

disapprove, the proposed rule change (File No. SR-EDGX-2014-05).

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁶

Kevin M. O'Neill,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72081; File No. SR-NYSEArca-2014-04]

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing of Amendment No. 1 and Order Instituting Proceedings To Determine Whether To Approve or Disapprove a Proposed Rule Change, as Modified by Amendment No. 1, To Amend NYSE Arca, Inc.'s Rules by Revising the Order of Priority of Bids and Offers When Executing Orders in Open Outcry

May 2, 2014.

I. Introduction

On January 15, 2014, NYSE Arca, Inc. ("Exchange" or "NYSE Arca") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to revise the order of priority of bids and offers when executing orders in open outcry. The proposed rule change was published for comment in the **Federal Register** on February 3, 2014.³ On March 18, 2014, the Commission extended the time period for Commission action on the proposal to May 2, 2014.⁴ The Commission received ten comment letters from seven commenters regarding the proposal,⁵ as

well as a response to the comment letters from NYSE Arca.⁶ On April 29, 2014, the Exchange filed Amendment No. 1 to the proposed rule change.⁷ The Commission is publishing this notice and order to solicit comments on the proposed rule change, as modified by Amendment No. 1, from interested persons and to institute proceedings pursuant to Section 19(b)(2)(B) of the Act⁸ to determine whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to the proposed rule change, nor does it mean that the Commission will ultimately disapprove the proposed rule change. Rather, as discussed below, the Commission seeks additional input from interested parties on the changes to the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal

NYSE Arca proposes to amend its rules governing the priority of bids and offers on its Consolidated Book by revising the order of priority in open outcry to afford priority to bids and offers represented by Market Makers⁹ and Floor Brokers¹⁰ (collectively, "Crowd Participants")¹¹ over certain equal-priced bids and offers of non-Customers¹² on the Consolidated

Book¹³ during the execution of an order in open outcry on the Floor¹⁴ of the Exchange.¹⁵

Current Rule 6.75(a) provides that any bids displayed on the Consolidated Book have priority over same-priced bids represented in open outcry. Such priority also is described in current Rule 6.47, which governs crossing orders in open outcry. Floor Broker crossing transactions, as described in Rule 6.47(a)(3), may not trade ahead of bids or offers on the Consolidated Book that are priced equal to or better than the proposed crossing price. The Exchange stated that, because of this priority afforded to the Consolidated Book, Crowd Participants who have negotiated a large transaction ultimately might not be able to participate in its execution.¹⁶

The Exchange proposed to restructure its priority rules so that bids and offers of Crowd Participants would have priority over equal-priced bids and offers of non-Customers on the Consolidated Book that are ranked in time priority behind any equal-priced Customer bids and offers on the Consolidated Book. Equal-priced Customer¹⁷ interest would continue to be afforded priority over Crowd Participants in the execution of an open outcry transaction. In addition, consistent with the existing price/time priority presently applicable to bids and offers on the Consolidated Book, equal-priced non-Customer bids and offers ranked in time priority ahead of Customer interest also would be afforded priority over Crowd Participants in the execution of an open outcry transaction. In the Exchange's view, the proposed rule change strikes the appropriate balance between encouraging larger negotiated transactions in open outcry, while at the

Regulatory Officer, Susquehanna International Group, LLP ("SIG"), dated March 14, 2014 ("SIG Letter"); and Letter from Darren Story, dated March 21, 2014 ("Story Letter II").

⁶ See Letter from Martha Redding, Chief Counsel, NYSE Euronext, dated April 4, 2014 ("NYSE Arca Response").

⁷ In Amendment No. 1, the Exchange revised the rule text for proposed Rule 6.47: (1) To clarify that Floor Brokers, when crossing two orders in open outcry, may not trade through any non-Customer bids or offers on the Consolidated Book that are priced better than the proposed execution price; and (2) to conform the term "bids and offers" to "bids or offers" in paragraphs (a) and (c) thereunder. Amendment No. 1 has been placed in the public comment file for SR-NYSEArca-2014-04 at <http://www.sec.gov/comments/sr-nysearca-2014-04/nysearca201404.shtml> (see letter from Martha Redding, Chief Counsel, NYSE Euronext, to Kevin M. O'Neill, Deputy Secretary, Commission, dated April 30, 2014) and also is available on the Exchange's Web site at http://www.nyse.com/nyse-notices/nysearca/rule-filings/pdf.action;jsessionid=FACF4F6772B1316D973F5D4E2D258ACE?file_no=SR-NYSEArca-2014-04&seqnum=2.

