SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-101648; File No. 4-698)

November 18, 2024

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 Regarding Reporting of Certain Verbal Activity, Floor and Upstairs Activity

I. Introduction

On August 2, 2024, the Consolidated Audit Trail, LLC ("CAT LLC"), on behalf of the following parties to the National Market System Plan Governing the Consolidated Audit Trail (the "CAT NMS Plan" or "Plan"):[1] BOX Exchange LLC, Cboe BYX Exchange, Inc., Cboe BZX Exchange, Inc., Cboe EDGA Exchange, Inc., Cboe EDGX Exchange, Inc., Cboe C2 Exchange, Inc., Cboe Exchange, Inc., Financial Industry Regulatory Authority, Inc., Investors Exchange LLC, Long-Term Stock Exchange, Inc., MEMX, LLC, Miami International Securities Exchange 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, New York Stock Exchange LLC, NYSE American LLC, NYSE Arca, Inc., NYSE Chicago, Inc., and NYSE National, Inc. (collectively, the "Participants")) filed with the Securities and Exchange Commission ("SEC" or "Commission") pursuant to Section 11A(a)(3) of the Securities Exchange Act of 1934 ("Exchange Act"),[2] and Rule 608 thereunder,[3] a proposed amendment to the CAT NMS Plan to amend existing requirements for the consolidated audit trail

[1] The CAT NMS Plan is a national market system plan approved by the Commission pursuant to Section 11A of the Exchange Act and the rules and regulations thereunder. See Securities Exchange Act Release No. 79318 (Nov. 15, 2016), 81 FR 84696 (Nov. 23, 2016). The full text of the CAT NMS Plan is available at www.catnmsplan.com. Unless otherwise defined herein, capitalized terms used herein are defined as set forth in the CAT NMS Plan.

[2] 15 U.S.C 78k-1(a)(3).

[3] 17 CFR 242.608.

("CAT") regarding the reporting of certain verbal activity, floor and upstairs activity (the "Verbal Quotes Amendment").[4] Notice of the Verbal Quotes Amendment was published in the Federal Register on August 20, 2024.[5]

This order institutes proceedings, under Rule 608(b)(2)(i) of Regulation NMS,[6] to determine whether to disapprove the Verbal Quotes Amendment or to approve the Verbal Quotes Amendment with any changes or subject to any conditions the Commission deems necessary or appropriate.

II. Background

Rule 613(j)(9) of Regulation NMS and Section 1.1 of the CAT NMS Plan define the term "reportable event" as including, but not limited to, the original receipt or origination, modification, cancellation, routing, and execution (in whole or in part) of an order, and receipt of a routed order.[7] The term "order" is defined in Rule 613(j)(8) of Regulation NMS and Section 1.1 of the CAT NMS Plan as including: (i) any order received by a member of a national securities exchange or national securities association from any person; (ii) any order originated by a member of a national securities exchange or national securities association; or (iii) any bid or offer.[8] "Bid" and "offer" are defined in Rule 600(b)(16) of Regulation NMS as the bid price or offer price communicated by a member of an exchange or association to any broker-dealer or to

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4 See Letter from Brandon Becker, CAT NMS Plan Operating Committee Chair, to Vanessa Countryman, Secretary, Commission, dated August 2, 2024.

5 See Securities Exchange Act Release No. 100727 (Aug. 14, 2024), 89 FR 67499 (Aug. 20, 2024) (the "Notice").

6 17 CFR 242.608(b)(2)(i).

7 17 CFR 242.613(j)(9).

8 17 CFR 242.613(j)(9).

any customer, at which it is willing to buy or sell one or more round lots of an NMS security, as principal or agent, but excluding indications of interest.[9]

Rule 613 and the CAT NMS Plan both require that the Industry Members and the Participants capture and report quotes and orders that meet the definition of a CAT reportable event, with no exclusion for verbal quotes and orders.[10] The Commission previously granted CAT LLC's request for temporary exemptive relief until July 31, 2026[11] for the reporting to CAT of the following activities: (i) "floor broker verbal announcements of firm orders on an exchange that are otherwise reported as systematized orders; (ii) market maker verbal announcements of firm quotes on an exchange trading floor; (iii) telephone discussions between an Industry Member and a client that may involve firm bid and offer communications; and (iv) unstructured electronic and verbal communications that are not currently captured by Industry Member order management or execution systems (e.g., Bloomberg chats, text messages)."[12]

III. Summary of the Verbal Quotes Amendment

CAT LLC proposes to amend the CAT NMS Plan to state that the activities subject to the July 2023 Exemptive Order (the "Exempt Activities") shall not be reportable as Participant Data or Recorded Industry Member Data that Participants and Industry Members, as applicable, must

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9 17 CFR 242.600(b)(8).

