GLOBAL MARKETS ADVISORY GROUP
395 Springfield Avenue, Suite 4
Berkeley Heights, N.J. 07922
(908) 219-4310

To:	CAT Bid Team	From:	Daniel M. Labovitz
Subject:	Summary of SEC Exemptive Relief	Date:	March 3, 2016

On March 1, 2016, the Securities and Exchange Commission issued its Order Granting Exemptions from Certain Provisions of Rule 613 Pursuant to Section 36(a)(1) of the Securities Exchange Act of 1934 (the "Exemption Order").

I. BACKGROUND

The Exemption Order responds to several requests by the SROs for exemptive relief from various provisions of the CAT NMS rule. The exemptive requests were submitted to the SEC in three submissions: an initial request on January 30, 2015; a supplemental request on April 3, 2015; and a second supplemental request on September 2, 2015.

The SROs submitted these requests on a parallel track with the CAT NMS Plan: the first version was filed with the SEC on September 30, 2014; and an Amended and Restated CAT NMS Plan was submitted on February 27, 2015. Notably, the Amended and Restated CAT NMS Plan assumed that the Commission would grant the SROs' various exemptive requests. That assumption will likely have a positive effect on the project's implementation timeline, because it means that the SEC can now expeditiously proceed with publishing the CAT NMS Plan without waiting for the SROs to submit a third version of the Plan incorporating the exemptive relief. The implications for the industry are also significant: since the assumptions in Amended and Restated CAT NMS Plan have now been essentially validated, industry participants can be reasonably certain that there will not be any additional material changes to the plan. They can (and undoubtedly will) therefore begin preparing comment letters to the Commission.

It is important to bear in mind that the SEC is <u>not</u> deciding at this point whether the SROs' proposed alternatives to the CAT NMS Rule provisions are more efficient or effective than the original requirements in Rule 613. The SEC is merely allowing the SROs to propose the alternatives for consideration as part of the CAT NMS Plan; it will decide whether to approve or deny the proposed alternatives after receiving public comments on the overall Plan, including the proposed alternatives.

The remainder of this memo summarizes the key elements of the exemptive relief that the SEC is granting.

II. SUMMARY OF PROPOSALS AND EXEMPTIVE RELIEF

A. Options Market Maker Quotes

1. The problem

Reg NMS Rule 613 currently requires that the details of the option market makers' quotations must be reported to CAT by both the options market makers[1] and the options exchanges to which they route their quotes.[2] The SROs believe that the information submitted by the options market makers and the options exchanges will be largely identical.

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose a CAT NMS Plan that would only require the option exchanges to report to CAT. The SROs project that eliminating the duplicative information will reduce the size of the data reported to CAT by up to 18 billion records per day, and will result in a cost savings to the CAT Processor of between $2 million and $16 million over five years.

The only data element that would be missing under the SROs' alternative is the time that a market maker routes its quote (or modification or cancellation of the quote). Accordingly, the SROs are proposing that options market makers be required to submit to the relevant options exchange an element known as the "Quote Sent Time", which the options exchanges will, in turn, submit to the CAT repository without change.

B. Customer ID

1. The problem

Reg NMS Rule 613 currently requires SROs and CAT Reporters to use a single, unique Customer-ID and CAT-Reporter ID for each customer and broker-dealer. The SROs are concerned that the administrative burden of assigning unique customer IDs will have negative down-stream impacts, including making the account-opening and on-boarding process more inefficient; and requiring firms to reprogram their account management systems to include the Customer ID. They are also concerned about information security: if security at one firm is compromised and Customer IDs are stolen, those Customer IDs would be compromised for all firms. Smaller firms, with fewer resources for information security, could therefore make the entire system insecure, even for the largest firms with well-resourced information security teams. Firms would prefer to use existing account identifiers as the basis for identifying customers when submitting to the CAT.