⁸ 15 U.S.C. 78s(b)(2)(B).

⁹ See Rule 6.32 (Market Maker Defined).

¹⁰ See Rule 6.43 (Options Floor Broker Defined).

¹¹ The term "Crowd Participants" means the Market Makers appointed to an option issue under Rule 6.35, and any Floor Brokers actively representing orders at the best bid or offer on the Exchange for a particular option series. See Rule 6.1(b)(38).

¹² A non-Customer is a market participant who does not meet the definition of Customer as defined in paragraph (c)(6) of Rule 15c3-1 under the

Securities Exchange Act of 1934, 17 CFR 240.15c3-1. See Rule 6.1(b)(29).

¹³ The Exchange also proposed to make non-substantive changes to existing rule text contained in Rules 6.47 and 6.75. See Notice, 79 FR at 6260 for a description of these non-substantive changes.

¹⁴ See Rule 1.1(i).

¹⁵ The term "Consolidated Book" means the Exchange's electronic book of limit orders for the accounts of Public Customers and broker-dealers, and Quotes with Size. See Rule 6.1(b)(37).

¹⁶ See Notice, 79 FR at 6258. The Exchange stated that Crowd Participants could negotiate a transaction with an understanding of the make-up of bids and offers on the Consolidated Book at the beginning of open outcry. However, as the trade is executed, the Consolidated Book could update with newly-arriving electronically-entered bids and offers that have priority under current Rule 6.75(a). The Exchange noted that, given the speed at which quotes can flicker in the Consolidated Book, Crowd Participants who have agreed to a transaction in open outcry do not know if they will actually participate on the trade until after execution. *Id.* at 6258-59.

¹⁷ See *supra* note 12.

⁵ 15 U.S.C. 78s(b)(2)(A)(ii)(I).

⁶ 17 CFR 200.30-3(a)(31).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 71425 (January 28, 2014), 79 FR 6258 ("Notice").

⁴ See Securities Exchange Act Release No. 71733 (March 18, 2014), 79 FR 16072 (March 24, 2014).

⁵ See Letter from Darren Story, dated January 29, 2014 ("Story Letter I"); Letter from Abraham Kohen, AK FE Consultants LLC, dated January 31, 2014 ("Kohen Letter I"); Letter from David Spack, Chief Compliance Officer, Casey Securities, LLC, dated February 3, 2014 ("Casey Letter"); Letter from Abraham Kohen, AK FE Consultants LLC, dated February 4, 2014 ("Kohen Letter II"); Letter from Angel Alvira, dated February 12, 2014 ("Alvira Letter"); Letter from Donald Hart, dated February 12, 2014 ("Hart Letter I"); Letter from Doug Patterson, Chief Compliance Officer, Cutler Group, LP, dated February 13, 2014 ("Cutler Letter"); Letter

same time protecting Customer interest on the Consolidated Book, and any interest that has time priority over such protected Customer interest.¹⁸

To effect this change to its floor priority rules, the proposal would amend the Exchange's rules as follows. As noted above, Rule 6.75(a) presently states that the highest bid shall have priority but where two or more bids for the same option contract represent the highest price and one such bid is displayed on the Consolidated Book, such bid shall have priority over any bid at the post (*i.e.*, the Trading Crowd.)¹⁹ The Exchange proposed to amend Rule 6.75(a)²⁰ by limiting the priority of bids in the Consolidated Book over bids in the Trading Crowd solely to those bids for Customers along with non-Customers that are ranked in time priority ahead of such Customers.²¹

