

MEMO# 35428

September 7, 2023

SEC Adopts Amended Funding Model for the Consolidated Audit Trail

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TO: ICI Members

Equity Markets Advisory Committee

SEC Rules Committee SUBJECTS: Trading and Markets RE: SEC Adopts Amended Funding Model for the Consolidated Audit Trail

On September 6, 2023, the SEC issued an order, in a 3-2 vote, approving amendments related to the National Market System (NMS) Plan governing the funding model for the Consolidated Audit Trail (CAT). The full order is available [here](#), the fact sheet is available [here](#), and the press release is available [here](#).

The CAT NMS Plan requires participants to the CAT NMS Plan (Participants)^[1] and members of a national securities exchange or national securities association (Industry Members) to fund the CAT. The purpose of the funding model is to provide a framework for the recovery of the Participants' costs to create, develop, and maintain the CAT. The adopted amendments set forth the method for allocating the costs to fund the CAT among Participants and Industry Members utilizing an "Executed Share Model." Previously, the CAT costs were to be allocated based on messaging traffic.

The Executed Share Model will allocate costs by charging fees to Participants and Industry Members based on executed equivalent share volume.^[2] Under the Executed Share Model, fees will be allocated equally among (1) the Industry Member that is a CAT executing broker for the buyer in a transaction, (2) the Industry Member that is the CAT executing broker for the seller in a transaction, and (3) the Participant. Such fee for each aforementioned entity will be calculated by multiplying the number of executed equivalent shares in the transaction by one-third and by a "fee rate." The fee rate for CAT fees related to prospective CAT costs would be determined by dividing the reasonably budgeted CAT costs for the upcoming year by the reasonably projected total executed equivalent share volume of all transactions for that year. In addition to prospective costs, Industry Members will also be required to cover historical costs already paid by Participants pursuant to the same three-party fee allocation.^[3] However, for calculating the fee rate for historical CAT costs, the CAT operating committee will divide incurred costs by the reasonably projected total executed equivalent share volume of all transactions during a projected recovery period, which may be no less than two years but no more than five years.

The amendments would further provide that for every new fee rate and adjustment to the fee rate, the Participants must file a Section 19(b) filing with the SEC to implement such fee rate on Industry Members. Further, the CAT LLC's operating committee is required to set a "reasonable" operating budget, as well as to make sure that fees, costs, and expenses are reasonable and will be reasonably incurred in connection with the development, implementation, and operation of the CAT. These filings would be published for public comment.

SEC Chair [Gary Gensler](#) and Commissioners [Peirce](#), [Crenshaw](#), [Uyeda](#), and [Lizárraga](#) delivered statements on the order. While Chair Gensler and Commissioners Crenshaw and Lizárraga vote in favor of the order and discussed the overall importance of the CAT, Commissioners Peirce and Uyeda voted against the order and focused their comments on the costs and expenses of the CAT. Commissioner Peirce noted that Participants have spent nearly \$500 million on the CAT to date and, whereas the original projected annual budget in 2016 was approximately \$50 million, the current budget in 2023 is \$223 million. She also highlighted that Industry Members will be required to pay for historical costs, even though they had very limited say in shaping the CAT, its budget, and incurred expenses. Commissioner Uyeda, quoting a comment letter, stated that "annual increases in CAT operating costs during the past three years [were] 73.2%, 27.3% and 27.0%, respectively, [and] are not sustainable over the long term." Both Commissioners noted the very real possibility that all fees would likely be pushed down to investors.

Kevin Ercoline
Assistant General Counsel

Notes

[1] "Participants" are the national securities exchanges and FINRA, the only national securities association currently existing (collectively, the self-regulatory organizations).

[2] "Executed equivalent share volume" is calculated utilizing executions and a particular multiplier depending on whether the security is an NMS stock, a listed option, or an OTC equity security.

[3] Participants will "pay" for their share of historical costs by cancelling loans made to CAT LLC.