industry Members. In considering the reasonableness of the fees imposed by the CAT Fee Filings, the Commission must not ignore the indirect costs incurred by Industry Members from the Participants' failed decision to hire Thesys.[22]

Moreover, the Participants do not address in the CAT Fee Filings why it is appropriate to pass along to Industry Members any costs related to transitioning from Thesys to FINRA CAT as the Plan Processor. Participants incurred these costs as a direct result of their decision to initially hire Thesys. Based on their representations in the CAT Fee Filings, the Participants correctly exclude $14,749,362 of costs related to terminating the relationship with Thesys, which the Participants represent includes costs related to the American Arbitration Association, the legal assistance of Pillsbury with regard to the arbitration with Thesys CAT, and the settlement costs related to the arbitration with Thesys CAT. The Participants, however, fail to address why it is appropriate to pass along any costs related to transitioning the Plan Processor role from Thesys to FINRA CAT. We continue to believe that all costs related to the Participants' failed decision to hire Thesys as the Plan Processor should be excluded, including costs related to the transitioning to FINRA CAT as the Plan Processor, and not just the ones incurred during the proposed Thesys Exclusion Period. Accordingly, the CAT Fee Filings should be amended to

[21] The Participants represent that these Excluded Costs also include legal and consulting fees incurred by them during this time.

[22] See Bloomberg L.P. v. SEC (D.C. Cir. 2022) ("In this case, the Commission's failure to respond to relevant and significant comments about the direct and indirect costs of FINRA's proposed data service was sufficient to render its decision arbitrary and capricious.")

exclude all Thesys-related costs from being passed along to Industry Members, including the costs associated with transitioning the Plan Processor role from Thesys to FINRA CAT.

4. The Participants' Costs Related to the CAT Design and Build / Amazon Web Services

SIFMA has significant concerns that poor choices made by the Participants and Thesys during the period in which Thesys served as the Plan Processor have led to design flaws in the CAT that have resulted in it incurring significant and unnecessary CAT costs that continue to persist to this day. We also have concerns that Commission staff direction in the design and build of the CAT system have also led the CAT to incur significant and unnecessary costs. Relatedly, the Commission's imposition of the FAMs may have caused the Participants to prioritize speed over efficiency and cost control in the design and build of the CAT. These design flaws appear to be especially evident in the Amazon Web Services ("AWS") costs incurred by the CAT, which make up the vast majority of the costs incurred by the CAT.

The bulk of the historical costs for the CAT (as well as anticipated future costs) are for AWS compute and storage costs. Unfortunately, the CAT Fee Filings do not provide any information for the Commission or Industry Members to evaluate whether the AWS fees incurred are reasonable. Notwithstanding the Participants' assertions that AWS has provided competitive prices for the services rendered, the most important aspect of evaluating the reasonableness of the costs of those services is evaluating whether the AWS services required were themselves reasonable. In other words, was CAT designed in such a way to most efficiently utilize cloud computing and cloud storage, or did original design decisions carried forward from the failed Thesys implementation lock FINRA CAT into inefficient and very costly methods of using cloud services. Moreover, to what extent did expanding Commission requirements, strict timing deadlines, and interpretations of the Plan lead the Participants to undertake or maintain costly or inefficient cloud services that would otherwise have not been required or could have been significantly mitigated by more reasoned oversight of the Plan. Given that costs are four to five times greater than what the Commission had estimated in approving the CAT NMS Plan in 2016, it is illogical to think that fees can be evaluated for reasonableness under the Exchange Act without a thorough analysis of why costs, message traffic, storage and compute requirements, and other items that factored into the estimate are so much greater than originally expected. It is not plausible that increased volume is the only reason why CAT costs are many magnitudes greater than estimated, as the Participants seem to suggest.

Given the enormous size of the AWS costs incurred by the Participants so far and expected to be incurred in the future, we strongly urge the Commission to facilitate the establishment of a separate working group that includes Industry Members to focus on ways the CAT system can be made more efficient from a cost perspective while still achieving its goal. We would expect that one of the primary focuses of such a group would be on the services provided by AWS and ways to reduce their costs, as well as potential ways in which the CAT can reduce its reliance on AWS. Industry Members have significant expertise in the use of cloud services to handle their data and have offered their expertise to the Participants many times over the years, however, the Participants have repeatedly ignored these offers. Accordingly, we urge

the Commission to help facilitate such a working group. We note that this is not an empty request from SIFMA, as SIFMA members have started work on a detailed list of potential changes to the CAT system that we believe will improve its efficiency and reduce its costs without degrading its regulatory purpose. This list could help serve as a starting point for such a group.