Rule 6.76 presently governs order ranking, display and allocation of orders on the NYSE Arca Options platform ("OX system"). The Exchange proposed new paragraph (d) to Rule 6.76 that would set forth the priority of bids and offers on the Consolidated Book against orders executed through open outcry in the Trading Crowd. The proposed text provides a step-by-step description of the order of priority to be afforded bids and offers of both Customers and non-Customers on the Consolidated Book. The Exchange noted that the priority scheme described in proposed Rule 6.76(d) is consistent with the proposed changes to Rule 6.75.²²

The Exchange also proposed to include language in Rule 6.76(d)(4) that sets forth certain OTP Holder²³ obligations under Section 11(a) of the

Act.²⁴ The proposed rule text states that, notwithstanding the priority scheme set forth in proposed Rule 6.76(d)(2), an OTP Holder effecting a transaction on the Floor for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion pursuant to the "G Rule" must still yield priority to any equal-priced non-OTP Holder bids or offers on the Consolidated Book.²⁵

Rule 6.47 outlines the procedures used when a Floor Broker attempts to cross two orders in open outcry. Currently, Floor Brokers must trade against all equal-priced Customer and non-Customer bids and offers in the Consolidated Book before effecting a cross transaction in the Trading Crowd. The Exchange proposed to revise Rule 6.47 to conform the priority rules applicable to open outcry cross transactions to the proposed changes described above. Accordingly, the Exchange proposed to amend the procedures for the crossing scenarios described in Rule 6.47²⁶ by stating that Floor Brokers, when crossing two orders in open outcry, must yield priority to: (1) Any Customer bids or offers on the Consolidated Book that are priced equal to or better than the proposed execution price and to any non-Customer bids or offers on the Consolidated Book that are ranked ahead of such equal or better-priced Customer bids or offers; and (2)

to any non-Customer bids or offers on the Consolidated Book that are priced better than the proposed execution price.²⁷ The Exchange noted that Floor Brokers would be required to trade against equal and better-priced Customer bids or offers on the Consolidated Book, any better-priced bids or offers of non-Customers on the Consolidated Book and any non-Customer bids or offers that are ranked ahead of equal-priced Customer bids or offers, before attempting a cross transaction.²⁸ Consistent with proposed Rule 6.75(a), Floor Brokers would not be required to trade against equal-priced non-Customer bids and offers that are ranked behind such Customer and non-Customer bids and offers.²⁹

The Exchange stated that it would announce the implementation date of the proposed rule change by Trader Update to be published no later than 90 days following approval³⁰ and the implementation date would be no later than 90 days following the issuance of the Trader Update.

III. Comment Letters and NYSE Arca's Response

The Commission received ten comment letters from seven commenters.³¹ NYSE Arca submitted a response to the comment letters.³²

Five of the commenters, four of whom identified themselves as Crowd Participants on NYSE Arca,³³ generally were supportive of the proposal to revise the order of priority of bids and offers when executing orders in open outcry.³⁴ Four of these commenters stated a view that the proposal would allow NYSE Arca to compete with other exchanges that currently have similar priority rules.³⁵ Three of these

²⁴ Specifically, pursuant to Section 11(a)(1)(G) of the Exchange Act and Rule 11a1-1(T) thereunder (the "G Rule"), an OTP Holder may effect transactions on the Floor for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion, provided that such transaction yields priority in execution to orders for the account of persons who are not OTP Holders or associated with OTP Holders. See 15 U.S.C. 78k(a)(1)(G) and 17 CFR 11a1-1(T). The Exchange stated that the proposed rule text is based on the rules of the Chicago CBOE and NYSE MKT on behalf of NYSE Amex Options. See Notice, 79 FR at 6259 (citing CBOE Rule 6.45A(b)(i)(D) and NYSE MKT Rule 910NY).

²⁵ According to the Exchange, at this time, no OTP Holder that currently operates on the Exchange's Floor as a Floor Broker enters orders for its own account, the account of an associated person, or an account with respect to which it or an associated person has investment discretion. The Exchange stated, however, that the Financial Industry Regulatory Authority, Inc. on behalf of NYSE Regulation, Inc., monitors whether Floor Brokers comply with Section 11(a) of the Act. See *id.*

²⁶ The crossing scenarios described in Rule 6.47 are: (a) Non-Facilitation (Regular Way) Crosses; (b) Facilitation Procedures; (c) Crossing Solicited Orders; (d) Mid-Point Cross; and (e) Customer-to-Customer Cross. The Exchange did not propose any change to Rule 6.47(d) relating to Mid-Point Cross, and thus Mid-Point Cross transactions would not be affected by the proposed rule change. Telephone conversation between Glenn Gsell, Managing Director, NYSE Arca and Commission staff, dated April 23, 2014.

