

Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-PEARL-2017-32 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-PEARL-2017-32. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-PEARL-2017-32, and should be submitted on or before August 17, 2017.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>20</sup>

**Eduardo A. Aleman,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-81189; File No. 4-698]

**Joint Industry Plan; Order of Summary Abrogation of Amendment No. 2 to the National Market System Plan Governing the Consolidated Audit Trail by Bats BYX Exchange, Inc., Bats BZX Exchange, Inc., Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., BOX Options Exchange LLC, C2 Options Exchange, Incorporated, Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., Financial Industry Regulatory Authority, Inc., Investors' Exchange LLC, Miami International Securities Exchange, LLC, MIAX PEARL, LLC, NASDAQ BX, Inc., Nasdaq GEMX, LLC, Nasdaq ISE, LLC, Nasdaq MRX, LLC, NASDAQ PHLX LLC, The NASDAQ Stock Market LLC, New York Stock Exchange LLC, NYSE Arca, Inc., NYSE MKT LLC and NYSE National, Inc.**

July 21, 2017.

### I. Introduction

Notice is hereby given that the Securities and Exchange Commission ("Commission"), pursuant to Section 11A of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 608 thereunder,<sup>2</sup> is summarily abrogating Amendment No. 2 to the National Market System Plan Governing the Consolidated Audit Trail ("CAT NMS Plan" or "Plan").

On May 23, 2017,<sup>3</sup> participants of the CAT NMS Plan ("Participants")<sup>4</sup> filed with the Commission a proposal to

<sup>1</sup> 15 U.S.C. 78k-1.

<sup>2</sup> 17 CFR 242.608.

<sup>3</sup> The Participants initially submitted the amendment on May 9, 2017, but subsequently withdrew the amendment and refiled the current submission on May 23, 2017.

<sup>4</sup> The Participants are: Bats BYX Exchange, Inc., Bats BZX Exchange, Inc., Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., BOX Options Exchange LLC, C2 Options Exchange, Incorporated, Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., Financial Industry Regulatory Authority, Inc., Investors' Exchange LLC, Miami International Securities Exchange, LLC, MIAX PEARL, LLC, NASDAQ BX, Inc., Nasdaq GEMX, LLC, Nasdaq ISE, LLC, Nasdaq MRX, LLC, NASDAQ PHLX LLC, The NASDAQ Stock Market LLC, New York Stock Exchange LLC, NYSE Arca, Inc., NYSE MKT LLC and NYSE National, Inc.

amend the Plan ("Amendment No. 2"),<sup>5</sup> pursuant to Section 11A of the Act,<sup>6</sup> and Rule 608 thereunder.<sup>7</sup> The Amendment, which was effective upon filing pursuant to Rule 608(b)(3)(i) of Regulation NMS,<sup>8</sup> sets forth the Consolidated Audit Trail ("CAT") fees to be paid by the Participants.

### II. Description of the Amendment

Prior to filing Amendment No. 2, the Participants filed the CAT NMS Plan with the Commission,<sup>9</sup> pursuant to Section 11A of the Act<sup>10</sup> and Rule 608 of Regulation NMS thereunder,<sup>11</sup> to create, implement and maintain the CAT. The Plan was published for comment in the *Federal Register* on May 17, 2016,<sup>12</sup> and approved by the Commission, as modified, on November 15, 2016.<sup>13</sup> Under the CAT NMS Plan, the Operating Committee of a newly formed company—CAT NMS, LLC (the "Company"), of which each Participant is a member—has the discretion to establish funding for the Company to operate the CAT, including establishing fees that the Participants and Industry Members will pay ("CAT Fees").<sup>14</sup>

The Plan specified that, in establishing the funding of the Company, the Operating Committee shall establish "a tiered fee structure in which the fees charged to: (i) CAT Reporters that are Execution Venues, including ATSs, are based upon the level of market share; (ii) Industry Members' non-ATS activities are based upon message traffic; and (iii) the CAT Reporters with the most CAT-related activity (measured by market share and/or message traffic, as applicable) are generally comparable (where, for these comparability purposes, the tiered fee structure takes into consideration

<sup>5</sup> See Letter from Michael Simon, Chair, CAT NMS Plan Operating Committee, to Brent J. Fields, Secretary, Commission, dated May 22, 2017 ("Letter"). See also Securities Exchange Act Release No. 80930 (June 14, 2017), 82 FR 28180 (June 20, 2017) ("Notice"), available at <https://www.sec.gov/rules/sro/nms/2017/34-80930.pdf>.

<sup>6</sup> 15 U.S.C. 78k-1.

<sup>7</sup> 17 CFR 242.608.

<sup>8</sup> 17 CFR 242.608(b)(3)(i).

<sup>9</sup> See Letter from the Participants to Brent J. Fields, Secretary, Commission, dated September 30, 2014; and Letter from Participants to Brent J. Fields, Secretary, Commission, dated February 27, 2015. On December 23, 2015, the Participants submitted an amendment to the CAT NMS Plan. See Letter from Participants to Brent J. Fields, Secretary, Commission, dated December 23, 2015.

<sup>10</sup> 15 U.S.C. 78k-1.

<sup>11</sup> 17 CFR 242.608.

<sup>12</sup> Securities Exchange Act Release No. 77724 (April 27, 2016), 81 FR 30614 (May 17, 2016) ("CAT NMS Plan Notice").

<sup>13</sup> Securities Exchange Act Release No. 79318 (November 15, 2016), 81 FR 84696 (November 23, 2016) ("Approval Order").

<sup>14</sup> Section 11.1(b) of the CAT NMS Plan.

<sup>20</sup> 17 CFR 200.30-3(a)(12).

affiliations between or among CAT Reporters, whether Execution Venues and/or Industry Members).<sup>15</sup> Under the Plan, such fees are to be implemented in accordance with various funding principles, including an “allocation of the Company’s related costs among Participants and Industry Members that is consistent with the [ ] Act taking into account . . . distinctions in the securities trading operations of Participants and Industry Members and their relative impact upon the Company resources and operations” and the “avoid[ance of] any disincentives such as placing an inappropriate burden on competition and reduction in market quality.”<sup>16</sup>

The Participants submitted this Amendment No. 2 to the Plan to establish the CAT Fees to be charged to themselves, as Execution Venues.<sup>17</sup> In addition, the Participants submitted proposed rule changes to adopt fees to be charged to Industry Members, including Industry Members that are Execution Venue ATSS (“Industry Member Fee Filings”), which are described below.<sup>18</sup> The text of the Industry Member Fee Filings is substantially similar to Amendment No. 2. On June 30, 2017, the Commission temporarily suspended the Industry Member Fee Filings and instituted proceedings to determine whether those filings should be approved or disapproved.<sup>19</sup>

The Plan specifies that, in establishing the funding of the Company, the Operating Committee shall establish “a tiered fee structure in which the fees charged to: (i) CAT Reporters that are Execution Venues, including ATSS, are based upon the level of market share; (ii) Industry Members’ non-ATS activities are based upon message traffic; and (iii) the CAT Reporters with the most CAT-related activity (measured by market share and/or message traffic, as applicable) are generally comparable (where, for these comparability purposes, the tiered fee structure takes into consideration affiliations between or among CAT Reporters, whether Execution Venues and/or Industry Members.”<sup>20</sup> Under the Plan, such fees are to be implemented in accordance with various funding principles, including an “allocation of the Company’s related costs among Participants and Industry Members that is consistent with the [ ] Act” and the “avoid[ance of] any disincentives such as placing an inappropriate burden on competition and reduction in market quality.”<sup>21</sup>