10 Unstructured verbal or manual communications on exchange floors and "upstairs" are reportable events under Rule 613 and the CAT NMS Plan because firm verbal quotes and orders, whether they occur on an exchange floor or "upstairs," are reportable to CAT if they are a firm bid or offer. See Securities Exchange Act Release No. 90405 (Nov. 12, 2020), 85 FR 73544, at 73546-547 (Nov. 18, 2020) ("November 2020 Exemptive Order").

11 See November 2020 Exemptive Order (granting the requested relief until July 31, 2023); Securities Exchange Act Release No. 98023 (July 28, 2023), 88 FR 51369 (Aug. 3, 2023) (the "July 2023 Exemptive Order") (extending the relief until July 31, 2026).

12 See Notice, 89 FR at 67499.

record and report to the Central Repository.[13] Specifically, proposed new Section 6.3(g) of the CAT NMS Plan would state the following:

> "Notwithstanding any other provision of SEC Rule 613 or the CAT NMS Plan, the following categories of data shall not be reportable to the Central Repository under Section 6.3(d):
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> (i) floor broker verbal announcements of firm orders on an exchange that are otherwise reported as systematized orders;
> (ii) market maker verbal announcements of firm quotes on an exchange trading floor;
> (iii) telephone discussions between an Industry Member and a client that may involve firm bid and offer communications; and
> (iv) unstructured electronic and verbal communications that are not currently captured by Industry Member order management or execution systems (e.g., electronic chats, text messages)."[14]

CAT LLC states that the Verbal Quotes Amendment is intended to have an effect similar to permanent incorporation into the CAT NMS Plan of the existing Commission-approved temporary exemptive relief within the July 2023 Exemptive Order, without the added conditions to relief.[15] CAT LLC states that the Verbal Quotes Amendment is not intended to affect activity

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13 See Notice, 89 FR at 67499.

14 See id. at 67501. CAT LLC states that the term "client" in the Verbal Quotes Amendment is intended to include both a non-Industry Member customer of the Industry Member or another Industry Member. Id. In addition, CAT LLC proposes to add references to new Section 6.3(g) to Section 6.3(d) and Section 6.4(d)(i) of the CAT NMS Plan. Specifically, CAT LLC proposes to add the parenthetical phrase "(subject to the exclusions outlined in Section 6.3(g))" to Section 6.3(d) and Section 6.4(d)(i) of the CAT NMS Plan. Id.

15 Id. The July 2023 Exemptive Order conditioned relief on the Participants providing the Commission a written status update on the reporting of these quotes and orders by July 31, 2025, including, for both verbal activity on exchange floors and upstairs activity separately, an analysis of the feasibility of traders contemporaneously recording firm bid and offer information for verbal and manual quotes and orders, and an implementation plan for the reporting of these quotes and orders. July 2023 Exemptive Order, 88 FR at 51370-71.

that is currently reported to CAT or to otherwise modify the categories in the July 2023 Exemptive Order.[16]

CAT LLC states that the Verbal Quotes Amendment is merited because of the impact on overall CAT costs of requiring reporting of the Exempt Activities.[17] CAT LLC estimates that these costs could be in the billions.[18] CAT LLC further states that the Verbal Quotes Amendment is appropriate because it is technologically infeasible to reliably, accurately, and consistently collect and report data concerning the Exempt Activities.[19]

CAT LLC also states that no technological developments have occurred that would make reporting the Exempt Activities cost-effective.[20] CAT LLC states that market participants continue to work on developing this technology, but that a number of Industry Members have conducted internal analyses on this question and concluded that there is currently no artificial intelligence software or algorithm with a feasible architecture to accurately capture and report the Exempt Activities to the CAT in an automated manner.[21] CAT LLC states that, given that the technology has not developed in the four years since the original November 2020 Exemptive Order, it is "exceedingly unlikely" that it will develop to a usable point over the next two years.[22] Moreover, because there is no existing technological solution, CAT LLC states that reporting the Exempt Activities would require substantial human intervention, which would also add

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16 See Notice, 89 FR at 67501.

17 See id.

18 See id. A letter cited by CAT LLC provides additional detail on these estimates. See Letter from Howard Meyerson, Managing Director, Financial Information Forum, to Commission at 20 (Dec. 16, 2022) ("December 2022 FIF Letter").

