

# Client Update

## SEC Approves CAT Plan While Mitigating Data Security Concerns

### NEW YORK

Lee Schneider  
lschneid@debevoise.com

Zila Acosta-Grimes  
zracosta@debevoise.com

Lilya Tessler  
ltessler@debevoise.com

### WASHINGTON, D.C.

Luke Dembosky  
ldembosky@debevoise.com

On November 15, 2016, the Securities and Exchange Commission (“SEC”) voted and approved the consolidated audit trail (“CAT Plan”), a comprehensive trade reporting system that will allow regulators to access all trade activity in U.S. equity and options markets.<sup>1</sup> The CAT Plan would build a central repository that receives, consolidates and retains the trade and order data reported, owned by a Delaware limited liability company (the “CAT NMS LLC”). We discussed the details of the proposed CAT Plan earlier this year when the rule was proposed.<sup>2</sup> This update highlights the SEC’s approval of the CAT Plan with certain amendments stemming from industry feedback, along with a brief discussion of the inherent data security concerns.

### WHAT CHANGED IN THE FINAL PLAN?

Compared to the May 2016 proposal, the SEC responded to industry feedback by amending the plan with the following changes:

- **Data Security:** The proposed CAT Plan gave the Plan Processor<sup>3</sup> the responsibility for security and confidentiality of all CAT Plan data received and reported to the central repository. In the approved CAT Plan, the SEC strengthened several data security requirements, including with respect to personally identifiable information (“PII”). Data security has been a significant concern to the public and is discussed in greater detail below.

<sup>1</sup> Press Release, SEC, [SEC Approves Plan to Create Consolidated Audit Trail](#) (Nov. 15, 2016). See also [SEC Release No. 34-79237](#) (Nov. 15, 2016).

<sup>2</sup> [The SEC Proposes the CAT Plan, but at What Cost?](#), Debevoise & Plimpton LLP (May 17 2016).

<sup>3</sup> Plan Processor means the Initial Plan Processor or any other Person selected by the Operating Committee pursuant to SEC Rule 613 and Sections 4.3(b)(i) and 6.1, and with regard to the Initial Plan Processor, the Selection Plan, to perform the CAT processing functions required by SEC Rule 613 and set forth in the CAT NMS Plan. [SEC Release No. 34-77724](#) (Apr. 27, 2016).

- **Clock Synchronization:** In the proposed plan, each participant and industry member is required to synchronize its business clocks to within 50 milliseconds of the time maintained by the National Institute of Standards and Technology (“NIST”), at a minimum and consistent with industry standards. The final CAT Plan tightened the clock synchronization standards for self-regulatory organizations (“SROs”) to within 100 microseconds of the time maintained by the NIST. This would require SROs to assess industry standards for clock synchronization based on the type of market participant or system, rather than the industry as a whole, and reflect that refined assessment annually in a report submitted to the SEC. The change is intended to enable regulators to better sequence order events across multiple exchanges.
- **CAT Governance:** The proposed plan outlined the composition of the advisory committee to the CAT NMS LLC. As part of the approval, the SEC expanded the membership of the advisory committee to include an additional investor representative and a representative of a service bureau that provides CAT Plan reporting services.
- **Retirement of Existing Regulatory Reporting Systems:** The final CAT Plan accelerated the deadline for SROs to submit proposals to retire regulatory data reporting systems that will be rendered obsolete by the CAT Plan. The change is intended to reduce the burden on broker-dealers reporting duplicative trade data to multiple systems.

## LOOKING FORWARD

### Ongoing Concern: Data Security

Data Security has been a significant concern for the industry in designing the CAT Plan. More broadly, regulators have made cybersecurity a focus across the financial services industry. Several regulators have published proposed regulations and guidance on the topic.<sup>4</sup> In response to industry feedback, the SEC strengthened the data security requirements of the CAT Plan for the Plan Processor who is tasked with implementing the requirements.

---

<sup>4</sup> See [A Week of Hot News in Cybersecurity and Data Privacy](#), Debevoise & Plimpton LLP (Mar. 8, 2016); [New York’s Proposed Cyber Regulations: Implications and Challenges](#), Debevoise & Plimpton LLP (Sept. 15, 2016); [SFC Cybersecurity Review of Internet/Mobile Trading Systems](#), Debevoise & Plimpton LLP (Oct. 17, 2016); [Federal Financial Regulators to Propose Enhanced Cyber Risk Management Standards](#), Debevoise & Plimpton LLP (Oct. 25, 2016); [UK Government Launches Five Year National Cyber Security Strategy](#), Debevoise & Plimpton LLP (Nov. 2, 2016).

The final CAT Plan establishes various data security requirements regarding connectivity, encryption, and access to PII. The Plan Processor is required to comply with the NIST Cybersecurity Framework and the SROs to maintain information security protocols. In addition, an annual evaluation of the information security program is required. The Plan Processor is required to evaluate the central repository's information security program at least annually. Further, the Plan Processor is responsible for developing access controls to the central repository, a comprehensive information security program and designating a Chief Information Security Officer, who would have various cybersecurity responsibilities. Comments made by industry groups note that the central repository of the CAT Plan may be a significant target for cyber criminals and hackers.<sup>5</sup> Specifically, SIFMA reiterates that it would be "essential that the CAT have robust protections for the massive volume of sensitive transaction data and [PII] it will track and store, which will include social security numbers for every person with a brokerage account."<sup>6</sup>

While the final CAT Plan contained additional data security requirements, financial institutions should continue to monitor this issue, especially once the Plan Processor is selected and begins to design the data security protocols.

### Next Steps

Within the next two months the SROs must select a Plan Processor to implement the CAT Plan; including developing policies and building a central depository. SROs will be required to begin reporting to the central depository within one year, large broker-dealers will begin reporting the following year and small broker-dealers the year after. Industry members should start thinking about compliance and technology changes that will be requirement at each firm, and how this initiative may be integrated with other recent regulatory changes.<sup>7</sup>

\* \* \*

Please do not hesitate to contact us with any questions.

---

<sup>5</sup> For comments made to the proposed CAT Plan see the SEC's [website](#).

<sup>6</sup> Press Release, SIFMA, [SIFMA Highlights Concerns with the Proposed Plan for Developing a CAT System](#), (July 18, 2016).

<sup>7</sup> See [Final DOL Fiduciary Rules Simplify Some Mechanics, but Retain Core Principles . . . and Flaws](#), Debevoise & Plimpton LLP (Apr. 13, 2016).