To establish the CAT Fees permitted by the Plan, the Participants submitted Amendment No. 2. As noted above, Amendment No. 2 adopted fees applicable to the Participants, as Execution Venues, which are described below.<sup>22</sup>

*A. Execution Venue Tiers*<sup>23</sup>

1. NMS Stocks and OTC Equity Securities

Amendment No. 2 establishes fixed fees to be paid by Execution Venues<sup>24</sup> depending on the market share of that Execution Venue in NMS Stocks and OTC Equity Securities. Market share for Execution Venues will be calculated by share volume, except the market share for a national securities association that has trades reported by its members to its trade reporting facility or facilities for reporting transactions effected otherwise than on an exchange in NMS Stocks or OTC Equity Securities will be calculated based on share volume of trades reported, excluding the share volume reported to such national securities association by an Execution Venue.<sup>25</sup>

Under Amendment No. 2, each Equity Execution Venue will be ranked by market share and assigned to one of two tiers that have been predefined by percentages (the “Equity Execution Venue Percentages”).<sup>26</sup> The Participants noted that the percentage of costs recovered by each Equity Execution Venue tier will be determined by predefined percentage allocations (the “Equity Execution Venue Recovery Allocation”).<sup>27</sup>

The following table sets forth the specific Equity Execution Venue Percentages and Equity Execution Recovery Allocations:<sup>28</sup>

Equity execution venue tier	Percentage of equity execution venues	Percentage of execution venue recovery	Percentage of total recovery
Tier 1 .....	25.00	26.00	6.50
Tier 2 .....	75.00	49.00	12.25

<sup>15</sup> Section 11.2(c) of the CAT NMS Plan. See Article XI of the CAT NMS Plan for additional detail; see also, e.g., Notice, *supra* note 5, at 28181–28183 for additional description of the CAT NMS Plan requirements.

<sup>16</sup> See Section 11.2(b) and (e) of the CAT NMS Plan.

<sup>17</sup> See Letter, *supra* note 5. See also Notice, *supra* note 5. Section 1.1 of the CAT NMS Plan defines “Execution Venue” as “a Participant or an [ATS] (as defined in Rule 300 of Regulation ATS) that operates pursuant to Rule 301 of Regulation ATS (excluding any such ATS that does not execute orders).”

<sup>18</sup> For additional details regarding these fees, see, e.g., Securities Exchange Act Release Nos. 80675 (May 15, 2017), 82 FR 23100 (May 19, 2017) (SR–MIAX–2017–18); 80676 (May 15, 2017), 82 FR 23083 (May 19, 2017) (SR–PEARL–2017–20); 80697 (May 16, 2017), 82 FR 23398 (May 22, 2017) (SR–BX–2017–023); 80691 (May 16, 2017), 82 FR 23344 (May 22, 2017) (SR–CHX–2017–08); 80692 (May 16, 2017), 82 FR 23325 (May 22, 2017) (SR–IEX–2017–16); 80696 (May 16, 2017), 82 FR 23439 (May 22, 2017) (SR–NASDAQ–2017–046); 80693 (May 16,

2017), 82 FR 23363 (May 22, 2017) (SR–NYSE–2017–22); 80698 (May 16, 2017), 82 FR 23457 (May 22, 2017) (SR–NYSEArca–2017–52); 80694 (May 16, 2017), 82 FR 23416 (May 22, 2017) (SR–NYSEMKT–2017–26); 80710 (May 17, 2017), 82 FR 23639 (May 23, 2017) (SR–FINRA–2017–011); 80721 (May 18, 2017), 82 FR 23864 (May 24, 2017) (SR–BOX–2017–16); 80713 (May 18, 2017), 82 FR 23956 (May 24, 2017) (SR–GEMX–2017–17); 80715 (May 18, 2017), 82 FR 23895 (May 24, 2017) (SR–ISE–2017–45); 80726 (May 18, 2017), 82 FR 23915 (May 24, 2017) (SR–MRX–2017–04); 80725 (May 18, 2017), 82 FR 23935 (May 24, 2017) (SR–PHLX–2017–37); 80786 (May 26, 2017), 82 FR 25474 (June 1, 2017) (SR–C2–2017–017); 80785 (May 26, 2017), 82 FR 25404 (June 1, 2017) (SR–CBOE–2017–040); 80784 (May 26, 2017), 82 FR 25448 (June 1, 2017) (SR–BatsEDGA–2017–13); 80809 (May 30, 2017), 82 FR 25837 (June 5, 2017) (SR–BatsBYX–2017–11); 80822 (May 31, 2017), 82 FR 26148 (June 6, 2017) (SR–BatsBZX–2017–38); and 80821 (May 31, 2017), 82 FR 26177 (June 6, 2017) (SR–BatsEDGX–2017–22).

<sup>19</sup> See Securities Exchange Act Release No. 81067 (June 30, 2017), 82 FR 31656 (July 7, 2017).

<sup>20</sup> Section 11.2(c) of the CAT NMS Plan. See Article XI of the CAT NMS Plan for additional detail; see also, e.g., Notice, *supra* note 5, at 28181–28183 for additional description of the CAT NMS Plan requirements.

<sup>21</sup> See Section 11.2(c) and (e) of the CAT NMS Plan.

<sup>22</sup> For additional details regarding these fees, see, e.g., Notice, *supra* note 5.

<sup>23</sup> Amendment No. 2 establishes different tiers for Equity and Options Execution Venues.

<sup>24</sup> See *supra* note 17. For purposes of determining the CAT Fees for ATSS, the Participants categorized ATSS (excluding ATSS that do not execute orders) as Execution Venues. The Commission notes that the CAT Fees for Execution Venue ATSS were proposed in the Industry Member Fee Filings and that Amendment No. 2 addresses fees applicable to the Participants, as Execution Venues.

<sup>25</sup> Section 11.3(a)(i) of the CAT NMS Plan; see also, e.g., Notice, *supra* note 5, at 28186.

<sup>26</sup> See, e.g., Notice, *supra* note 5, at 28186.

<sup>27</sup> See, e.g., *id.*

<sup>28</sup> See, e.g., *id.*

Equity execution venue tier	Percentage of equity execution venues	Percentage of execution venue recovery	Percentage of total recovery
Total .....	100	75	18.75

2. Listed Options

Amendment No. 2 establishes fixed fees to be paid by Execution Venues depending on the Listed Options market share of that Execution Venue. Market share for Execution Venues will be calculated by contract volume.<sup>29</sup> Under

Amendment No. 2, each Options Execution Venue will be ranked by market share and assigned to one of two tiers that have been predefined by percentages (the “Options Execution Venue Percentages”).<sup>30</sup> The Participants noted that the percentage of costs recovered by each Options Execution

Venue tier will be determined by predefined percentage allocations (the “Options Execution Venue Recovery Allocation”).<sup>31</sup> The following table sets forth the specific Options Execution Venue Percentages and Options Execution Venue Recovery Allocations:<sup>32</sup>

Options execution venue tier	Percentage of options execution venues	Percentage of execution venue recovery	Percentage of total recovery
Tier 1 .....	75.00	20.00	5.00
Tier 2 .....	25.00	5.00	1.25
Total .....	100	25	6.25