19 Id.

20 See Notice at 67502-03.

21 See id. (citing December 2022 FIF Letter at 5).

22 See Notice at 67502.

significantly to the costs.[23] Specifically, CAT LLC states that the only way for the Participants and Industry Members to report the Exempt Activities to the CAT would be to manually capture these events by requiring a human being to listen to every verbal interaction of every floor broker, market maker, or upstairs trader either live or from tape, and/or to sift through electronic communications to determine if and precisely when a quote was given and whether it was firm.[24] CAT LLC states that there also would be considerable costs to implement the reporting of the Exempt Activities beyond the above-described costs to maintain such reporting.[25] CAT LLC further states that reporting the Exempt Activities would also disrupt trading and reduce the use of firm quotations and orders.[26]

CAT LLC states that these significant costs "would not provide enough value from a regulatory and surveillance perspective to outweigh their substantial costs" because most of the relevant data that could be gleaned from the Exempt Activities is already gathered in some other form in CAT.[27] CAT LLC states that on all exchanges with floor trading, every order must be systematized upon receipt by the floor broker on the floor of the exchange and is reportable to the CAT.[28] CAT LLC states that an order is "systematized" when (A) the order is sent electronically to the floor broker's system at the exchange; or (B) the order is manually systematized by the floor broker upon receipt outside of the floor broker's system and prior to representation in the floor trading crowd.[29] CAT LLC states that therefore all firm bids or offers

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23 See Notice at 67502-03.

24 Id.

25 Id.

26 See Notice at 67503.

27 Id.

28 Id.

29 See Notice at 67503.

represented by a floor broker must be associated with orders that have already been systematized.[30] CAT LLC states that because the Participants require that any firm verbal interest expressed by a floor broker must be related to a CAT reportable systematized order, and any resulting trade must be reported to CAT, all verbal interest expressed by a floor broker that may be a CAT Reportable Event is already reported to CAT.[31] In addition, CAT LLC states that any cancellation or change to an order transmitted to an exchange floor broker must occur within the systematized order record.[32] CAT LLC states that there is additional information that would be associated with the Exempt Activities, but states that such additional information does not need to be captured to allow for effective surveillance and regulation of exchange floor activity.[33]

CAT LLC states therefore that the ultimate regulatory value-add of expanding the existing CAT reporting to include the Exempt Activities is minimal given the scope of the data associated with the Exempt Activities that is already reported.[34] CAT LLC further states that communications related to the Exempt Activities do not lend themselves to the types of market manipulation considered in the adoption of Rule 613 because such communications are not widely disseminated.[35] CAT LLC concludes that any small incremental value added for regulatory purposes would be significantly outweighed by costs imposed on Industry Members, their customers, and the Participants, as well as the disruption to trading on Participant trading floors.[36]

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30 Id.

31 See Notice at 67502-03.

32 Id.

33 See id.

34 See id.

35 See id.

36 Id.

IV. Summary of Comments

The Commission received one comment letter in connection with the Verbal Quotes Amendment.[37] The commenter supports the Verbal Quotes Amendment stating that: (i) automated capture of the Exempt Activities is not possible based on current technology; (ii) the costs for manually capturing, interpreting and reporting the Exempt Activities will be significant;[38] (iii) the CAT NMS Plan and the Commission's approval order do not address these significant costs; (iv) Industry Members will curtail their current verbal activity in the absence of relief, which could result in reduced execution quality for customer orders and reduced market liquidity; (v) prices communicated in upstairs one-to-one unstructured communications are not firm because they are not binding on the communicating party and always require a further affirmative action by the communicating party; (vi) that the regulatory value of the data is not clear; and (vii) the Exemptive Activities could be defined as "pre-order communications," but are not orders under Commission Rule 613 because they cannot result in a trade execution unless an order is transmitted and received subsequent to such a pre-order communication and prior to the time of trade execution"[39]

FIF states that if the Commission does not provide permanent relief for reporting the Exempt Activities, it would be necessary for the Commission to: (i) provide support for this position based on Commission precedent;[40] (ii) publicly communicate its reasoning in writing;

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37 See Letter from Howard Meyerson, Managing Director, Financial Information Forum ("FIF") to Secretary, Commission, dated September 9, 2024, available at https://www.sec.gov/comments/4-698/4698-518035-1490942.pdf ("September 2024 FIF Letter"), enclosing December 2022 FIF Letter.

38 FIF states that the annual cost to report the Exempt Activities would be in excess of $4.4 billion, subject to an increase for inflation in the period of time following the submission of the December 2022 FIF Letter. September 2024 FIF Letter at 3.

39 September 2024 FIF Letter at 2-4.

40 FIF states that unstructured verbal and electronic upstairs activities are not reportable to CAT under Rule 613 because they represent indications of interest—not orders. December 2022 FIF Letter at 11-12. CAT

(iii) clearly explain the conditions under which specific verbal activity would be or would not be reportable to CAT; and (iv) ensure that the CAT system and CAT documentation are updated to clearly describe the required reporting (including how specific fields, such as duration, should be reported).[41] FIF states that the Commission would need to complete these four steps at least three years prior to any implementation of CAT reporting for the Exempt Activities.[42]

V. Proceedings to Determine Whether to Approve or Disapprove the Verbal Quotes Amendment and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Rule 608(b)(2)(i) of Regulation NMS,[43] and Rules 700 and 701 of the Commission's Rules of Practice,[44] to determine whether to disapprove the Verbal Quotes Amendment or to approve the Verbal Quotes Amendment with any changes or subject to any conditions the Commission deems necessary or appropriate. The Commission is instituting proceedings to have sufficient time to consider the issues raised by the proposal, including comments received. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described below, the Commission seeks and encourages interested persons to provide comment on the Verbal Quotes Amendment.

