

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>11</sup>

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*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-70158; File No. SR-BX-2013-047]

### Self-Regulatory Organizations; NASDAQ OMX BX, Inc.; Notice of Filing of a Proposed Rule Change To Assume Operational Responsibility for Certain Surveillance Activity Currently Performed by FINRA Under the Exchange's Authority and Supervision

August 12, 2013.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 31, 2013 NASDAQ OMX BX, Inc. ("BX" or "Exchange"), filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange is proposing to assume operational responsibility for certain surveillance activity currently performed by the Financial Industry Regulatory Authority ("FINRA") under the Exchange's authority and supervision.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

#### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

##### 1. Purpose

Section 6 of the Act requires that national securities exchanges enforce their members' compliance with federal securities laws and rules as well as the exchanges' own rules.<sup>3</sup> As a self-regulatory organization ("SRO"), BX must conduct surveillance of trading on the Exchange as part of a comprehensive regulatory program that also includes member examinations and investigation and prosecution of suspicious activity. Since its acquisition by The NASDAQ OMX Group, Inc., BX has contracted with FINRA through various regulatory services agreements to perform certain surveillance and other regulatory functions on its behalf. However, as the Commission has made clear with respect to BX's affiliate, the NASDAQ Stock Exchange LLC ("NASDAQ"), "the Nasdaq Exchange bears the responsibility for self-regulatory conduct and primary liability for self-regulatory failures, not the SRO retained to perform regulatory functions on the Exchange's behalf."<sup>4</sup>

Notwithstanding its use of FINRA, the Exchange has also retained operational responsibility for a number of surveillance and other regulatory functions including real-time surveillance, qualification of companies listed on NASDAQ and most surveillance related to its affiliated options markets. Historically BX retained operational responsibility in areas where BX's expertise regarding its own markets, technology and listed companies enhanced regulation. For the reasons outlined below, BX now proposes to reallocate operational responsibility from FINRA to BX Regulation for a limited number of equities surveillance patterns and related review functions focused on:

- Manipulation patterns that monitor solely BX activity, including patterns that monitor activity that might impact the opening and closing cross process on NASDAQ and compliance with minimum bid listing requirements by companies listed on NASDAQ, and
- Monitoring of compliance by NASDAQ member firms with elements of Regulation M and NASDAQ Rule 4619 compliance, which will include data from BX.

FINRA operates a full suite of equities surveillance patterns on behalf of BX

that covers many types of potential misconduct. In recent years FINRA, with BX's oversight and approval, modified a number of these BX patterns to incorporate data from markets operated by NYSE Euronext. BX plans to continue to participate in this cross-market surveillance performed by FINRA, some of which focuses on identifying similar violative activity, which will not be impacted by this proposal. However, a limited number of FINRA's patterns only review BX market data and detect conduct occurring only on the Exchange. These patterns incorporate unique elements of BX's market structure and focus on trading activity in the BX that might impact the opening and closing cross process on NASDAQ,<sup>5</sup> as well as activity on BX that might impact minimum bid listing standards for securities listed on NASDAQ, an area already regulated by NASDAQ. An additional pattern monitors attempts to manipulate BX using small orders to advantage larger orders placed on the opposite side of the BX market at an improved price (often referred to as "odd lot manipulation" or "mini-manipulation").

BX believes that its expertise in its own market structure coupled with its continued monitoring of these activities in real-time will enable it to enhance existing patterns to better detect improper activity on its market. In addition, these patterns, the underlying rules, and analytical requirements are similar to patterns BX regulatory personnel already operate for affiliated options markets. For example, BX regulatory personnel routinely monitor affiliated options markets for market closing activity and other patterns designed to detect various types of price influence.

In a separate filing NASDAQ also proposes to assume operational responsibility for real-time monitoring of compliance by market makers that are members of an underwriting syndicate with the quoting and trading restrictions in Rules 101 and 103 under the Act<sup>6</sup> and NASDAQ Rule 4619.<sup>7</sup> The activity is monitored in real-time and firms are called upon receipt of regulatory alerts to prevent potential or further violations. MarketWatch already has responsibility for monitoring similar activity on BX by market makers participating in secondary offerings, although this surveillance is not

<sup>5</sup> FINRA runs additional patterns looking for manipulation of trading on BX as part of its cross market manipulation patterns.