3. Tier Assignments

The Participants stated that market share for Execution Venues will be sourced from data reported to the CAT System after the commencement of CAT reporting.<sup>33</sup> Prior to the commencement of CAT reporting, the Participants stated that market share for Execution Venues will be sourced from publicly-available market data, including data made publicly available by Bats and FINRA.<sup>34</sup>

B. Industry Member Tiers

Amendment No. 2 describes the fixed fees to be established by the Industry Member Fee Filings to be payable by Industry Members, based on message traffic.<sup>35</sup> Each Industry Member (other than Execution Venue ATs<sup>36</sup>) will be ranked by message traffic and assigned to one of nine tiers that have been predefined by percentages (the “Industry Member Percentages”).<sup>37</sup> The

Participants noted that the percentage of costs recovered by each Industry Member tier will be determined by predefined percentage allocations (the “Industry Member Recovery Allocation”).<sup>38</sup> The following table sets forth the specific Industry Member Percentages and Industry Member Recovery Allocations:<sup>39</sup>

Industry member tier	Percentage of industry members	Percentage of industry member recovery	Percentage of total recovery
Tier 1 .....	0.500	8.50	6.38
Tier 2 .....	2.500	35.00	26.25
Tier 3 .....	2.125	21.25	15.94
Tier 4 .....	4.625	15.75	11.81
Tier 5 .....	3.625	7.75	5.81
Tier 6 .....	4.000	5.25	3.94
Tier 7 .....	17.500	4.50	3.38
Tier 8 .....	20.125	1.50	1.13
Tier 9 .....	45.000	0.50	0.38
Total .....	100	100	75

The Participants explained that, prior to the start of CAT reporting, “message traffic” will be comprised of historical

equity and equity options orders, cancels and quotes provided by each exchange and FINRA over the previous three months.<sup>40</sup> The Participants stated

<sup>29</sup> Section 11.3(a)(ii) of the CAT NMS Plan; see also, e.g., Notice, *supra* note 5, at 28187.

<sup>30</sup> See, e.g., Notice, *supra* note 5, at 28187.

<sup>31</sup> See, e.g., *id.*

<sup>32</sup> See, e.g., *id.*

<sup>33</sup> See, e.g., *id.* at 28188.

<sup>34</sup> See, e.g., *id.*

<sup>35</sup> The CAT NMS Plan provides that the CAT Fees payable by Industry Members shall include message traffic generated by: (i) An ATS that does not execute orders that is sponsored by an Industry

Member and (ii) routing orders to and from any ATS sponsored by an Industry Member. See Section 11.3(b) of the CAT NMS Plan. The Participants noted, however, that Industry Member fees will not be applicable to an ATS that qualifies as an Execution Venue. See, e.g., Notice, *supra* note 5, at 28183.

<sup>36</sup> The Participants defined “Execution Venue ATs” as alternative trading systems that execute transactions in Eligible Securities. See, e.g., Notice, *supra* note 5, at 28181.

<sup>37</sup> See, e.g., *id.* at 2810328183.

<sup>38</sup> See, e.g., *id.*

<sup>39</sup> See, e.g., *id.* at 28184–5.

<sup>40</sup> See, e.g., *id.* at 28185. The Commission approved exemptive relief allowing options market-maker quotes to be reported to the Central Repository by the relevant Options Exchange in lieu of requiring that such reporting be done by both the Options Exchange and the options market-maker. See Securities Exchange Act Release No. 77265 (March 1, 2017), 81 FR 11856 (March 7, 2016). The Participants stated that this exemption applies to

that prior to the start of CAT reporting, (1) orders will be comprised of the total number of equity and equity options orders received and originated by a member of an exchange or FINRA over the previous three-month period, as well as order routes and executions originated by a member of FINRA, (2) cancels will be comprised of the total number of equity and equity option cancels received and originated by a member of an exchange or FINRA over a three-month period, and (3) quotes will be comprised of information readily available to the exchanges and FINRA, such as the total number of historical equity and equity options quotes received and originated by a member of an exchange or FINRA over the prior three-month period.<sup>41</sup> After an Industry Member begins reporting to the CAT, the Participants noted that “message

traffic” will be calculated based on the Industry Member’s Reportable Events.<sup>42</sup>

*C. Allocation of Costs*

In determining the cost allocation between Industry Members (other than Execution Venue ATSSs) and Execution Venues, the Participants stated that the Operating Committee decided that 75% of total costs recovered will be allocated to Industry Members (other than Execution Venue ATSSs) and 25% will be allocated to Execution Venues.<sup>43</sup> In determining the cost allocation between Equity Execution Venues and Options Execution Venues, the Participants stated that the Operating Committee further determined to allocate 75% of Execution Venue costs recovered to Equity Execution Venues and 25% to Options Execution Venues.<sup>44</sup>

*D. Fee Levels*

The Participants explained that the sum of the CAT Fees is designed to recover the total costs of building and operating the CAT. They stated that the Operating Committee has estimated overall CAT costs—including development and operational costs, third-party support costs (including historic legal fees, consulting fees, and audit fees), insurance costs, and operational reserve costs—to be \$50,700,000 in total for the year beginning November 21, 2016.<sup>45</sup> The Participants stated that, based on the estimated costs and the calculations for the funding model, the Operating Committee determined to impose the following fees.

For Equity Execution Venues:<sup>46</sup>

Tier	Monthly CAT fee	Quarterly CAT fee	CAT fees paid annually
1 .....	\$21,125	\$63,375	\$253,500
2 .....	12,940	38,820	155,280

For Options Execution Venues:<sup>47</sup>

Tier	Monthly CAT fee	Quarterly CAT fee	CAT Fees paid annually
1 .....	\$19,205	\$57,615	\$230,460
2 .....	13,204	39,612	158,448

For Industry Members (other than Execution Venue ATSSs):<sup>48</sup>

Tier	Monthly CAT fee	Quarterly CAT fee	CAT fees paid annually
1 .....	\$33,668	\$101,004	\$404,016
2 .....	27,051	81,153	324,612
3 .....	19,239	57,717	230,868
4 .....	6,655	19,965	79,860
5 .....	4,163	12,489	49,956
6 .....	2,560	7,680	30,720
7 .....	501	1,503	6,012
8 .....	145	435	1,740
9 .....	22	66	264

*E. Initial and Periodic Tier Reassignments*

The Operating Committee will assign fee tiers every three months based on

options market-maker quotes for CAT reporting purposes only. Therefore, the Participants indicated that options market-maker quotes will be included in the calculation of total message traffic for options market-makers. *See, e.g., Notice, supra* note 5, at 28185 n.29.

<sup>41</sup> *See, e.g., id.* at 28185.

<sup>42</sup> *See, e.g., id.* If an Industry Member (other than an Execution Venue ATS) has no orders, cancels or quotes prior to the commencement of CAT

market share or message traffic, as applicable, from the prior three months.<sup>49</sup> For the initial tier assignments, the Participants stated that

reporting, or no Reportable Events after CAT reporting commences, the Participants stated that the Industry Member would not have a CAT Fee obligation. *See, e.g., id.* at n. 31.

<sup>43</sup> *See, e.g., id.* at 28188.