Rule 608(b)(2) of Regulation NMS provides that the Commission "shall approve a national market system plan or proposed amendment to an effective national market system plan, with such changes or subject to such conditions as the Commission may deem necessary or

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LLC states that the analysis in the December 2022 FIF Letter explaining why unstructured verbal and electronic upstairs activities are not reportable to CAT under Rule 613 (including the challenges that would be associated with reporting those activities) applies equally to communications on exchange trading floors. See Notice, supra note 5, at 67499.

41 September 2024 FIF Letter at 4.

42 Id.

43 17 CFR 242.608(b)(2)(i).

44 17 CFR 201.700; 17 CFR 201.701.

appropriate, if it finds that such plan or amendment is necessary or appropriate in the public interest, for the protection of investors and the maintenance of fair and orderly markets, to remove impediments to, and perfect the mechanisms of, a national market system, or otherwise in furtherance of the purposes of the [Exchange] Act."[45] Rule 608(b)(2) further provides that the Commission shall disapprove a national market system plan or proposed amendment if it does not make such a finding.[46] In the Notice, the Commission sought comment on the proposed amendment, including whether the proposed amendment is consistent with the Exchange Act.[47] In this order, pursuant to Rule 608(b)(2)(i) of Regulation NMS,[48] the Commission is providing notice of the grounds for disapproval under consideration:

- whether, consistent with Rule 608 of Regulation NMS, the Participants have demonstrated that the Verbal Quotes Amendment is necessary or appropriate in the public interest, for the protection of investors and the maintenance of fair and orderly markets, to remove impediments to, and perfect the mechanisms of, a national market system, or otherwise in furtherance of the purposes of the Exchange Act;[49] and
- whether, and if so how, the Verbal Quotes Amendment would affect efficiency, competition or capital formation.

Under the Commission's Rules of Practice, the "burden to demonstrate that a NMS plan filing is consistent with the Exchange Act and the rules and regulations issued thereunder … is

45 17 CFR 242.608(b)(2).

46 Id.

47 See Notice at 67504.

48 17 CFR 242.608(b)(2)(i).

49 17 CFR 242.608(b)(2).

on the plan participants that filed the NMS plan filing."[50] The description of the NMS plan filing, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding, and "[a] mere assertion that the NMS plan filing is consistent with those requirements is not sufficient."[51] Any failure of the plan participants that filed the NMS plan filing to provide such detail and specificity may result in the Commission not having a sufficient basis to make an affirmative finding that the NMS plan filing is consistent with the Act and the applicable rules and regulations thereunder.[52]

VI. Commission's Solicitation of Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the Verbal Quotes Amendment. In particular, the Commission invites the written views of interested persons concerning whether the Verbal Quotes Amendment is consistent with the Exchange Act, the rules and regulations thereunder, or any other provisions of the CAT NMS Plan. The Commission asks that commenters address the sufficiency and merit of the Participants' statements in support of the Verbal Quotes Amendment, and to consider the impact of the Verbal Quotes Amendment on efficiency, competition, and capital formation, in addition to any other comments they may wish to submit about the Verbal Quotes Amendment.

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50 17 CFR 201.701(b)(3)(ii).

51 Id.

52 Id.

Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 608(b)(2)(i) of Regulation NMS, any request for an opportunity to make an oral presentation.

Interested persons are invited to submit written data, views, and arguments regarding whether the Verbal Quotes Amendment should be approved or disapproved by [insert date 21 days after publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days after publication in the Federal Register]. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number 4-698 on the subject line.

Paper comments:

- Send paper comments in triplicate to: Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number 4-698 (CAT Verbal Quotes Amendment). This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (https://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the Verbal Quotes Amendment that are filed with the Commission, and all written communications relating to the Verbal Quotes Amendment between the Commission and any person, other than

those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the Participants' principal offices. Do not include personal identifiable information in submissions; you should submit only information that you wish to make available publicly. We may redact in part or withhold entirely from publication submitted material that is obscene or subject to copyright protection. All submissions should refer to File Number 4-698 (CAT Verbal Quotes Amendment) and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[53]

Sherry R. Haywood,

Assistant Secretary.

[53] 17 CFR 200.30-3(a)(85).