<sup>6</sup> 17 CFR 242.101 and 17 CFR 242.103.

<sup>7</sup> SR-NASDAQ-2013-102.

<sup>11</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78f.

<sup>4</sup> Securities Exchange Act Release No. 53128 at 28 (January 13, 2006), 71 FR 3550, 3556 (January 23, 2006).

currently active as BX does not have any registered market makers. However, the pattern run for NASDAQ would incorporate BX data, thereby adding to the efficacy of the NASDAQ pattern.

BX plans to operate the surveillance patterns referenced above in the SMARTS surveillance system. SMARTS is a state-of-the-art surveillance platform used in 26 markets and by 9 government regulators around the world. BX plans to use SMARTS for both real-time monitoring and the limited non-real time surveillance covered by this proposal. Running the patterns in real-time will permit an expedited review of critical alerts that previously would not have been completed the same day. It will now be easier to quickly compare unusual activity noted as part of BX's operations monitoring of market activity with surveillance alerts. BX anticipates being able to refer a broader cross section of problematic activity to FINRA for expedited review than was previously the case.

BX Regulation intends to leverage its existing staff of experienced analysts, lawyers, programmers and market structure experts to perform the new functions covered by this proposal. This group is working with BX's regulatory technology group to develop and test the surveillance patterns that will run in the SMARTS system. This distribution of responsibilities was the result of detailed discussions between BX and FINRA that focused on reallocating responsibilities based on the core competencies of each organization. BX Regulation and FINRA have developed comprehensive plans covering the transition and the groups have met regularly over more than nine months to ensure a smooth transition of the work and prevent any gaps in surveillance coverage. BX and FINRA anticipate a phased transition of patterns, with BX formally relieving FINRA of operational responsibility for each pattern once testing, training, procedures and other preparations are completed. FINRA will retire each pattern once relieved of responsibility. After the transition, BX Regulation will review surveillance alerts and refer potentially violative conduct to FINRA using existing processes and systems. FINRA will continue to have operational responsibility for the vast majority of surveillances involving BX's equity market as well as examination and enforcement matters, subject to BX's supervision and ultimate responsibility.

The provisions of BX Rule 0150 require that BX obtain Commission approval if regulatory functions subject to the regulatory services agreement in effect at the time BX first executed the

agreement in 2008 are no longer performed by FINRA or another independent self-regulatory organization. For the reasons stated above, BX believes that the reassignment of operational responsibility for a limited number of equities surveillance patterns will further its regulatory program and benefit investors and the markets. Commission approval of the proposal would allow NASDAQ OMX to better leverage data and systems across its three equities exchanges, including NASDAQ OMX PHLX, an affiliate of BX, that does not have an equivalent to Rule 0150 requiring Commission approval for this reallocation.

In addition, BX notes that its proposal is consistent with, but more limited than, surveillance work performed by other national securities exchanges. The SEC has previously approved several applications for registration as national securities exchanges in which the SRO proposed to perform its own surveillance function. For example, the SEC approved BATS Exchange's application where BATS performed most surveillance for its markets, finding in its approval order that it was consistent with the Act for BATS Exchange to contract with FINRA to perform regulatory functions limited to "examination, enforcement, and disciplinary functions."<sup>8</sup> Similarly, BX understands that Miami International Securities Exchange ("MIAX") performs the majority of its surveillance operations in-house. This is consistent with MIAX's Form 1, which states that the new exchange entered into a regulatory services agreement with CBOE that is limited to "conducting *certain* market surveillances" in addition to other regulatory work.<sup>9</sup>

## 2. Statutory Basis

BX believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,<sup>10</sup> in general and with Sections 6(b)(5) of the Act,<sup>11</sup> in particular in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and

open market and a national market system, and, in general, to protect investors and the public interest. The Exchange believes that this proposal is in keeping with those principles by leveraging the SMARTS technology system that has the ability to operate in real-time and, as a consequence, will permit BX to react more quickly to potential manipulation in the applicable regulatory areas covered by this proposal. The surveillance patterns to be reallocated to BX involve solely activity on BX's own market. BX believes that its expertise in its own market structure, coupled with its existing monitoring of these activities in real-time, will enable it to enhance current patterns to better detect improper activity on its market. In addition, BX will be able to leverage the knowledge and the regulatory staff that already perform similar work for affiliated options markets.