<sup>44</sup> *See, e.g., id.*

<sup>45</sup> *See, e.g., id.* The Participants further noted that CAT-related costs incurred prior to November 21, 2016 will be addressed via a separate filing. *See, e.g., id.* at n.34.

the Company will calculate the relevant tier for each CAT Reporter using the prior three months of data.<sup>50</sup> The Participants explained the Company

<sup>46</sup> *See, e.g., id.* at 28189.

<sup>47</sup> *See, e.g., id.*

<sup>48</sup> *See, e.g., id.*

<sup>49</sup> *See, e.g., id.* at 28194.

<sup>50</sup> *See, e.g., id.* The Participants indicated that such data will be comprised of historical equity and equity options orders, cancels, and quotes provided by the Participants over the previous three-month period. *See, e.g., id.; see also* notes 40–42 *supra* and accompanying text.

will calculate subsequent tier assignments using the three months of data prior to the relevant tri-monthly date.<sup>51</sup> The Participants noted that any movement of CAT Reporters between tiers will not change the criteria for each tier or the fee amount corresponding to each tier.<sup>52</sup> According to the Participants, a CAT Reporter's assigned tier will depend not only on its own message traffic or market share, but also on the message traffic or market share across all CAT Reporters.<sup>53</sup>

#### F. Changes to Fee Levels and Tiers

The Participants noted that Section 11.3(d) of the CAT NMS Plan states that "[t]he Operating Committee shall review such fee schedule on at least an annual basis and shall make any changes to such fee schedule that it deems appropriate."<sup>54</sup> The Participants stated that, as part of such reviews, the Operating Committee will review the distribution of Industry Members and Execution Venues across tiers and make any updates to the percentage of CAT Reporters allocated to each tier as may be necessary.<sup>55</sup> In addition, the Participants asserted that such reviews would consider the estimated ongoing CAT costs and the level of the operating reserve, in order to adjust CAT Fees as appropriate.<sup>56</sup> The Participants further stated that any changes to the number of tiers in the funding model or the fees assigned to each tier will be filed with the Commission pursuant to Rule 608 of the Act and become effective in accordance with the requirements of Rule 608.<sup>57</sup>

Pursuant to Rule 608(b)(3)(i) under Regulation NMS,<sup>58</sup> the Participants designated Amendment No. 2 as establishing or changing a fee or other charge collected on their behalf in connection with access to, or use of, the facilities contemplated by the Plan. As a result, Amendment No. 2 was effective upon filing with the Commission. On June 14, 2017, the Commission issued notice of Amendment No. 2.<sup>59</sup>

### III. Summary of Comments and Participants' Response

While no comments were received on Amendment No. 2 to the CAT NMS

Plan, the Commission received a number of comment letters on the Industry Member Fee Filings, and a response to such comments from the Participants. Because the text of the Industry Member Fee Filings is substantially similar to this Amendment No. 2, the Commission believes the comment letters are relevant to this Order and has summarized the comments on the Industry Member Fee Filings below.<sup>60</sup>

#### Necessity of the CAT

One commenter asks whether the CAT is a "worthwhile endeavor,"<sup>61</sup> arguing that the CAT is largely duplicative of existing electronic audit trails, and suggesting that the goals of the CAT can be accomplished at a fraction of the cost set forth in the filings.<sup>62</sup> The commenter also believes

<sup>60</sup> Since the Industry Member Fee Filings were designed to adopt fees to be charged to Industry Members to fund CAT, the Commission considered all comments received regardless of the comment file to which they were submitted. See Letter from Theodore R. Lazo, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association, to Brent J. Fields, Secretary, Commission (dated June 6, 2017) ("SIFMA Letter"), available at: <https://www.sec.gov/comments/sr-batsbx-2017-38/batsbx201738-1788188-153228.pdf>; Letter from Patricia L. Cerny and Steven O'Malley, Compliance Consultants, to Brent J. Fields, Secretary, Commission (dated June 12, 2017) ("Cerny & O'Malley Letter"), available at: <https://www.sec.gov/comments/sr-cboe-2017-040/cboe2017040-1799253-153675.pdf>; Letter from Daniel Zinn, General Counsel, OTC Markets Group Inc., to Eduardo A. Aleman, Assistant Secretary, Commission (dated June 13, 2017) ("OTC Markets Letter"), available at: <https://www.sec.gov/comments/sr-finra-2017-011/finra2017011-1801717-153703.pdf>; Letter from Joanna Mallers, Secretary, FIA Principal Traders Group, to Brent J. Fields, Secretary, Commission (dated June 22, 2017) ("FIA Letter"), available at: <https://www.sec.gov/comments/sr-cboe-2017-040/cboe2017040-1819670-154195.pdf>; Letter from Stuart J. Kaswell, Executive Vice President and Managing Director, General Counsel, Managed Funds Association, to Brent J. Fields, Secretary, Commission (dated June 23, 2017) ("MFA Letter"), available at: <https://www.sec.gov/comments/sr-finra-2017-011/finra2017011-1822454-154283.pdf>; and Letter from Suzanne H. Shatto, Investor, to Commission (dated June 27, 2017) ("Shatto Letter"), available at: <https://www.sec.gov/comments/sr-batsedgx-2017-22/batsedgx201722-154443.pdf>. The Commission also received a comment letter which is not pertinent to the Industry Member Fee Filings and Amendment No. 2. See Letter from Christina Crouch, Smart Ltd., to Brent J. Fields, Secretary, Commission (dated June 5, 2017) ("Smart Letter"), available at: <https://www.sec.gov/comments/sr-batsbx-2017-38/batsbx201738-1785545-153152.htm>. The Commission also has received a letter from the Participants responding to the comments received. See Letter from CAT NMS Plan Participants to Brent J. Fields, Secretary, Commission (dated June 29, 2017) ("Response from Participants"), available at <https://www.sec.gov/comments/sr-batsbx-2017-11/batsbx201711-1832632-154584.pdf>.

<sup>61</sup> See FIA Letter, *supra* note 60, at 2.

<sup>62</sup> See *id.* See also Cerny & O'Malley Letter, *supra* note 60, at 4 (suggesting that the CAT will not capture any new violative activity not currently disclosed under current surveillance practices).

that the CAT is not justified in terms of costs and benefits and warns that any costs assessed to broker-dealers will ultimately be passed on to investors.<sup>63</sup> Similarly, another commenter believes that fees imposed on broker-dealers are likely to be passed through to investors, effectively limiting investor choice in execution venues.<sup>64</sup>

In response to the comment questioning the utility of the CAT, the Participants explain that they are obligated to build the CAT by Rule 613.<sup>65</sup> Further, the Participants state that the CAT NMS Plan requires them to eliminate existing systems and rules made duplicative by the CAT and that they have already filed proposals to accomplish this for certain such systems and rules.<sup>66</sup> The Participants add that the CAT is intended to replace the current audit trails (which vary in data and scope, among other ways) with a single, comprehensive audit trail.<sup>67</sup>

#### Funding Authority

One commenter challenges the imposition of a CAT Fee on Industry Members, arguing that the Participants have not provided justification for imposing such a fee and that the Industry Members should not be obligated to pay any costs or expenses other than the direct costs to build and operate the CAT.<sup>68</sup> Two commenters note that broker-dealers already pay the Participants a significant amount in regulatory funding, and argue that costs other than the direct costs to build and operate the CAT (such as insurance and consulting) should be borne by the Participants as the costs they incur to do business as self-regulatory organizations, as well as any costs incurred before the approval of the CAT NMS Plan.<sup>69</sup>

In their response, the Participants state that Rule 613 of Regulation NMS ("Rule 613")<sup>70</sup> contemplates broker-dealers contributing to the funding of CAT.<sup>71</sup> Because the CAT improves

<sup>63</sup> See FIA Letter, *supra* note 60, at 2.