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative method for identifying customers, known as the "Customer Information Approach". In this approach, firms would use a "firm-designated identifier" ("FDI") for each trading account, which could be the existing identifier, provided that the FDIs are unique across the firm for each business date. Broker-dealers would be required to submit an initial set of information identifying the customer to the Central Repository (and thereafter submit updates periodically and as needed).[3] The CAT Processor would link the FDI with the identifying information and then assign a unique Customer-ID to the customer for use in the CAT database, and would create a secure method and process for ensuring that broker-dealers provide daily or periodic updates to the identifying information. The SROs believe that this process would place the information security burden on the CAT Processor (who is likely more equipped than smaller firms to handle

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[1] Options market makers would have to report the CAT Order ID; the date and time the order is *routed*; the CAT Reporter ID of the market maker and the exchange to which the order is routed; and the material terms of the order.

[2] Exchanges would have to report the CAT Order ID; the date and time the order is *received*; the CAT Reporter ID of the market maker and the exchange receiving the route; and the material terms of the order.

[3] The required information would include account type; account effective date; the Customer's name, address, date of birth, tax identification number or Social Security number; the individual's role in the account; and, if applicable, the Legal Entity Identifier ("LEI") and/or Large Trader ID.

it adequately), while not unnecessarily burdening the existing customer/account identification infrastructure that is already in place at firms.

C. Modification and Cancellation of Orders

1. The problem

Reg NMS Rule 613 requires that CAT Reporters submit the CAT-Reporter ID of the broker-dealer, or the Customer-ID of the person, giving a modification or cancellation instruction. The SROs believe that this requirement introduces a potential mismatch between the level of detail required when an order is originated and the level of detail when an order is modified or cancelled: in the former situation, only the Customer-ID is required, which is an account-level identifier. This means that for accounts with multiple owners, there would be no record of the *person* who originated the order, only the account from which it originated. The SROs believe that when it is necessary, they and the SEC have the ability to drill down into the account with the firms to identify the specific person who originated an instruction. In the ordinary course, however, they believe that the critical piece of information for regulators is not the identity of the person initiating an instruction, but whether the instruction originated from the Customer or was instead initiated by the broker-dealer or exchange.

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative in which the CAT Reporter would report whether a modification or cancellation instruction was given by the Customer associated with the order, or was initiated by the broker-dealer or exchange associated with the order.

D. Effective Date vs. Account Opening Date

1. The problem

Reg NMS Rule 613 requires broker-dealers to report to the Central Repository "Customer Account Information", including the date the account was opened. The SROs have identified several circumstances where the date that the account was opened either can't be determined, or would be inaccurate due to extenuating circumstances. These include circumstances where:

- A relationship identifier, rather than a parent account, has been established for an institutional customer relationship;
- Legacy system data issues prevent a broker-dealer from providing account opening dates for accounts established before the CAT implementation
    - A broker-dealer has switched back-office providers or clearing firms, and the new back-office or clearing firm system identifies the account open date as the date the account was opened on the new system;
    - A broker-dealer is acquired and the account open date becomes the date than account was opened on the post-merger back office/clearing system;
    - A broker-dealer maintains multiple dates associated with accounts and do not consistently designate which is the account opening date (since the parameters of each date are determined by the individual broker-dealer);
    - No account opening date exists for proprietary accounts of the broker-dealer

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative in which

(a) if there is no account open date because there is a relationship identifier in lieu of an account, for relationships established before the CAT implementation, the effective date would be either the date the broker-dealer established the relationship identifier, or the date when trading began using the relevant relationship identifier. For relationships established after the CAT implementation, the effective date would be the date the broker-dealer established the relationship identifier (and no later than the date the first order received);[4]

(b) If there is no account open date because of one of the legacy systems data issues above, for accounts established before the CAT implementation, broker-dealers would be permitted to report an "effective date" in lieu of an account open date.

- In cases where the date was lost because of a new or changed back-office/clearing system, the effective date would be the date the account was established, either directly or via system transfer, at the relevant broker-dealer.
- If the lack of account open date is because of inconsistent date records, the effective date would be the earliest available date.
- If the lack of account open date is because there is no recorded account open date for a proprietary account, the effective date would be either (i) the date the account was established in the broker-dealer or its system(s), or the (ii) the date when proprietary trading began in the account.

The proposed alternatives would not apply if the "date account opened" is available.

