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August 16, 2021

Ms. Vanessa Countryman
Secretary
US Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Joint Industry Plan; Order Instituting Proceedings to Determine Whether to Approve or Disapprove an Amendment to the National Market System Plan Governing the Consolidated Audit Trail (File No. 4-698)

Dear Ms. Countryman:

The Investment Company Institute (“ICI”)¹ is writing to respond to the Securities and Exchange Commission’s (“Commission”) request for additional comment² on the proposed amendment to the Consolidated Audit Trail (“CAT”) National Market System Plan (“CAT NMS Plan”) to revise the CAT funding model (“proposed CAT Funding Model”).³ The CAT NMS Plan Participants, *i.e.*, the SROs, most recently proposed a revised CAT Funding Model, which, we unfortunately cannot support. We therefore recommend that the Commission disapprove the proposed amendment and encourage the SROs to work with Industry Members and other non-

¹ The [Investment Company Institute](https://www.ici.org) (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI’s members manage total assets of US\$31.5 trillion in the United States, serving more than 100 million US shareholders, and US\$9.6 trillion in assets in other jurisdictions. ICI carries out its international work through [ICI Global](https://www.ici.org/global), with offices in London, Hong Kong, and Washington, DC.

² Joint Industry Plan; Order Instituting Proceedings to Determine Whether to Approve or Disapprove an Amendment to the National Market System Plan Governing the Consolidated Audit Trail, Release No. 34-92451, 86 Fed. Reg. 40114 (July 26, 2021).

³ Joint Industry Plan; Notice of Filing of Amendment to the National Market System Plan Governing the Consolidated Audit Trail by BOX Exchange LLC; Cboe BYX Exchange, Inc., Cboe BZX Exchange, Inc., Cboe EDGA Exchange, Inc., Cboe EDGX Exchange, Inc., Cboe C2 Exchange, Inc. and Cboe Exchange, Inc., Financial Industry Regulatory Authority, Inc., Investors Exchange LLC, Long-Term Stock Exchange, Inc., Miami International Securities Exchange LLC, MEMX, LLC, MIAX Emerald, LLC, MIAX PEARL, LLC, Nasdaq BX, Inc., Nasdaq GEMX, LLC, Nasdaq ISE, LLC, Nasdaq MRX, LLC, Nasdaq PHLX LLC, The NASDAQ Stock Market LLC; and New York Stock Exchange LLC, NYSE American LLC, NYSE Arca, Inc., NYSE Chicago, Inc., and NYSE National, Inc., Release No. 34-91555, 86 Fed. Reg. 21050 (Apr. 21, 2021) (“Proposed Amendment”).

SRO participants to establish an alternative that is consistent with the Securities Exchange Act of 1934 (“Exchange Act”) and rules thereunder.⁴

ICI has two primary concerns. First, the proposed message traffic-based allocation methodology may harm market quality and liquidity for all NMS securities, including exchange-traded funds (ETFs). In addition, non-SRO participants are not able to provide meaningful input into how the CAT is administered, despite ultimately shouldering the CAT’s considerable operational costs. Although the proposed funding model would allocate those costs specifically to Industry Members, we expect these costs to likely be passed down in part to registered funds and their investors.⁵ These concerns are heightened by the CAT’s 2021 annual operating cost estimate, which is significantly higher than the operating cost estimates provided in past years.⁶ To ensure a more collaborative and constructive approach to administering the CAT, we strongly recommend that the Commission amend the CAT NMS Plan to include non-SRO participant representation on the Operating Committee, including representatives of registered funds.

I. Cost Allocation Methodology

The proposed CAT Funding Model would implement a bifurcated approach that apportions the CAT’s development, implementation, and operating costs between the plan Participants and Industry Members. Industry Members as a group would be required to pay 75 percent of those costs and each would be assessed a fee based on the level of message traffic generated by their respective market activities, *e.g.*, orders or quoting. As proposed, these fees would be subject to certain market making discounts, as well as a minimum fee and maximum fee level.

This funding model is not consistent with the Exchange Act, which requires the equitable allocation of reasonable fees⁷ that do not unfairly discriminate between customers, issuers, brokers, or dealers⁸ and do not impose unnecessary or inappropriate burdens on competition.⁹

⁴ The CAT NMS Plan defines “Industry Members” as members of a national securities exchange or a national securities association, *i.e.*, broker-dealers. CAT NMS Plan at Section 1.1. We refer to “non-SRO participants” herein to include Industry Members as well as registered funds and other market participants.

⁵ The CAT NMS Plan itself states that “broker-dealers may seek to pass on to investors their costs to build and maintain the CAT, which may include their own costs and any costs passed on to them by Participants The extent to which these costs are passed on to investors depends on the materiality of the costs and the ease with which investors can substitute away from any given broker-dealer.” *See* CAT NMS Plan at Appendix C-57.

⁶ For example, the CAT Operating Committee has estimated the CAT’s 2021 operating budget to be approximately \$133 million. *See* Exhibit B of Proposed Amendment. This represents a significant increase over the prior 2017 estimate of annual operating costs of approximately \$51 million. Amendment No. 2 of CAT NMS Plan at 30 (June 14, 2017).

⁷ 15 U.S.C. 78f(b)(4); 15 U.S.C. 78o-3(b)(5).