<sup>64</sup> See MFA Letter, *supra* note 60, at 2.

<sup>65</sup> See Response from Participants, *supra* note 60, at 17.

<sup>66</sup> See *id.* at 18. As an example of such a filing, the Participants cite to Securities Exchange Act Release No. 80783 (May 26, 2017), 82 FR 25423 (June 1, 2017) (SR-FINRA-2017-013), wherein FINRA proposes to eliminate the Order Audit Trail System. See Response from Participants, *supra* note 60, at 18 n.103.

<sup>67</sup> See Response from Participants, *supra* note 60, at 18.

<sup>68</sup> See SIFMA Letter, *supra* note 60, at 2-4.

<sup>69</sup> See FIA Letter, *supra* note 60, at 2-3; see also SIFMA Letter, *supra* note 60, at 3-4.

<sup>70</sup> 17 CFR 242.613.

<sup>71</sup> See Response from Participants, *supra* note 60, at 3.

<sup>51</sup> See, e.g., Notice, *supra* note 5, at 28194.

<sup>52</sup> See, e.g., *id.*

<sup>53</sup> See, e.g., *id.*

<sup>54</sup> See, e.g., *id.*

<sup>55</sup> See, e.g., *id.*

<sup>56</sup> See, e.g., *id.* The Participants further noted that any surplus of the Company's revenues over its expenses will be included within the operational reserve to offset future fees. See, e.g., *id.*

<sup>57</sup> See, e.g., *id.*

<sup>58</sup> 17 CFR 242.608(b)(3)(i).

<sup>59</sup> See *supra* note 5.

regulatory oversight of the securities markets, the Participants believe that it would be equitable to require broker-dealers and Participants to fund the CAT.<sup>72</sup> The Participants further believe that Rule 613 and the Approval Order<sup>73</sup> support their recovery of costs related to the creation, implementation and maintenance of the CAT NMS Plan, such as third-party support costs, the operational reserve and insurance costs, through the CAT Fee.<sup>74</sup>

#### Industry Member Input

Three commenters argue that the funding decisions would have benefited from greater involvement from Industry Members.<sup>75</sup> Two commenters assert that the Participants' development of the funding model should have involved collaboration with the broker-dealer community.<sup>76</sup> One commenter opines that if broker-dealers had been involved in the development of the funding model, such participation would have been helpful in understanding why market participants are subject to CAT fees and the rationale for the proposed fee structure.<sup>77</sup> Another commenter believes that the proposed fees lack substantive input from the Industry Members.<sup>78</sup> The third commenter recommends that the CAT NMS Plan Operating Committee include market participant representatives with respect to funding and data security, to enhance transparency and mitigate potential conflicts of interest.<sup>79</sup>

In response to the comment that the funding model should have been the result of greater industry collaboration, the Participants assert that market participants were given the opportunity to comment on the funding model through the CAT NMS Plan Notice<sup>80</sup> and that, in developing the funding model, the Participants considered the input of members of the industry through the "Development Advisory Group" that was formed to provide industry feedback on the development of the CAT NMS Plan.<sup>81</sup> Further, the Participants assert that the proposed

fees provide the opportunity for public comment on the fees.<sup>82</sup>

#### Conflicts of Interest

Three commenters raise concerns about Participant conflicts of interest in setting the CAT fees.<sup>83</sup> One commenter argues that, through the Industry Member Fee Filings, the Participants are imposing unreasonable fees on their competitors, the Industry Members, who, as members of the Participants, have no recourse but to pay the fees or risk regulatory action.<sup>84</sup> This commenter states that 88% of the total costs of building and operating the CAT are allocated to broker-dealers and ATSS under the proposed fees, suggesting the Participants decided to allocate nearly all of the costs of CAT to their competitors.<sup>85</sup> Accordingly, the commenter recommends that an independent third party should have established the proposed CAT Fees to prevent the Participants from setting fees to their benefit.<sup>86</sup>

Another commenter argues that the Participants have a clear conflict of interest when setting their own cost allocation.<sup>87</sup> This commenter states that the not-for-profit structure of the Company is essential to the CAT NMS Plan, seeks assurance that the Company has filed for business league status and, if so, asks whether the application has been approved.<sup>88</sup> The third commenter believes the process to establish the CAT fees does not address the Participants' potential conflicts of interest related to their commercial interests.<sup>89</sup>

In their response, the Participants explain that it is unnecessary to require an independent third party to establish the CAT Fees, in part because the funding of the CAT is designed to protect against any conflicts of interest in the Participants' ability to set fees, through the operation of the CAT on a break-even basis (such that any fees collected would be used toward CAT costs and an appropriate reserve, and that surpluses would offset fees in future payment).<sup>90</sup> The Participants also refer to the application of the Company

to be organized as a tax-exempt business league, which would require that no part of the Company's net earnings can inure to the benefit of the Participants and that the Company is not organized for profit.<sup>91</sup> Additionally, the Participants note that the obligation to create, develop and maintain the CAT is their own responsibility, so they must have the ability to establish reliable funding and not an independent third party.<sup>92</sup>

In response to the comment asking about the status of the Company's application to be organized as a tax-exempt business league, the Participants state that the Company filed its IRS application on May 5, 2017, and that the application is currently pending. The Participants explain that if the IRS does not approve the application, the Company will operate as set forth in the Plan, but may be required to pay taxes. They believe that it is premature to include a tax contingency plan in the proposals.<sup>93</sup>

#### Allocation of Fees

Several commenters raise concerns about the proposed allocation of CAT fees.<sup>94</sup> One commenter argues that the Industry Member Fee Filings are not an equitable allocation of reasonable fees under Section 6(b)(4) or Section 15A(b)(5) of the Act.<sup>95</sup> This commenter notes that the proposed fees allocate approximately 88% of the total costs of building and operating the CAT to broker-dealers and ATSS<sup>96</sup> and questions the "comparability" justification provided by the Participants for allocating 75% of the total CAT costs to Industry Members, stating that the proposed fees are not comparable at the highest tiers.<sup>97</sup> Similarly, another commenter opines that the 75%/25% allocation of the CAT costs is inequitable, explaining that the Participants will be able to realize cost savings from the retirement of regulatory reporting processes.<sup>98</sup> A third commenter notes that it is unable to understand the justification for the 75% allocation to broker-dealers,<sup>99</sup> and the fourth commenter believes that the Participants are disproportionately imposing fees on Industry Members,

<sup>72</sup> See *id.* at 4.

<sup>73</sup> See *supra* note 13.

<sup>74</sup> See Response from Participants, *supra* note 60, at 7–8.

<sup>75</sup> See SIFMA Letter; FIA Letter; MFA Letter, *supra* note 60.

<sup>76</sup> See SIFMA Letter, *supra* note 60, at 2–3; see FIA Letter, *supra* note 60, at 2 (stating "we struggle to understand how excluding other market participants and taking input only from the Plan Participants is anything but prejudicial").

<sup>77</sup> See FIA Letter, *supra* note 60, at 2.