As part of the efforts focused on AWS costs, we also recommend that the AWS CAT contract be shared in a secure manner with members of this group or otherwise securely shared with a select group of SIFMA members. Despite Industry Member requests, the Participants will not share with Industry Members a copy of their AWS CAT contract. And even though the Commission is a direct beneficiary of the CAT system as a regulatory user of it, the Commission will not mandate the disclosure of that contract. Such disclosure is critical to Industry Members' understanding of the AWS bills and can easily be done in a secure manner to address any CAT security concerns. Further, such disclosure is critical to trying to find ways to increase the efficiency of the CAT. We also note that the Participants and the Commission have never indicated whether any consideration has been given to shopping around for a different cloud service provider than AWS, which seems like an appropriate course of action from a cost management perspective.

5. Public Relations Costs Incurred by the Participants

While not material from an overall CAT cost perspective, it is absurd that the Participants are seeking through the CAT Fee Filings to pass along the public relations costs incurred by them during the time period covered by the CAT Fee Filings. The public relations firms hired by the Participants were hired to represent them, not Industry Members. In this regard, the way the Participants may position CAT before Congress and the public should not be the responsibility of Industry Members, who likely have different views and whose views would not be represented in such an arrangement. Accordingly, none of the amounts paid to the public relations firms should be passed along to Industry Members, which based on the CAT Fee Filings appears to be $366,709 and the CAT Fee Filings should be amended to reflect this.[23]

6. The Participants' Justifications of the Proposed CAT Fees

With regard to the Participants' obligation to justify the proposed CAT fees in the CAT Fee Filings, the Commission stated in approving the CAT Funding Model that it was not making findings regarding the reasonableness of the CAT fees to be charged by the Participants.[24] Rather, it said that such determinations would be made in connection with the fee filings submitted by the Participant under Section 19(b) of the Exchange Act. However, the Participants in the CAT Fee Filings are using Commission findings from its approval of the CAT Funding Model to inappropriately justify the fees they seek to charge Industry Members. For example, in the Statutory Basis section of the CAT Fee Filings, the Participants point back to the Commission's findings in the CAT Funding Model approval order that it is appropriate for the

[23] Based on the CAT Fee Filings, these public relations costs consist of $224,669 for the Pre-FAM Period, $7,700 for the FAM Period 1, $41,940 for the FAM Period 2, and $92,400 for FAM Period 3.

[24] See, e.g., CAT Funding Model at 62637.

Participants to be able to recover certain costs, such as legal costs, and then effectively assert that any legal costs they seek to recover through the CAT Fee Filings must be reasonable because the Commission gave them the green light to recover such costs in the CAT Funding Model approval order.

The Participants seem to be under the misapprehension that the Commission's approval of the CAT Funding Model relieves them of their obligation under the Exchange Act to demonstrate that the proposed CAT fees are consistent with the Exchange Act Fee standards. As set forth in Section 200.700(b)(3)(i) of the Commission's Rules of Practice, the burden to "demonstrate that a proposed rule change is consistent with the Exchange Act and the rules and regulations issued thereunder that are applicable to the self-regulatory organization is on the self-regulatory organization that proposed the rule change." The superficial analysis by the Participants in the CAT Fee Filings regarding the reasonableness of the CAT fees and their satisfaction of the other Exchange Act fee standards does not provide the Commission with sufficient data to allow it to articulate a satisfactory explanation for an approval of the proposed CAT fees, 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). The Commission should therefore reject the Participants' justifications in the CAT Fee Filings to support the proposed fees, as each cost sought to be recovered by the Participants must be independently justified and supported under the Exchange Act.

SIFMA also notes that although we appreciate the Commission's issuance of OIPs regarding the CAT Fee Filings, we fail to understand why the Commission did not include a more pointed discussion regarding the justifications the Participants put forward in the filings for why the proposed CAT fees meet the Exchange Act fee standards. This stands in contrast to the Commission's discussion in its recent order instituting proceedings related to a fee filing by the Municipal Securities Rulemaking Board ("MSRB").[25] In issuing that OIP related to the MSRB filing, the Commission stated that:

> Under the Commission's Rules of Practice, the "burden to demonstrate that a proposed rule change is consistent with the [Act] and the rules and regulations issued thereunder ...is on the [SRO] that proposed the rule change." The description of a proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding, and any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Act and the applicable rules and regulations. Moreover, "unquestioning reliance" on an SRO's representations in a proposed rule change would not be sufficient to justify Commission approval of a proposed rule change. [footnotes omitted]

The CAT Fee Filings similarly raise complicated issues under the Exchange Act fee standards. Thus, it seems surprising that the Commission would not include similar language in the CAT Fee Filings OIPs. The lack of inclusion of such language in the CAT Fee Filings OIPs suggests

[25] See Release No. 34-99444 (January 29, 2024), 89 FR 7424 (February 2, 2024).

that the Commission is acting arbitrarily by employing different standards of review for various SRO fee filings.