²⁷ See Notice, 79 FR at 6259-60 for examples illustrating the proposed priority changes as applicable for Non-Facilitation and Facilitation Crosses. See also Amendment No. 1, *supra* note 7.

²⁸ See Notice, 79 FR at 6259.

²⁹ The Exchange stated its belief that affording priority to Crowd Participants ahead of such non-Customer interest on the Consolidated Book would create an increased incentive for block-sized transactions on the Floor. See Notice, 79 FR at 6259.

³⁰ See Notice, 79 FR at 6260.

³¹ See *supra* note 5.

³² See *supra* note 6.

³³ See Casey Letter (Floor Broker); Alvira Letter (Market Maker); Hart Letters I and II (Market Maker); Cutler Letter (Crowd Participant), *supra* note 5.

³⁴ See Story Letter I; Casey Letter; Alvira Letter; Hart Letter I; Cutler Letter; Hart Letter II; and Story Letter II.

³⁵ See Casey Letter ("The Proposal would still leave Arca Crowd Participants at a slight disadvantage to crowd participants on CBOE and Amex, but would go a long way towards leveling the playing field"); Alvira Letter ("I would like to see us in a competitive balance with the AMEX who

¹⁸ See Notice, 79 FR at 6259.

¹⁹ The term "Trading Crowd" means all Market Makers who hold an appointment in the option classes at the trading post where such trading crowd is located and all Market Makers who regularly effect transactions in person for their Market Maker accounts at that trading post, but generally will consist of the individuals present at the trading post. See Rule 6.1(b)(30).

²⁰ The Exchange noted that the changes made to Rule 6.75(a) dealing with the priority of "bids" also would effect a corresponding change to the meaning of Rule 6.75(b) dealing with "offers," although there would be no change to the rule text in Rule 6.75(b). See Notice, 79 FR at 6259.

²¹ See Notice, 79 FR at 6259-60 for examples illustrating how the Exchange's priority and allocation rules would be applied under the proposed rule change.

²² See Notice, 79 FR at 6259. According to the Exchange, the inclusion of a description of open outcry priority procedures in Rule 6.76 would serve as a useful cross reference to Rule 6.75. The Exchange stated that including such a cross reference is consistent with similar rule structures by the Chicago Board Options Exchange, Inc. ("CBOE") and NYSE MKT LLC ("NYSE MKT"). See *id.* (citing CBOE Rule 6.45A(b) and NYSE MKT Rule 964NY(e)).

²³ See Rule 1.1(q).

commenters stated that the proposal would allow Crowd Participants to compete with bids and offers of non-Customers on the Consolidated Book,³⁶ and two of them stated that Crowd Participants were the market participants most likely to provide services during times of market duress.³⁷ Two commenters also noted that the rule change would maintain priority for Customer orders resting on the Consolidated Book.³⁸

Two commenters stated their belief that the proposal would increase competition on the floor for orders,³⁹ and one of these commenters noted that this competition would benefit the investing public.⁴⁰ Similarly, two commenters stated their view that the proposal would improve investor executions on the floor.⁴¹ One commenter noted that the proposal

have already implemented the change”); Cutler Letter (“AMEX and CBOE currently have similar rules in place”); and Hart Letter II (“This would enable the PCX to level the rules with other exchanges”). See also SIG Letter (“the proposal at least relates in part to a legitimate competitive concern”).

³⁶ See Casey Letter (“The current market structure leaves NYSE Arca Crowd Participants and their customers at a distinct disadvantage . . . to non-customer professional traders, including High Frequency Traders”); Hart Letter I (“This rule disadvantages floor based market makers, which are the only ones providing liquidity when the markets are under duress”); and Cutler Letter (“This Proposed Rule change will level the competitive balance between floor market makers and electronic non-customer professional traders”).