<sup>78</sup> See SIFMA Letter, *supra* note 60, at 2–3.

<sup>79</sup> See MFA Letter, *supra* note 60, at 2.

<sup>80</sup> See *supra* note 12.

<sup>81</sup> See Response from Participants, *supra* note 60, at 2–3.

<sup>82</sup> See *id.* at 2.

<sup>83</sup> See SIFMA Letter, FIA Letter, MFA Letter, *supra* note 60.

<sup>84</sup> See SIFMA Letter, *supra* note 60, at 2–3.

<sup>85</sup> See *id.* at 2–3.

<sup>86</sup> See *id.*

<sup>87</sup> See FIA Letter, *supra* note 60, at 2.

<sup>88</sup> See *id.* at 3. This commenter raises concerns about the impact on the costs and allocations if the Company's application to become a business league is not approved by the Internal Revenue Service ("IRS"). *Id.*

<sup>89</sup> See MFA Letter, *supra* note 60, at 2.

<sup>90</sup> See Response from Participants, *supra* note 60, at 11.

<sup>91</sup> See *id.*

<sup>92</sup> See *id.* at 11–12.

<sup>93</sup> See *id.* at 11, 18.

<sup>94</sup> See SIFMA Letter; Cerny & O'Malley Letter, FIA Letter; MFA Letter, *supra* note 60.

<sup>95</sup> See SIFMA Letter, *supra* note 60, at 3.

<sup>96</sup> See *id.* at 3 n.4.

<sup>97</sup> See *id.* at 3.

<sup>98</sup> See Cerny & O'Malley Letter, *supra* note 60, at 2.

<sup>99</sup> See FIA Letter, *supra* note 60, at 3.

which could put Industry Members at a competitive disadvantage.<sup>100</sup>

In response to comments regarding the allocation of CAT costs, the Participants first state that the 88% figure cited in the first commenter's letter is the cost broker-dealers will incur directly to comply with the reporting requirements of the CAT, not the CAT Fees.<sup>101</sup> The Participants also note that this is an aggregate number and reflects the fact that there are 75 times more Industry Members that would report to the CAT than Participants.<sup>102</sup>

In addition, the Participants explain that the Operating Committee believed that the 75%/25% division of total CAT costs between Industry Members and Execution Venues maintained the greatest level of comparability, considering affiliations among or between CAT Reporters.<sup>103</sup> The Participants state that although the Tier 1 and 2 fees for Industry Members would be higher than those for Execution Venues, the fees paid by Execution Venue complexes would be higher than those paid by Industry Member complexes.<sup>104</sup> The Participants also note that the cost allocation takes into account that there are approximately 25 times more Industry Members that would report to the CAT than Execution Venues.<sup>105</sup>

#### Tiering Methodology

Two commenters believe that the proposed tiering methodology is inequitable and unreasonable.<sup>106</sup> Both commenters raise concerns that the tiers will be applied inequitably because Industry Members will be assessed fees based on their message traffic (the biggest cost component of the CAT), while Participants will be assessed fees on their market share.<sup>107</sup> One of the commenters notes that, although the Participants proposed nine tiers for Industry Members, they have only proposed two tiers for Execution Venues,<sup>108</sup> "claiming that additional

tiers would have resulted in significantly higher fees for Tier 1 [E]xecution [V]enues and diminish comparability between [E]xecution [V]enues and Industry Members."<sup>109</sup> Both commenters believe the result will "maximize costs for broker-dealers and minimize costs for Plan Participants."<sup>110</sup> One of the commenters also questions why it makes sense to charge a fixed fee for all market participants within a single tier, and whether the fixed-fee tiers set forth therein could create incentives for market participants to limit their quoting and trading activities as their trading volumes approach higher tiers.<sup>111</sup>

In response to the comments that the tiering methodology is inequitable and unreasonable because Participants will be assessed fees based on market share, rather than message traffic, the Participants explain that charging broker-dealers based on message traffic is the most equitable means to establish their fees because message traffic is a significant cost driver of CAT. Accordingly, the Participants believe that it is appropriate to use message traffic to assign fee tiers to broker-dealers.<sup>112</sup> The Participants state that charging Execution Venues based on message traffic, on the other hand, will result in large and small Execution Venues paying comparable fees as both types of Execution Venues produce similar amounts of message traffic.<sup>113</sup> The Participants believe such a result would be inequitable; therefore, they decided to base fees for Execution Venues and broker-dealers on different criteria.<sup>114</sup>

In response to a commenter's concern that the Participants only established two tiers for themselves, the Participants state that the CAT NMS Plan permits them to establish only two tiers and that two tiers were sufficient to distinguish between the Execution Venues.<sup>115</sup> The Participants state that adding more tiers will significantly increase fees for Tier 1 and Tier 2

Execution Venues with the result of fees for Tier 1 Execution Venues being much higher than fees for Tier 1 Industry Members.<sup>116</sup> In turn, the Participants believe that such a result will violate Section 11.2(c) of the CAT NMS Plan, which states that, in establishing the funding of the Company, the Operating Committee shall seek to establish a tiered fee structure in which the fees charged to the CAT Reporters with the most CAT-related activity (measured by market share and/or message traffic) are generally comparable (where, for these comparability purposes, the tiered fee structure takes into consideration affiliations between or among CAT Reporters, whether Execution Venues and/or Industry Members).<sup>117</sup>

In response to the comment asking why it makes sense to charge a fixed fee for all market participants within a single tier and questioning the results of fixed-fee tiering, the Participants explain that the proposed approach "helps ensure that fees are equitably allocated among similarly situated CAT Reporters, thereby lessening the impact of CAT fees on smaller firms,"<sup>118</sup> and provides predictability of payment obligations.<sup>119</sup> The Participants also state that the fixed-fee approach provides elasticity to take into account any changes in message traffic levels through the use of predefined fixed percentages instead of fixed volume thresholds, and would not likely cause CAT Reporters to change their behavior (and impact liquidity) to avoid being placed in a higher tier.<sup>120</sup>

#### Options Market-Maker Fees

One commenter believes that the proposed fees will be unsustainable for small options market-makers.<sup>121</sup> The commenter explains that because the nature of their business requires the generation of quotes, the proposed assessment of fees based on message traffic will place small options market-makers in the top Industry Member fee tiers, "[a]lthough this category of broker-dealer is relatively small in terms of net worth . . . ." <sup>122</sup> The commenter notes

<sup>100</sup> See MFA Letter, *supra* note 60, at 2.

<sup>101</sup> See Response from Participants, *supra* note 60, at 5.

<sup>102</sup> See *id.*

<sup>103</sup> See *id.* at 15.

<sup>104</sup> See *id.* The Participants note that "the proposed funding model estimates total fees for associated Participant complexes that are in several cases nearly two to three times larger than the single largest broker-dealer complex." See *id.* at 6.

<sup>105</sup> See *id.* at 15.

<sup>106</sup> See SIFMA Letter; FIA Letter, *supra* note 60.

<sup>107</sup> See FIA Letter, *supra* note 60, at 3; SIFMA Letter, *supra* note 60, at 4 (stating "the Plan Participants proposals inexplicably propose a tiering mechanism for themselves that is based on not their relative impact to the CAT system, but instead on their relative market share").

<sup>108</sup> See SIFMA Letter, *supra* note 60, at 4.

