

FINANCIAL INFORMATION FORUM

February 3, 2023

By electronic mail to rule-comments@sec.gov

Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
Attn: Secretary

Re: File Number SR-FINRA-2022-031: Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Adopt FINRA Rules 6151 (Disclosure of Order Routing Information for NMS Securities) and 6470 (Disclosure of Order Routing Information for OTC Equity Securities)

Dear Secretary,

On December 20, 2020, the Financial Information Forum (“FIF”)¹ submitted a comment letter on SR-FINRA-2022-031 filed by the Financial Industry Regulatory Authority (“FINRA”) with the Securities and Exchange Commission (the “Commission”)² and the Commission’s associated Notice of Filing.³ The filing by FINRA (the “FINRA Rule Filing”) proposes to adopt FINRA Rule 6470 (Disclosure of Order Routing Information for OTC Equity Securities) to require FINRA member firms to publish order routing reports for orders in OTC Equity Securities (as defined in the FINRA Rule Filing). FIF is submitting this supplemental comment letter, which relates specifically to reporting for trade messages sent through, and quotes posted on, an inter-dealer quotation system (“IDQS”) for OTC Equity Securities. This letter discusses trading workflows that are available through the OTC Link ATS, which is an IDQS, and recommends how the venue for execution should be reported for these workflows in the routing reports proposed in the FINRA Rule Filing.

¹ FIF (www.fif.com) was formed in 1996 to provide a centralized source of information on the implementation issues that impact the securities industry across the order lifecycle. Our participants include broker-dealers, exchanges, back office service bureaus, and market data, regulatory reporting and other technology vendors in the securities industry. Through topic-oriented working groups, FIF participants focus on critical issues and productive solutions to technology developments, regulatory initiatives, and other industry changes.

² Financial Industry Regulatory Authority, “Proposed Rule Change to Adopt FINRA Rules 6151 (Disclosure of Order Routing Information for NMS Securities) and 6470 (Disclosure of Order Routing Information for OTC Equity Securities),” SR-FINRA-2022-031 (Nov. 16, 2022), available at <https://www.finra.org/sites/default/files/2022-05/SR-FINRA-2022-013.pdf>.

³ Securities Exchange Act Release No. 96415 (Nov. 30, 2022), 87 FR 74762 (Dec. 6, 2022).

All steps in the workflows below involve a single symbol. IB1 refers to an introducing broker. MM1, MM2 and MM3 represent three market makers. In each workflow below, a customer of IB1 submits a buy order to IB1 and one or more market makers are posting an offer to sell on the IDQS. The offer to sell can be a proprietary quote of the market maker or the representation of a customer order to sell as a quote on the IDQS, as indicated in the specific workflow below.

Workflow 1: Market maker executes against order from customer of introducing broker

Steps: A market maker (MM1) posts a proprietary quote in the IDQS; an introducing broker (IB1) receives a buy order from a customer; IB1, acting as agent, directs a trade message via the IDQS to lift (execute against) MM1’s quoted offer; the IDQS delivers the trade message to MM1; MM1 executes the order.

Proposed reporting: FIF members propose that IB1 report the IDQS as the venue for execution. FIF members have three distinct reasons for this recommendation. First, this is how Rule 606 reporting occurs for an order-driven ATS and how OTC route reporting would occur for an order-driven ATS. Second, this reporting is consistent with how firms report this activity to the Consolidated Audit Trail (“CAT”).⁴ Third, requiring IB1 to report the market maker as the venue for execution would create complications for the MAX order workflow described below and potentially other IDQS workflows.

Workflow 2: Introducing broker executes customer order against counter from market maker

Steps: MM1 posts a proprietary quote in the IDQS; IB1 receives a buy order from a customer; via the IDQS, IB1, acting as agent, directs a trade message to lift MM1’s quoted offer; the IDQS delivers the trade message to MM1; via the IDQS, MM1 directs a trade message directed to IB1 (this is a counter-offer by MM1); the IDQS delivers the trade message to IB1; IB1 agrees to the counter, resulting in a trade execution.

Proposed reporting: FIF members propose that IB1 report the IDQS as the venue for execution even though IB1 is the executing broker for this trade. Reporting should be based on the initial routing action taken by IB1 which, in this case, was directing a trade message to MM1 via the IDQS.

Workflow 3: Three market makers execute against order from customer of introducing broker

Steps: Each of three market makers (MM1, MM2 and MM3) posts a proprietary quote in the IDQS; the offer-side quantity of each quote is 100 shares; IB1 receives a buy order from a customer; IB1, acting as agent, directs three separate trade messages via the IDQS to lift the quoted offers of MM1, MM2 and

⁴ See, for example, CAT Industry Member Reporting Scenarios, Version 4.10 (Oct. 21, 2022), available at https://catnmsplan.com/sites/default/files/2022-10/10.21.22_Industry_Member_Tech_Specs_Reporting_Scenarios_v4.10_CLEAN.pdf (“CAT Transaction Reporting Scenarios”), at 232-238. In CAT, IB1 is required to report an order route to the IDQS, and the IDQS is required to report an order route to MM1. In its order route report, IB1 is required to identify MM1 as part of a handling instructions value.