In analyzing the proposed CAT fees under the Exchange Act fee standards, the Participants also do not discuss at all the amount of money Industry Members have spent on their own systems and processes to be able to report to the CAT. In approving the CAT Funding Model, the Commission found that it was reasonable for the Participants to exclude such Industry Member compliance costs in connection with establishing the allocation of CAT costs between the Participants and Industry Members.[26] As SIFMA noted in comments on the CAT Funding Model, some of the larger Industry Members have spent millions of dollars and devoted countless staff hours to developing internal systems capable of reporting order, transaction and customer data to the CAT and workable reporting specifications for the CAT.[27] However, the CAT Funding Model approval order does not address whether the Participants can ignore such Industry Member compliance costs in connection with meeting their obligation under the Exchange Act to demonstrate that the proposed CAT fees are reasonable. Indeed, the Susquehanna precedent suggests otherwise.

7. The CAT Fee Filings further Demonstrate the Flaws with the CAT Funding Model

The Participants' attempt to pass along CAT costs such as the costs they incurred in trying to shift CAT breach liability to Industry Members, and their costs for public relations firms, further demonstrate the flaws with the CAT Funding Model. It is now very clear that the SROs will try to pass along virtually any CAT cost incurred by them, regardless of how absurd it is to do so. Moreover, when given the chance by the Commission in the future, it is very likely that the Participants will attempt to shift their share of CAT costs onto Industry Members through rule filings submitted under Section 19(b) of the Exchange, as FINRA is already seeking to do,[28] resulting in 100% of CAT costs being borne in the first instance by Industry Members. Of note, the Participants on May 22, 2023 submitted an exemptive relief request ("Exemptive Request") to "extend until August 31, 2024 the target deadline in Section 11.6(a)(i)(D) of December 30, 2022 for Full Implementation of CAT NMS Plan Requirements."[29] If the Commission were to grant the Exemptive Request, we expect that the Participants will seek to recoup 100% of CAT-related costs incurred by them since December 30, 2022 despite failing to deliver a fully functional CAT by this date as required by CAT NMS Plan.

It is critical from a cost management and accountability perspective for the Participants who govern and control the CAT to have responsibility for paying costs incurred by it. Otherwise, they have no incentive to manage those costs. Yet, through the CAT Funding Model, the Commission is allowing the Participants to ultimately shift 100% of the responsibility for paying for the CAT to Industry Members. Not only does this eliminate the Participants'

[26] See CAT Funding Model at 62637.

[27] See, e.g., (https://www.sec.gov/comments/4-698/4698-20154753-322976.pdf).

[28] See Release No. 34-99372 (January 17, 2024), 89 FR 11153 (February 13, 2024).

[29] See (https://www.catnmsplan.com/sites/default/files/2023-06/05.22.23-Exemption-Request-Regarding-FAM-4.pdf).

incentive to appropriately manage CAT costs, but it also eliminates their incentive to push back on Commission staff when they request changes to the CAT system that deviate from the CAT NMS Plan requirements and/or are not supportable from a cost management perspective. It is also inconsistent with the shared costs requirement under the CAT NMS Plan and the Exchange Act requirement that fees be equitably allocated.

Relatedly, the CAT Funding Model and the CAT Fee Filings expose significant flaws in the CAT governance process because the entities will pay for the majority of the CAT under the approved model – the Industry Members - have no role in managing the CAT's expenses or choosing its vendors. The notion put forth by the Participants that the industry cannot be trusted with a governance role over the CAT as an industry regulatory system is unsupportable, as the whole system of self-regulation set up under the Exchange Act is based on the idea of the industry policing itself through the SROs. While SROs today have a majority of public directors on their boards, Industry Members still are members of those boards that oversee the SROs. They certainly could serve in a similar capacity with regard to the CAT. Moreover, the level of SEC's involvement and oversight of the CAT further reduces the potential of Industry Members to use their governance role to undermine the effectiveness of CAT.

III. The Participants Have Not Demonstrated that They Have Met FAMs 1 through 3

Under the terms of the CAT Funding Model and the CAT NMS Plan, the Participants are required to demonstrate that they have met FAMs 1 through 3 to recover costs incurred by them during the June 22, 2020 through December 31, 2021 period covered by these FAMs. The Participants have not made such a showing, and accordingly, are not entitled to recover 100% of the costs incurred by them during the period covered by these FAMs.