<sup>109</sup> See *id.*

<sup>110</sup> See FIA Letter, *supra* note 60, at 3; see also SIFMA Letter, *supra* note 60, at 4.

<sup>111</sup> See FIA Letter, *supra* note 60, at 3.

<sup>112</sup> See Response from Participants, *supra* note 60, at 6.

<sup>113</sup> See *id.* at 6.

<sup>114</sup> See *id.* The Participants also explain that, while ATSs have varying levels of message traffic, they operate similarly to exchanges and therefore were categorized as Execution Venues. See *id.* at 6–7.

<sup>115</sup> See *id.* at 13. The Participants also state that, unlike for Industry Members, the data for Execution Venues "did not suggest a break point(s) for the markets with less than 1% market share that would indicate an appropriate threshold for creating a new tier or tiers." *Id.*

<sup>116</sup> See *id.* at 14.

<sup>117</sup> See *id.*; Section 11.2(c) of the CAT NMS Plan.

<sup>118</sup> See Response from Participants, *supra* note 60, at 14.

<sup>119</sup> See *id.*

<sup>120</sup> See *id.*

<sup>121</sup> See Cerny & O'Malley Letter, *supra* note 60, at 1. The commenter notes that options market-makers have an obligation to quote "hundreds of thousands of options series" and that this fact was acknowledged by the Commission, which exempted them from submitting their quotes to the Central Repository. See *id.* at 3; see also note 40 *supra*.

<sup>122</sup> See Cerny & O'Malley Letter, *supra* note 60, at 1.

that the top three tier fees for Industry Members are comparable to the largest equity Execution Venues, which it states is neither equitable nor fair.<sup>123</sup> The commenter also believes that smaller broker-dealers, such as options market-makers and other electronic trading firms, will be in the top fee tiers, while larger “full-service” firms that produce fewer electronic messages would be in the lower fee tiers.<sup>124</sup> The commenter argues that this result is not equitable or fair to smaller market participants.<sup>125</sup>

Additionally, the commenter believes that charging Industry Members on the basis of message traffic will disproportionately impact options market-makers because, unlike for equities, message traffic would include options strikes and series.<sup>126</sup> Further, the commenter notes that options market-makers have continuous quoting obligations imposed by the exchanges, and consequently, expected increases in the options classes listed by the exchanges will increase CAT fees for options market-makers.<sup>127</sup> The commenter adds that the proposed fees may impact the ability of small options market-makers to provide liquidity and that such Industry Members may choose to leave the market-making business in order to avoid quoting requirements.<sup>128</sup>

In their response, the Participants explain that since message traffic is a major cost component for CAT, they believe it is an appropriate basis for assigning Industry Member fee tiers.<sup>129</sup> The Participants note that options market-makers will produce a large amount of message traffic to be processed by the CAT, so the Participants intend to charge them CAT fees.<sup>130</sup>

#### ATS Fees

One commenter objects to the proposed fees for ATSs, which are the same fees as Participants under the Industry Member Fee Filings, as unreasonable, because it believes the fees would result a significant burden on small ATSs and a barrier to entry for new ATSs that would not similarly apply to the Participants.<sup>131</sup>

<sup>123</sup> See *id.* at 3.

<sup>124</sup> See *id.* at 4.

<sup>125</sup> See *id.*

<sup>126</sup> See *id.* at 2.

<sup>127</sup> See *id.* at 3.

<sup>128</sup> See *id.* at 3, 4, 5.

<sup>129</sup> See Response from Participants, *supra* note 60, at 6, 17.

<sup>130</sup> See *id.* at 17 n.96; see also note 40, *supra*.

<sup>131</sup> See SIFMA Letter, *supra* note 60, at 4. SIFMA states that Tier 2 Execution Venues will produce significantly more reports to CAT than Tier 2 ATSs, but points out that Tier 2 Execution Venues and Tier 2 ATSs will be subject to the same CAT Fees. See *id.*

Another commenter objects to the Industry Member Fee Filings’ treatment of smaller Equity Execution Venues (such as low volume ATSs), opining that such treatment is unfair and anti-competitive.<sup>132</sup> The commenter also argues that smaller Execution Venues that were assigned to the second fee tier would be required to pay two-thirds of the fees allocated to “the enormous NYSE or Nasdaq exchanges.”<sup>133</sup> This commenter suggests adding at least one tier for small ATSs executing in the aggregate less than 1% of NMS stocks (based on trade volume), as well as for ATSs executing OTC Equity securities, and allocating approximately 1.5% of the total costs assigned to all Execution Venues to that tier.<sup>134</sup>

In response to the comment noting that charging ATSs the same CAT fees as Execution Venues would result in a significant burden on smaller ATSs and act as a barrier to entry, the Participants reiterate that two fee tiers for Execution Venues were appropriate because adding tiers would “compromise the comparability of fees between Execution Venues and Industry Members with the most CAT-related activity. . . . [C]reating additional tiers could have unintended consequences on the funding model such as creating greater discrepancies between the tiers.”<sup>135</sup> The Participants also explain that they decided to treat Execution Venues and ATSs in the same way because of the similarities of their business models and estimated burden on CAT.<sup>136</sup>

In response to the comment recommending the addition of a tier for small ATSs executing in the aggregate less than 1% of NMS stocks, the Participants explain that two fee tiers for Execution Venues were appropriate because adding tiers would “compromise the comparability of fees between Execution Venues and Industry Members with the most CAT-related activity.”<sup>137</sup> The Participants also state that they considered adding more than two tiers of Execution Venue fees, but that doing so would result greatly increase the fees imposed on Tier 1 Equity Execution Venues and “diminish comparability between Execution Venues and Industry Members in a manner that would be difficult to justify under the funding model.”<sup>138</sup>

<sup>132</sup> See OTC Markets Letter, *supra* note 60, at 1–2.

<sup>133</sup> See *id.* at 9.

<sup>134</sup> See *id.*

<sup>135</sup> See Response from Participants, *supra* note 60, at 16.

<sup>136</sup> See *id.* at 6–7.

<sup>137</sup> See *id.* at 16.

<sup>138</sup> See *id.*

#### OTC Equity Securities Execution Venues

One commenter objects to the Industry Member Fee Filings’ treatment of Execution Venues for OTC Equity securities, opining that it is unfair and anti-competitive.<sup>139</sup> The commenter particularly objects to the assignment of OTC Link ATS to the first fee tier of Execution Venues with large Execution Venues for NMS Stocks.<sup>140</sup> The commenter states that OTC Link ATS was placed in the first CAT fee tier because fee tier assignments are inappropriately based on market share calculated from share volume.<sup>141</sup> The commenter states that the number of trades in OTC Equity Securities is relatively small,<sup>142</sup> as opposed to share volume “due to the disproportionately large number of shares being traded on the OTC equity market as compared to the NMS market . . . .”<sup>143</sup> The commenter explains that many OTC Equity Securities are priced at less than one dollar—and a significant number at less than one penny—and that low-priced shares tend to trade in larger quantities.<sup>144</sup> Because the fee tiers are based on market share calculated from share volume, the commenter points out that OTC Link ATS has the greatest market share of all of the Execution Venues in both NMS Stocks and OTC Equity Securities at 29.90% and accordingly was assigned to the same fee tier as exchanges that the commenter claims have approximately 20 times greater trading revenues than OTC Link ATS.<sup>145</sup> The commenter believes that this unfairly burdens the market for OTC Equity Securities.<sup>146</sup> The commenter recommends placing Execution Venues for OTC Equity Securities in separate tiers from large Execution Venues for NMS Stocks and allocating costs to tiers based on number of trades to align tiers with CAT usage and costs.<sup>147</sup> Specifically, the commenter believes that there should be

<sup>139</sup> See OTC Markets Letter, *supra* note 60, at 1–2.