MM3; the IDQS delivers each trade message to the applicable market maker; each market maker executes against the customer order.

Proposed reporting: FIF members propose that IB1 report the IDQS as the venue for execution for three distinct routes.

Workflow 4: Market makers executes against MAX order from introducing broker

Steps: Each of three market makers (MM1, MM2 and MM3) posts a proprietary quote in the IDQS; the offer-side quantity of each quote is 200 shares; IB1 receives a buy order from a customer; IB1, acting as agent, directs a MAX order for 400 shares to lift the quoted offers of MM1, MM2 and MM3; with a MAX order, IB1 is willing to execute against any of the three market makers quotes, but the maximum total quantity that IB1 can execute is 400 shares; the IDQS delivers the MAX order trade message to each market maker; MM1 executes against the customer order for 200 shares; MM2 executes against the customer order for 200 shares.

Proposed reporting: FIF members propose that IB1 report the IDQS as the venue for execution. This MAX order scenario demonstrates why reporting the market maker as the venue for execution would be problematic as IB1 would need to report three separate routes when in fact IB1 only sent one order route. In a more extreme case where IB1's customer order is for 100 shares and there are 10 market makers with posted quotes, IB1 would need to report ten separate routes even though IB1 only sent one order route and could only execute against one market maker. The reporting proposed by FIF members for this workflow is consistent with CAT.⁵

Workflow 5: Market maker executes customer order against order from customer of introducing broker

Steps: MM1 receives a sell order from a customer; MM1 represents the customer order as an offer-side quote on the IDQS; IB1 receives a buy order from a customer; via the IDQS, IB1, acting as agent, directs a trade message to lift MM1's quoted offer; the IDQS delivers the trade message to MM1; MM1 executes the order from IB1 against the order from MM1's customer.

Proposed reporting: FIF members propose that IB1 report the IDQS as the venue for execution. Workflow 5 is the same as Workflow 1 from the perspective of IB1. FIF members propose that MM1's representation of its customer's quote on the IDQS should not be reported as an order route to the IDQS. This posting is not an order route because no contra-party can execute this posted quote. Instead, for an execution to occur, a contra-party is required to direct a trade message to the IDQS to be delivered by the IDQS to MM1, and MM1 can then execute its customer order against the order from the contra-party. CAT requires that this activity by MM1 be reported as the route of a quote and not as an order route. In CAT, it is IB1 (and not MM1) that is routing an order.⁶ Since MM1 is not routing an order to the IDQS, the only alternative is for MM1 to report this event as a route to itself. This type of

⁵ Id. at 280-291.

⁶ Id. at 232-238.

reporting is discussed in FAQ 2.02 of the Commission’s Rule 606 FAQs in relation to Rule 606(b)(3) reporting.⁷

Workflow 6: Introducing broker executes customer order against counter from market maker representing customer order

Steps: MM1 receives a sell order from a customer; MM1 represents the customer order as an offer-side quote on the IDQS; IB1 receives a buy order from a customer; via the IDQS, IB1, acting as agent, directs a trade message to lift MM1’s quoted offer; the IDQS delivers the trade message to MM1; via the IDQS, MM1 directs a trade message directed to IB1 (this is a counter-offer by MM1); the IDQS delivers the trade message to IB1; IB1 agrees to the counter, resulting in a trade execution

Proposed reporting: As discussed in Workflow 2 above, FIF members propose that IB1 report the IDQS as the venue for execution even though IB1 is the executing firm for this trade. In this scenario, MM1 also should report the route of a customer order to the IDQS. This proposed reporting would be consistent with CAT.⁸

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The foregoing is not intended to represent all potential IDQS scenarios, but addressing the workflows above will greatly assist with addressing other workflows that arise.

FIF appreciates the opportunity to submit this supplemental comment letter on SR-FINRA-2022-031. If you would like clarification on any of the items discussed in this letter or would like to discuss further, please contact me at howard.meyerson@fif.com.

Very truly yours,

/s/ Howard Meyerson

Howard Meyerson
Managing Director, Financial Information Forum

⁷ FAQ 2.02 provides: “If the broker-dealer executes orders in its ATS and also executes orders elsewhere internally, such as (but not limited to) in a single dealer execution platform or an internal execution desk for crossing customer orders, the ATS must be reported as an execution venue for the executions that occur therein and the broker-dealer entity must be reported separately as an execution venue for the executions that occur internally at the broker-dealer but not in the ATS.” Securities and Exchange Commission, “Responses to Frequently Asked Questions Concerning Rule 606 of Regulation NMS,” available at <https://www.sec.gov/tm/faq-rule-606-regulation-nms>.

⁸ CAT Transaction Reporting Scenarios, at 238-248.