³⁷ See Hart Letter I (“market makers . . . are the only ones providing liquidity when the markets are under duress”) and Story Letter II (“Perhaps one of the most compelling arguments for floor based market-makers is that they are required to stand in and make two-sided markets in volatile environments. They cannot just turn off the machines and walk away”).

³⁸ See Story Letter I (“It will allow for price discovery and improvement, but at the same time maintaining protection for customer orders resting on the order book”) and Casey Letter (“As Crowd Participants will still be required to interact with any Customer orders in the Consolidated Book, public Customers will not be adversely affected”).

³⁹ See Casey Letter (“The Proposal, by creating more uniform open outcry priority rules across floors, will increase competition for execution of these negotiated transactions”) and Story Letter II (“This filing will create an advantage for price improving CUSTOMER orders”) (emphasis in original).

⁴⁰ See Casey Letter (“Increasing competition in financial markets is nearly always beneficial for investors; the Proposal would increase competition among options floor brokers, and would ultimately benefit the investing public”).

⁴¹ See Story Letter I (“This rule change will allow market participants to IMPROVE fills for customers without creating any disadvantage for other market participants”) and Casey Letter (“The execution of sizeable negotiated transactions in listed options is an important service provided to investors almost exclusively by the few remaining options Floor Brokers. The Proposal . . . will provide investors with greater flexibility, greater access to liquidity, and lower execution costs”) (emphasis in original).

would create an advantage for price improving customers.⁴²

Two commenters expressed concerns about the proposal.⁴³ One commenter stated its view that the proposal would disenfranchise and disadvantage certain market participants, and suggested instead that the Exchange give size preference for equal bid prices.⁴⁴ The commenter believed that such preference would be a more fair way of revising the priority of bids and offers.⁴⁵ This commenter further noted that, under the Exchange’s proposal, even small bids from Crowd Participants would take priority over electronic non-Customer bids.⁴⁶ The same commenter also noted its belief that best execution is not enhanced by allowing more exchanges to disadvantage other traders.⁴⁷ The commenter suggested that, regardless of the merits of high frequency trading, there was no reason to disadvantage all non-Customers by giving priority to one class of traders that would allow them to jump ahead of the queue.⁴⁸ One commenter who supported the proposal took issue with views expressed by this commenter and noted that current NYSE Arca rules are structured so as to disadvantage on-floor market makers.⁴⁹

Another commenter also raised concerns with the proposal.⁵⁰ The commenter acknowledged that the proposal would reduce the number of instances where high-frequency, non-Customer orders arriving on to the book could cause Crowd Participants to be “scaled-back” from agreed upon negotiated amounts. The commenter acknowledged that this “scaling back” currently presented certain operational and hedging challenges to Crowd Participants.⁵¹ The commenter remarked, however, that the proposal apparently was focused on attracting block cross volume to the Exchange.⁵²

The commenter noted that when NYSE Arca uses the term “Crowd Participants,” it appears to refer to off-floor trading houses that attempt to

⁴² See Story Letter II.

⁴³ See Kohen Letter I; Kohen II; and SIG Letter.

⁴⁴ See Kohen Letter I.

⁴⁵ See Kohen Letter I.

⁴⁶ See Kohen Letter I (“otherwise Crowd Participants’ 1 contract or 100 share bid will always take priority”).

⁴⁷ See Kohen Letter II.

⁴⁸ See Kohen Letter II.

⁴⁹ See Story Letter II.

⁵⁰ See SIG Letter.

⁵¹ See SIG Letter at 1.