<sup>140</sup> See *id.* at 1, 3, 5.

<sup>141</sup> See *id.* at 6–8. The commenter states that “[s]hare volume is an inappropriate method for determining market share, because the costs of operating the CAT are not correlated with the number of shares traded in any particular Execution Venue. Instead, CAT’s costs are impacted by the number of orders and executions.” See *id.* at 6. The commenter recommends using the number of trades in lieu of share volume, or dollar volume instead of share volume, for determining market share. See *id.* at 7–8.

<sup>142</sup> See *id.* at 4.

<sup>143</sup> See *id.* at 7.

<sup>144</sup> See *id.*

<sup>145</sup> See *id.* at 3.

<sup>146</sup> See *id.*

<sup>147</sup> See *id.* at 8.

separate tiers for the Execution Venues for OTC Equity Securities with approximately 0.5% of the total costs assigned to all Execution Venues allocated to that tier, or at least one additional tier for small ATSS executing in the aggregate less than 1% of NMS stocks (based on trade volume) and OTC Equity securities with approximately 1.5% of the total costs assigned to all Execution Venues allocated to that tier.<sup>148</sup>

In their response, the Participants state that the CAT NMS Plan provides for the use of share volume to calculate market share for Execution Venues that execute transactions in NMS Stocks or OTC Equity Securities.<sup>149</sup> The Participants explain that two fee tiers for Execution Venues were appropriate because adding tiers would “compromise the comparability of fees between Execution Venues and Industry Members with the most CAT-related activity”<sup>150</sup> and that they considered adding more than two tiers of Execution Venue fees, but that doing so would result greatly increase the fees imposed on Tier 1 Equity Execution Venues and “diminish comparability between Execution Venues and Industry Members in a manner that would be difficult to justify under the funding model.”<sup>151</sup> The Participants believe that the CAT Fees do not impose an unnecessary or inappropriate burden on competition on OTC Equity Securities Execution Venues in light of the potential negative impact of increasing the number of fee tiers applicable to Execution Venues and the decision to use market share, as calculated by share volume, as the basis for Execution Venue CAT Fees.<sup>152</sup>

#### IV. Discussion

Pursuant to Section 11A of the Act<sup>153</sup> and Rule 608(b)(3)(iii) of Regulation NMS thereunder,<sup>154</sup> at any time within 60 days of the filing of any such amendment, the Commission may summarily abrogate the amendment and require that the amendment be re-filed in accordance with paragraph (a)(1) of Rule 608<sup>155</sup> and reviewed in accordance with paragraph (b)(2) of Rule 608,<sup>156</sup> if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of

investors, or the maintenance of fair and orderly markets, to remove impediments to, and perfect the mechanisms of, a national market system or otherwise in furtherance of the purposes of the Act. Concerns have been raised regarding Amendment No. 2 and the Commission believes that the justifications provided by the Participants are not sufficient for the Commission to determine whether Amendment No. 2 is consistent with the Act. Accordingly, the Commission believes that the procedures provided by Rule 608(b)(2)<sup>157</sup> will provide a more appropriate mechanism for determining whether Amendment No. 2 is consistent with the Act.

The Commission believes that Amendment No. 2 raises questions as to whether the allocation of the total CAT costs recovered between and among Industry Members and Execution Venues is reasonable, equitable, and not unfairly discriminatory under Section 6 and Section 15A of the Act. Moreover, the Commission does not believe that the Participants have provided an adequate justification to support a determination that the allocation of 75% of total CAT costs recovered to Industry Members (other than Execution Venue ATSS) and 25% to Execution Venues is equitable and not unfairly discriminatory or that the fees will not result in an undue or inappropriate burden on competition. The Commission also does not believe that the Participants have adequately explained that the CAT Fees are consistent with the funding principles set forth in the CAT NMS Plan, which require that the allocation of “costs among Participants and Industry Members . . . is consistent with the [ ] Act taking into account . . . distinctions in the securities trading operations of Participants and Industry Members and their relative impact upon the Company resources and operations”<sup>158</sup> and required that such fees “avoid any disincentives such as placing an inappropriate burden on competition and a reduction in market quality.”

Further, the Commission believes that Amendment No. 2 raises questions as to whether the determination to place Execution Venues for OTC Equity Securities in the same tier structure as Execution Venues for NMS Stocks will result in an undue or inappropriate burden on competition under Section 6 and Section 15A. Specifically, the decision to group Execution Venues for OTC Equity Securities and NMS Stocks in one tier structure raises questions about the effect on competition,

recognizing that the application of share volume may lead to different outcomes as applied to OTC Equity Securities and NMS Stocks. Similarly, the decision to place Execution Venues representing less than 1% of NMS market share in the same tier structure as other Equity Execution Venues raises questions about burdens on competition. The Commission believes that the Participants have not provided adequate justification to support a conclusion that their tier structure will not result in an undue or inappropriate burden on competition.

#### V. Conclusion

For the reasons discussed above, the Commission believes that the procedures provided by Rule 608(b)(2) of Regulation NMS<sup>159</sup> will provide a more appropriate mechanism for determining whether Amendment No. 2 is consistent with the Act. Therefore, the Commission finds that it is necessary or appropriate in the public interest, for the protection of investors, or the maintenance of fair and orderly markets, to remove impediments to, and perfect the mechanisms of, a national market system or otherwise in furtherance of the purposes of the Act, to abrogate Amendment No. 2.

*It is therefore ordered*, pursuant to Section 11A of the Act,<sup>160</sup> and Rule 608 thereunder,<sup>161</sup> that Amendment No. 2 to the CAT NMS Plan be, and hereby is, summarily abrogated. If the Participants choose to re-file Amendment No. 2, they must do so pursuant to Section 11A of the Act and Amendment No. 2 must be re-filed in accordance with paragraph (a)(1) of Rule 608 of Regulation NMS<sup>162</sup> for review in accordance with paragraph (b)(2) of Rule 608 of Regulation NMS.<sup>163</sup>

By the Commission.

**Eduardo A. Aleman,**

*Assistant Secretary.*

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<sup>148</sup> See *id.* at 9.

<sup>149</sup> See Response from Participants, *supra* note 60, at 16.

<sup>150</sup> See *id.*

<sup>151</sup> See *id.*

<sup>152</sup> See *id.*

<sup>153</sup> 15 U.S.C. 78k-1.

<sup>154</sup> 17 CFR 242.608.

<sup>155</sup> 17 CFR 242.608(a)(1).

<sup>156</sup> 17 CFR 242.608(b)(2).

<sup>157</sup> 17 CFR 242.608(b)(2).

<sup>158</sup> Section 11.2(b) of the CAT NMS Plan.

<sup>159</sup> 17 CFR 242.608(b)(2).

<sup>160</sup> 15 U.S.C. 78k-1.

<sup>161</sup> 17 CFR 242.608.

<sup>162</sup> 17 CFR 242.608(a)(1).

<sup>163</sup> 17 CFR 242.608(b)(2).