⁸ 15 U.S.C. 78f(b)(5); 15 U.S.C. 78o-3(b)(6).

⁹ 15 U.S.C. 78f(b)(8); 15 U.S.C. 78o-3(b)(9). The proposed funding model is also inconsistent with the CAT’s own funding principles, which include “avoid[ing] any disincentives such as placing an inappropriate burden on competition and a reduction in market quality.” CAT NMS Plan at Section 11.2(e).

Not only would Industry Members as a group bear a significant majority of the CAT's overall costs, but assessing CAT fees to each Industry Member based on message traffic could lead to unintended consequences that diminish market quality and liquidity for all NMS securities.¹⁰

We highlight, for example, the potential effects of the message traffic-based allocation methodology on ETFs. ETF market makers are critical to providing market depth and tight spreads in these markets—their market activities, which include quoting and trading that helps to align ETF share prices with underlying values, can generate higher message levels than trading in other markets. Thus, the proposed methodology could further impose disproportionate costs on market makers, leading them to reduce quoting levels and/or offer wider bid-ask spreads to manage or offset those costs. This outcome could diminish ETF market competition and reduce investor choice in ETF products, which are an efficient and cost-effective way for investors to access a broad range of markets, sectors, regions, and industries.

We therefore strongly urge the Commission to disapprove the proposed funding model and encourage the plan Participants to work more closely with Industry Members and other non-SRO participants to develop an alternative approach that is fair and equitable.¹¹

II. CAT NMS Plan Governance

ICI strongly recommends that the Commission amend the CAT NMS Plan to add non-SRO representatives, including representatives of registered funds, to the Operating Committee.¹² In this instance, non-SRO participation on the Operating Committee would have enabled a broad range of affected market participants to directly work with plan Participants to develop a more workable cost allocation methodology. The existing governance structure, however, limits committee membership to SROs only, thus depriving non-SRO participants, such as registered funds, of a meaningful voice and limiting timely transparency into how the CAT is administered.

Given the cost and operational impact of the CAT on all market participants, we urge the Commission to change the existing governance model, which currently allows the SROs to administer the CAT on an exclusive basis. The actions of the Operating Committee, including

¹⁰ We acknowledge that the proposed funding model provides discounts from CAT fees for market making in equities that are intended to mitigate against potential disincentives to market making. The methodology for estimating the impact of such discounts, however, is overly complex and, therefore, cannot ensure that market makers would not change their market behavior in ways that would reduce market quality and liquidity.

¹¹ We note that several commenters recommend a funding model that resembles the manner through which Section 31 fees are administered. These fees are determined based on transaction volumes and, thus, could potentially avoid the problems that a message traffic-based approach may raise as described above. We believe that this approach warrants closer consideration.

¹² ICI previously recommended that the Commission modify the governance structure of the CAT NMS Plan prior to its adoption to include non-SRO participants. *See, e.g.*, Letter from David W. Blass, General Counsel, ICI, to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission (July 18, 2016), *available at* <https://www.sec.gov/comments/4-698/4698-8.pdf>.

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how it manages the CAT's operating expenses and allocates those costs, can profoundly affect the trading activity of registered funds and other market participants. Registered funds therefore have a strong interest in ensuring that the CAT operates in an efficient and cost-effective manner. While the Operating Committee recently proposed to provide greater transparency of the CAT's operating costs,¹³ we strongly believe that non-SRO participants should also be members of the Operating Committee. The recommended approach would allow them to assess and offer meaningful input regarding CAT administrative and operational matters on an ongoing basis. Since non-SRO participants ultimately may bear a large portion of the CAT's operating costs, they should be given the opportunity to facilitate cost savings, including through identifying and addressing the factors that have been driving up those costs.

* * *

We appreciate the opportunity to provide our views on the proposed CAT Funding Model and continue to support the ongoing regulatory and industry efforts to achieve full CAT implementation. These efforts will provide the data necessary to conduct effective market oversight and ensure that the markets operate in a fair, efficient, and orderly manner.¹⁴ If you have any questions, please feel free to contact me at ddonohue@ici.org or Nhan Nguyen, Assistant General Counsel at nhan.nguyen@ici.org.

Regards,

/s/ Dorothy Donohue

Dorothy Donohue
Deputy General Counsel, Securities Regulation

¹³ In response to commenters' concerns, the Operating Committee has offered to publicly disclose the CAT's annual operating budget at the start of each year, with quarterly updates. The committee also states that it plans to "provide greater clarity and education regarding the cost drivers for CAT to the industry through ongoing webinars and other methods." Letter from Michael Simon, CAT NMS Operating Committee to Vanessa Countryman, Secretary, Commission (July 14, 2021), available at <https://www.sec.gov/comments/4-698/4698-9061305-246406.pdf>.

¹⁴ We have long supported the CAT, which is a single audit trail that comprises all order and execution information for exchange-listed equities and options. *See, e.g.*, Letter from Karrie McMillan, General Counsel, ICI to Elizabeth M. Murphy, Secretary, Commission (Aug. 9, 2010), available at <https://www.sec.gov/comments/s7-11-10/s71110-50.pdf>.

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cc: The Honorable Gary Gensler
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman
The Honorable Allison Herren Lee
The Honorable Caroline Crenshaw

David Saltiel, Division of Trading and Markets
David Shillman, Division of Trading and Markets
John Roeser, Division of Trading and Markets