⁵² See SIG Letter at 1 (“This focus is made apparent by Arca when it asserts that the new rule . . . will provide greater opportunity for bids and offers of crowd participants to participate in open outcry transaction [sic] and therefore promote larger-sized negotiated transactions”).

internalize, in large part, block orders from institutional customers (*i.e.*, clean cross orders). The commenter acknowledged that this term also includes option market makers on the NYSE Arca Floor, but stated its view that the market maker participation in such orders is often minimal as a percentage of the total order size.⁵³ The commenter stated that the majority of available market maker liquidity at the Exchange is represented by a group of off-floor market maker firms that are collectively responsible for over 90% of displayed liquidity in multiply traded options, rather than on-floor market makers.⁵⁴

The commenter further stated its view that the proposal would attract more clean-cross type orders that it believes would further insulate customer interest from competition by parties other than crowd participants.⁵⁵ In its view, because such negotiations usually occur outside the view of off-floor market makers, the crosses often occur at prices that have not been sufficiently vetted by those most likely to offer price improvement.⁵⁶ Given its concerns, the commenter believed that the proposal would be detrimental to investors, as the opportunity for price improvement would be significantly diminished.⁵⁷

The commenter stated that the proposal did not provide an explanation regarding how more crowd participation in larger-sized block floor crosses would benefit customers or the market in general.⁵⁸ The commenter acknowledged that, as other floor exchanges have rules that place booked parity interest behind crowd participants, NYSE Arca’s proposal at least relates in part to a legitimate competitive concern for the Exchange.⁵⁹

⁵³ See SIG Letter at 2.

⁵⁴ See SIG Letter at 2. The commenter remarked that, due to the off-floor market makers, electronic crossing systems for block sized orders generally have shown to be a better alternative to floor crosses, at least on a transparency and price competition basis. *Id.*

⁵⁵ See SIG Letter at 2.

⁵⁶ See SIG Letter at 2. The commenter also noted that it had submitted a Petition for Rulemaking filed with the Commission in April 2013. The commenter represented that, in that petition, several market making firms (including the commenter) asserted their belief that exchanges with trading floors would generate better priced executions for customers if they required crosses to be auctioned through electronic systems that included off-floor registered market makers in the respective option classes. See Petition for Rulemaking Regarding Option Floor Crosses, File No. 4-662 (April 22, 2013), available at <http://www.sec.gov/rules/petitions/2013/petn4-662.pdf>.

⁵⁷ See SIG Letter at 2-3.

⁵⁸ See SIG Letter at 3.

⁵⁹ See SIG Letter at 3 (“No doubt, Arca relies heavily on open outcry crosses for transaction volume. And, no doubt, the more often that high-

However, the commenter stated that it was important that exchanges give sufficient reason why a proposed rule is not injurious to customers or the market in general, and that the Exchange's proposal fails to give such reasons, perhaps, as the commenter opined, because there were none to give.⁶⁰ The commenter requested that the Commission establish the reasoning behind the Exchange's desire to increase block-cross volume and the reasons, if any, for NYSE Arca's belief that more (and cleaner) block floor crosses were good for investors.⁶¹

One commenter who supported the proposal raised issues with the arguments made by the commenter who expressed several concerns regarding the proposal.⁶² The commenter who supported the proposal stated that the other commenter's concerns were misguided and unfounded because the proposal would allow for price improvement on any size order, whether large or not. The commenter who supported the proposal also noted the proposal would allow large market-making groups like that commenter to continue to provide inside markets and actually trade at those prices on NYSE Arca.⁶³ The commenter who supported the proposal disagreed with the suggestion that the proposal was necessarily about attracting clean-crosses outside the view of off-floor market makers, and stated its belief that the rule was designed to provide opportunity to improve markets.⁶⁴

NYSE Arca provided a response letter addressing issues raised by the commenters.⁶⁵ NYSE Arca emphasized that the proposal would align the rules of the Exchange with other U.S. options exchange trading floors, but with a unique caveat that any non-Customer electronic interest with time priority over a Customer order in the Book also would maintain priority over floor participants.⁶⁶

In response to one commenter's suggestion that the Exchange adopt a pure size priority model,⁶⁷ NYSE Arca stated that a wholesale restructuring of its priority model was beyond the scope of the current proposal.⁶⁸ NYSE Arca

further noted its view that such a model would unduly disadvantage small size retail customer orders by allowing later-arriving professional participants willing to trade a larger quantity to be accorded priority.⁶⁹