As noted, due to significant delays by the Participants in developing the CAT, the Commission amended the CAT NMS Plan through the May 2020 Amendments to include financial accountability milestones to increase the Participants' financial incentives to timely complete the CAT.[30] In proposing the milestones, the Commission observed that "the Participants had neither met the deadlines set forth in the CAT NMS Plan nor their own proposed extensions of those deadlines."[31] The Commission noted in adopting the milestones that "proposed amendments also will help to ensure that the Participants fulfill their obligations to deliver a functional CAT on a reasonably achievable timeframe."[32]

It is hard to see how the Commission could find that the Participants have met FAMs 1 through 3 when the Participant exchanges are reporting required data to the CAT differently. As discussed above, SIFMA members have discovered through their process of preparing for CAT billing that certain options exchanges are reporting to CAT the "give up" clearing firm as the Executing Broker in certain situations. However, other exchanges are reporting to CAT as the Executing Broker the firms that sent the order to the exchange for execution. Given the differences in CAT reporting among the exchanges, it is unclear how these transactions are being

[30] See supra note 5.

[31] Id.

[32] Id.

linked in CAT, and if they are able to be linked, whether the data would be meaningful from an audit trail perspective. At a minimum, the inability to link such transactions in CAT (or the regulatory value of such linkages if they are possible) would not seem to satisfy FAM 2, which requires sufficient linkage within CAT "to permit the Participants and the Commission to analyze the full lifecycle of an order across the national market system."

Similarly, it is hard to see how the Commission could find that the Participants have met FAMs 1 through 3 when the Participants are not capturing in the CAT standardized, electronic responses to request for quotes ("RFQs") that are not immediately actionable ("NIA Electronic RFQ Responses"). As evidenced by the Participants' May 23, 2023 exemptive request (and supplemented by their February 13, 2024 request),[33] the Commission is taking the position that NIA Electronic RFQ Responses need to be captured in CAT. This Commission position has placed the Participants in the position of having to seek exemptive relief for CAT reporting related to such events. Applying this Commission position to FAMs 1 through 3, means that the Participants have not met these FAMs because they are not capturing in CAT all of the events that the Commission believes are required to be captured. However, if the Commission were to grant such exemptive relief, the Participants would need to show, and Commission would need to explain, how the Participants met FAMs 1 through 3 in the context of the CAT Fee Filings even though the CAT is not capturing NIA Electronic RFQ Responses. Regardless of how it ultimately decides to address the exemptive request, the Commission needs to address whether or not the Participants have met FAMs 1 through 3 with regard to capturing NIA Electronic RFQ Responses. And based on their submission of the exemptive request, it appears that Participants have not met these FAMs because they are not capturing such events.

It is now more than two years past the December 31, 2021 FAM 3 end date, and well beyond the times in FAMs 1 through 3 by which the Participant needed to complete the milestones set forth in these FAMs to be able to recover costs incurred by them during the periods covered by these FAMs. Accordingly, the Participants should not be able to recover 100% of the CAT costs incurred by them during the period covered by FAMs 1 through 3.

Relatedly, with regard to FAM 4, we note that the Participants have submitted an Exemptive Request to extend until August 31, 2024, the FAM 4 deadline. As noted above, the Participants still have not completed the CAIS system, which they were supposed to have done by December 31, 2022 in accordance with FAM 4. As discussed in our letter responding to this Exemptive Request by the Participants, we believe the request is contrary to the public interest and the protection of investors, as the Commission is required to find under Section 36 of Exchange Act and/or Rule 608(e) of Regulation NMS, and therefore should be denied or rejected by the Commission.[34] Moreover, the granting of the Exemptive Request by the Commission only serves to punish Industry Members to the benefit of the Participants, who so far appear to have no accountability for delivering CAT in a timely manner. While we acknowledge that Participants have paid for CAT costs so far, certain of these costs eventually will be passed through to Industry Members.

---

[33] See, e.g., (https://www.catnmsplan.com/sites/default/files/2023-05/05.23.23-Exemption-Request-Regarding-Responses-to-Electronic-RFQs.pdf).

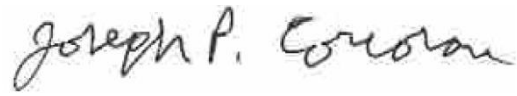
[34] See supra note 19.

* * *

SIFMA appreciates the opportunity to submit this letter to the Commission regarding the Participants' CAT Fee Filings. For the reason set for above, we urge the Commission to disapprove the filings, as the Participants have not met their burden of demonstrating that the proposed fees are consistent with the Exchange Act fee requirements. If you have any questions or need any additional information, please contact Ellen Greene at (212) 313-1287 or Joe Corcoran at (202) 962-7383.

Sincerely,

Ellen Greene
Managing Director
Equities & Options Market Structure



Joseph Corcoran
Managing Director, Associate General Counsel
SIFMA

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