E. CAT Reporter ID

1. The problem

Reg NMS Rule 613 requires that CAT Reporters report CAT-Reporter-IDs to the CAT for orders and certain Reportable Events. CAT Reporters must use the same CAT-Reporter-ID for each broker-dealer. The SROs are concerned that there is already a robust infrastructure for identifying firms via the Market Participant Identification process. They note, among other things, that the MPID provides more granular information than the proposed CAT-Reporter-ID, since one firm can have multiple MPIDs, and the MPID can identify activity at the department, business unit or trading desk level within a broker-dealer. They also note that many SRO surveillances currently run based on the MPID, and that moving to a CAT-Reporter-ID would require reprogramming those surveillances (and losing the benefit of the granularity of the MPID).

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative in which broker-dealers would report their existing SRO-assigned MPID used by the relevant SRO specifically for transactions occurring at that SRO, when reporting information to the Central Repository. Exchanges would similarly report the MPIDs used by the broker-dealers on that exchange or its systems in lieu of reporting the CAT-Reporter-ID. The CAT Processor, in turn, would link the MPIDs to the CAT-Reporter-ID for internal use, which ultimately links back to the responsible broker-dealer. SROs would be responsible for reporting and updating MPIDs on a daily basis. The CAT-Reporter-ID generated by the Central Repository for each CAT Reporter would be linked to SRO-assigned identifiers reported on orders and Reportable Events.

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[4] The SROs have also asked (and been granted by the SEC) exemptive relief from the requirement to report "account number" and "account type". For relationship identifiers, the firm would report the relationship identifier in place of the account number, and identify the "type" as "relationship" in the "account type".

Regulators could access information on the CAT Reporter based on either the CAT-Reporter-ID or by another identifier, including MPID.

F. Linking Order Executions to Allocations

1. The problem

Reg NMS Rule 613 requires each CAT Reporter to record and report to the CAT the account number of any subaccounts to which an execution is allocated, in whole or in part. The purpose of this requirement was to permit regulators to link the subaccount to which an allocation was made to the original order placed, and its execution. The SROs believe that this requirement would be extremely burdensome, and would result in artificial linkages that undermine any perceived benefits to regulators. They contend that even if the ultimate allocation of shares executed from an aggregated order is useful to regulators, tying allocations to individual executions is not useful, since the subaccount account information required under the rule would show an artificial relationship between any one execution and one allocation. For example, where shares that are aggregated and executed at an average price are allocated at the average price rather than at the price of any particular execution. This process would make it nearly impossible to associate one allocation with one execution.

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative in which CAT Reporters would send an Allocation Report following each execution to the Central Repository as part of the information required under the Rule. The report would include, at a minimum, (1) the number of shares allocated; (2) the FDI of any accounts or subaccounts to which the shares are allocated; (3) the time of the allocation; (4) the identifier of the firm reporting the allocation; (5) the security; (6) the price per share; and (7) the side of the order (buy/sell). Although there would not be a direct link in CAT between the subaccounts to which an execution is allocated and the execution itself, the Central Repository could use the FDI of the relevant subaccount to link the subaccount holder to those with authority to trade on behalf of the account. In addition, the Allocation Reports used in conjunction with order lifecycle information in the CAT could assist regulators in identifying the probable group of orders that led to allocations.

G. Time Stamp Granularity

1. The problem

Reg NMS Rule 613 requires CAT Reporters to record and report the time of each Reportable Event. In the case of Manual Order Events, the details for the Reportable Event must be "at least to the millisecond". The SROs have identified that it is not currently possible to time-stamp a manual event to the millisecond, since the actions, by their nature, take one second or longer to perform. They are concerned that a millisecond time stamp would create a false sense of precision for data that is by nature imprecise. In any case, the SROs were unable to find any company that produces a manual time-stamping device that records time to the millisecond.

2. The exemptive relief

The SROs asked for (and have been granted by the SEC) permission to propose an alternative in which a Manual Order Event would be recorded with a time stamp at least to the second. If such Manual Order Event is subsequently processed and captured electronically, that electronic capture would be recorded with a time stamp granularity at least to the millisecond.