In response to one commenter who expressed several concerns regarding the proposal, NYSE Arca stated that the concerns about the practice of crossing institutional orders without electronic participants providing price improvement was unrelated to the proposal to allocate priority among participants at the same price.⁷⁰ NYSE Arca noted that its rules would continue to give priority to participants who display an improved price.⁷¹

NYSE Arca disagreed with that commenter's suggestion that the proposal would attract more clean-cross type orders, noting that the proposal was intended to promote liquidity and price discovery, and stated that nothing would "insulate customer interest from competition by parties other than crowd participants."⁷² NYSE Arca stated that the proposal is intended to promote liquidity and price discovery on the Exchange by adopting a priority structure that would be similar to, but more favorable for electronic non-Customer participants than, the priority structure that exists on other U.S. options trading floors.⁷³ The Exchange pointed out that the execution price would have to be equal to or better than the NBBO and that Crowd Participants would have to yield to superior electronic bids or offers.⁷⁴ NYSE Arca stated further that the proposal would not reduce the ability or incentive for any participant to improve its displayed quote electronically, as the proposal only would impact the allocation of orders among multiple participants at the same price.⁷⁵

In response to the commenter's request that the Exchange explain why more (and cleaner) block floor crosses are good for investors, the Exchange noted its view that institutional trading desks provide a valuable service by providing liquidity to their customers for block-size orders.⁷⁶ The Exchange stated, however, that it did not believe that the total level of larger-size block floor crosses in the industry would increase as a result of its proposal.⁷⁷ The Exchange noted that other trading floors

currently execute existing institutional block cross volume, and the Exchange's goal was to offer an alternative venue for such executions.⁷⁸

IV. Proceedings To Determine Whether To Disapprove SR-NYSEArca-2014-04 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act⁷⁹ to determine whether the proposed rule change should be approved or disapproved.⁸⁰ Institution of such proceedings is appropriate at this time in view of the legal and policy issues that are raised by the proposal and are discussed below. As noted above, institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described in greater detail below, the Commission seeks and encourages interested persons to comment on the proposal, as modified by Amendment No. 1, and provide the Commission with additional comment to inform the Commission's analysis whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1.

Pursuant to Section 19(b)(2)(B) of the Act, the Commission is providing notice of the grounds for disapproval under consideration. In particular, Section 6(b)(5) of the Act⁸¹ requires that the rules of an exchange be designed, among other things, to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. In addition, Section 6(b)(8) of the Act⁸² requires that rules of an exchange do not impose any burden on competition not

⁷⁸ See NYSE Arca Response Letter at 3. The Exchange also provided examples where a firm looking to facilitate its customer order might choose to send the order to an exchange other than NYSE Arca under the Exchange's current priority rules.

⁷⁹ 15 U.S.C. 78s(b)(2)(B).

⁸⁰ Section 19(b)(2)(B) of the Act provides that proceedings to determine whether to disapprove a proposed rule change must be concluded within 180 days of the date of publication of notice of the filing of the proposed rule change. The time for conclusion of the proceedings may be extended for up to an additional 60 days if the Commission finds good cause for such extension and publishes its reasons for so finding or if the self-regulatory organization consents to the extension.

⁸¹ 15 U.S.C. 78f(b)(5).

⁸² 15 U.S.C. 78f(b)(8).

frequency professional booked orders break-up "matched" floor crosses, the more likely it becomes that off-floor facilitating firms will send their orders to other exchanges to be crossed").

⁶⁰ See SIG Letter at 3.

⁶¹ See SIG Letter at 3.

⁶² See Story Letter II.

⁶³ See Story Letter II.

⁶⁴ See Story Letter II.

⁶⁵ See NYSE Arca Response Letter.

⁶⁶ See NYSE Arca Response Letter at 1-4.

⁶⁷ See Kohen Letters I and II.

⁶⁸ See NYSE Arca Response Letter at 2.

⁶⁹ See NYSE Arca Response Letter at 2.

⁷⁰ See NYSE Arca Response Letter at 2.

⁷¹ See NYSE Arca Response Letter at 2.

⁷² See NYSE Arca Response Letter at 2-3.

⁷³ See NYSE Arca Response Letter at 3.

⁷⁴ See NYSE Arca Response Letter at 3.

