Invested in America

May 12, 2017

Robert W. Cook
President and Chief Executive Officer
FINRA
1735 K Street
Washington DC, 20006

Re: Rule 613 of Regulation NMS report on audit trail reporting for fixed income

Dear Mr. Cook:

The Securities Industry and Financial Markets Association ("SIFMA")[1] submits this letter to follow up our discussion with FINRA staff on the potential incorporation of fixed income securities into the Consolidated Audit Trail ("CAT"). We understand that Rule 613 of Regulation NMS requires FINRA and the other Participants in the CAT NMS Plan to provide the Securities and Exchange Commission ("SEC") with a document outlining how the Participants could incorporate fixed income into the CAT within six months after the effectiveness of the CAT NMS Plan.[2] Understanding the requirements of Rule 613 in this regard, SIFMA believes it is premature to develop any specific plans to incorporate fixed income securities into the CAT prior to the initial implementation of CAT for large broker-dealers, currently scheduled for November 2018. Accordingly, SIFMA recommends that the Participants begin any substantive discussions on the merits of the inclusion of fixed income securities only after the marketplace has tangible experience with CAT reporting. It is critical that any such discussion must rely on, and benefit from, deep industry engagement.

The initial phase of CAT will require audit trail reporting of complicated information in addition to equity transaction reporting, which the industry has experience reporting to FINRA's Order Audit Trail System ("OATS"). For example, the initial phase of CAT will include listed options and customer identification information, which are not currently reported to an audit trail system. In addition, the initial phase of CAT includes the requirement to use the customer data resident in the system to create a

[1] SIFMA is the voice of the U.S. securities industry. We represent the broker-dealers, banks and asset managers whose nearly 1 million employees provide access to the capital markets, raising over $2.5 trillion for businesses and municipalities in the U.S., serving clients with over $20 trillion in assets and managing more than $67 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] On November 15, 2016 the SEC approved the CAT NMS Plan.

linkage and identify the individuals who originated the order with the end customers who received an allocation (from the order). The intricacies of these new products and linkages should inform and educate the Participants, and provide them with a clearer understanding of the inner workings of CAT so that they can be better prepared to consider any additional reporting requirements for fixed income securities in late 2018 or early 2019. The upcoming Rule 613 submission should be focused on outlining the necessary steps to properly evaluate the merits of CAT requirements for the fixed income markets and the alternatives after the initial phase of broker-dealer reporting has begun in 2018. It should not attempt to draw premature conclusions without proper analysis and industry input.

Importantly, any plan to evaluate CAT for fixed income needs to include an analysis of the requirements for fixed income CAT reporting that builds and improves upon the process that was followed by the Participants and the industry for the initial reporting phase of CAT. The initial phase of CAT has been singularly focused on equities with no unique consideration given to fixed income, and the market structure and trade flows for fixed income are considerably different from the equities and listed options markets. For example, the existing fixed income infrastructure would make it extremely difficult for firms to track and report pre-order interactions in the same level of granularity required by CAT for equities and listed options. In this regard, the Participants should be forward thinking and should substantively engage the industry to consider the costs and benefits of any new requirements. Any new reporting model that may be considered must be consistent with the unique characteristics of the fixed income market rather than be an attempt to retrofit fixed income into the current equities-focused architecture.

Moreover, the Participants should undertake a dedicated and robust economic analysis that considers the costs and benefits for the potential expansion of reporting requirements to fixed income securities. The Participants should conduct this analysis only after they scope and develop some preliminary options for any new requirements with sufficient detail to ensure that the industry can reasonably respond to a cost survey.

The Participants must also consider any alternatives to a de novo CAT for fixed income securities, such as FINRA's Trade Reporting and Compliance ("TRACE") reporting system and the MSRB's Electronic Municipal Market Access (EMMA). Today, broker-dealers are investing considerable resources to ensure they are compliant with the significant new reporting requirement that will be effective for Treasury securities in July. Over the last few years, there have also been considerable new trade reporting requirements imposed by both FINRA and the MSRB to enhance the existing architectures with great expense to the industry. Consideration should also be given to the fact that the current TRACE and EMMA reporting regime is real-time rather than an end-of-day batch process. Unnecessarily changing the reporting paradigm for fixed income products to mirror the end-of-day CAT process would not only be expensive and onerous to firms, but would have the suboptimal result of reducing instead of adding value to the data collected. Accordingly, if any new requirements are to be imposed, there is strong interest in leveraging existing architecture to the greatest extent possible rather than developing a new system.

Given the sharp contrasts between the equity and fixed income markets, the governance for any fixed income considerations should be designed so that greater industry representation and input is required. For the most part, the Participants operating electronic, automated equity and listed options exchanges, and have little to no experience in the predominantly over-the-counter fixed income markets. Creating a governance structure to include formal representation by broker-dealers will help to ensure that any plan to include fixed income securities in the CAT properly reflects the underlying market fundamentals.

SIFMA recognizes that the Participants are required to file an outline with the SEC by May 15, 2017 to incorporate other securities, including fixed income, into the CAT. However, we hope that any submission merely outlines a process to gather the information required to make informed decisions and does not attempt to draw premature conclusions on the merits or the operational details of incorporating fixed income securities into the CAT without the benefit of deep industry engagement and input.

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SIFMA greatly appreciates FINRA's consideration of our comments on the impending SEC CAT filing on fixed income securities. We would be pleased to discuss these comments in greater detail with the staff of FINRA. If you have any questions, please contact Sean Davy (phone: 212-313-1118 or sdavy@sifma.org) or Ellen Greene (phone: 212-313-1287 or egreene@sifma.org).

Regards,

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Cc:

Robert Colby, Chief Legal Officer, Financial Industry Regulatory Authority
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