BX will continue to refer potentially violative conduct to FINRA for further review. Moreover, FINRA will continue to perform the vast majority of surveillance activity for BX's equities market, in many cases using patterns that incorporate data from other market centers. FINRA will also perform examination and enforcement work, subject to BX's supervision and ultimate responsibility.

BX also believes the proposal is consistent with the Act because, as the Commission has made clear on many occasions, an SRO cannot delegate its ultimate responsibility for surveillance in the absence of an SEC-approved agreement under Section 17(d)(2) of the Act, and therefore must remain involved and responsible for its regulatory program. In addition, BX notes that its proposal is consistent with, but more limited than, surveillance work performed by other national securities exchanges. As noted above, the SEC has previously approved several applications for registration as national securities exchanges in which the SRO proposed to perform its own surveillance function.<sup>12</sup> BX believes it would therefore be consistent with the Act for BX to perform a much more limited surveillance function than has been approved for other exchanges and, in fact, more limited than surveillance functions BX already performs for non-cash equities markets.

<sup>8</sup> Securities Exchange Act Release No. 34-58375 (August 18, 2008), 73 FR 49498 (August 21, 2008).

<sup>9</sup> Securities Exchange Act Release No. 34-68341 (December 3, 2012), 77 FR 73065 (December 7, 2012) (emphasis added).

<sup>10</sup> 15 U.S.C. 78f.

<sup>11</sup> 15 U.S.C. 78f(b)(5).

<sup>12</sup> See *supra* notes 8 and 9, and accompanying text discussing the surveillance work by BATS and MIAX.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

Written comments were neither solicited nor received.

### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission shall: (a) By order approve or disapprove such proposed rule change, or (b) institute proceedings to determine whether the proposed rule change should be disapproved.

### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. 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 email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BX-2013-047 on the subject line.

#### *Paper Comments*

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

All submissions should refer to File Number SR-BX-2013-047. This file number should be included on the subject line if email 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 Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule

change that are filed with the Commission, and all written communications relating to the proposed rule change 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 Web site 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 such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-BX-2013-047, and should be submitted on or before September 6, 2013.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-70162; File No. SR-EDGX-2013-31]

### **Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 2.5 To Outline the Continuing Education Requirements for Series 56 Licensees and Its Fee Schedule To Include Fees for the Series 56 Examination and Its Related Continuing Education Requirements**

August 12, 2013.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 6, 2013, EDGX Exchange, Inc. (the "Exchange" or "EDGX") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which items have been prepared by the Exchange. The Commission is publishing this notice to solicit

comments on the proposed rule change from interested persons.

### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The Exchange proposes to amend: (1) Exchange Rule 2.5 to: (i) outline the continuing education requirements for Authorized Traders<sup>3</sup> of Members<sup>4</sup> registered solely as Proprietary Traders<sup>5</sup> by having successfully completed the Proprietary Trader Qualification Examination ("Series 56"); and (ii) make a clarifying change to the Interpretation and Policy .06; and (2) the fees and rebates applicable to Members of the Exchange pursuant to EDGX Rule 15.1(a) and (c) ("Fee Schedule") to include fees for the Series 56 examination and its related continuing education requirements. All of the changes described herein are applicable to EDGX Members. The text of the proposed rule change is available on the Exchange's Internet Web site at [www.directedge.com](http://www.directedge.com), at the Exchange's principal office, and at the Public Reference Room of the Commission.

### **II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in sections A, B and C below, of the most significant aspects of such statements.

#### *A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change*

##### **1. Purpose**

The Exchange proposes to amend: (1) Rule 2.5 to: (i) outline the continuing

<sup>3</sup> "Authorized Trader" is defined as "a person who may submit orders (or who supervises a routing engine that may automatically submit orders) to the Exchange's trading facilities on behalf of his or her Member or Sponsored Participant." See Exchange Rule 1.5(c).

<sup>4</sup> "Member" is defined as "any registered broker or dealer, or any person associated with a registered broker or dealer, that has been admitted to membership in the Exchange. A Member will have the status of a "Member" of the Exchange as that term is defined in Section 3(a)(3) of the Act." See Exchange Rule 1.5(n).

<sup>5</sup> "Proprietary Trader" is defined under Interpretation and Policy .06(2) to Exchange Rule 2.5.

<sup>13</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.