⁷⁵ See NYSE Arca Response Letter at 3.

⁷⁶ See NYSE Arca Response Letter at 3.

⁷⁷ See NYSE Arca Response Letter at 3.

necessary or appropriate in furtherance of the Act.

NYSE Arca's proposal would revise the order of priority of bids and offers during the execution of orders in open outcry on NYSE Arca's Floor. The Exchange proposed to restructure its priority rules so that bids and offers of Crowd Participants would have priority over equal-priced bids and offers of Customer bids and offers on the Consolidated Book and bids and offers of non-Customers on the Consolidated Book that are ranked in time priority behind any equal-priced Customer bids and offers on the Consolidated Book. Thus, equal-priced Customer interest would continue to be afforded priority over Crowd Participants in the execution of an open outcry transaction. In addition, consistent with the existing price/time priority presently applicable to bids and offers on the Consolidated Book, equal-priced non-Customer bids and offers ranked in time priority ahead of Customer interest also would be afforded priority over Crowd Participants in the execution of an open outcry transaction.

The Exchange believes that its proposal strikes the appropriate balance between encouraging larger negotiated transactions in open outcry, while at the same time protecting Customer interest on the Consolidated Book, and any interest that has time priority over such protected Customer interest. The Exchange believes that larger-sized negotiated transactions will in turn lead to greater competition for orders, creating a more robust open outcry market and benefiting investors who choose to send orders to the Exchange. In the Exchange's view, the proposal would align its rules governing priority during open outcry transactions with the floor priority rules of other U.S. options exchanges, except that any non-Customer interest in the Consolidated Book with time priority over a booked Customer order would maintain priority over the trading crowd.

As detailed above, five commenters favored the proposal,⁸³ and two commenters expressed concerns about the proposal.⁸⁴ One of these commenters stated its view that the Exchange had not provided an explanation regarding how more crowd participation in larger-sized block floor crosses would benefit customers or the market in general.⁸⁵ This commenter stated its belief that the proposal would further insulate customer interest from competition by off-floor market makers

that primarily display their liquidity electronically, who the commenter believes would be most likely to offer price improvement. The other commenter who questioned the proposal believed that the proposal could disenfranchise and disadvantage certain market participants and suggest that size preference be given for equal bid prices. The Exchange in response stated that the first commenter's concerns were entirely unrelated to the proposal and that the proposal was instead intended to promote liquidity and price discovery, and that the second commenter's suggestion on size priority was beyond the scope of the proposal.

The Commission believes that questions are raised as to whether NYSE Arca's proposal is consistent with: (1) The requirements of Section 6(b)(5) of the Act, including whether the Exchange's proposed revisions to its rules regarding the order of priority in open outcry are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers; and (2) the requirements of Section 6(b)(8) of the Act, including whether the Exchange's proposed revisions to its rules regarding the order or priority in open outcry impose any unnecessary or inappropriate burden on competition. The Commission believes that the issues raised by the proposed rule change can benefit from additional consideration and evaluation.

V. Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data and arguments with respect to the concerns identified above, as well as any others they may have with the proposal, as modified by Amendment No. 1. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change, as modified by Amendment No. 1, is inconsistent with Sections 6(b)(5) and 6(b)(8) or any other provision of the Act, or the rules and regulations thereunder. 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 19b-4, any request for an

opportunity to make an oral presentation.⁸⁶

Interested persons are invited to submit written data, views and arguments concerning Amendment No. 1 and regarding whether the proposed rule change, as modified by Amendment No. 1, should be approved or disapproved by May 29, 2014. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by June 12, 2014. 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. Please include File Number SR-NYSEArca-2014-04 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 SR-NYSEArca-2014-04. 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;

⁸⁶ Section 19(b) (2) of the Act, as amended by the Securities Act Amendments of 1975, Public Law 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

⁸³ See *supra* note 33.

⁸⁴ See *supra* note 43.

⁸⁵ See SIG Letter.

the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make publicly available.

All submissions should refer to File Number SR-NYSEArca-2014-04 and should be submitted on or before May 29, 2014. If comments are received, any rebuttal comments should be submitted by June 12, 2014.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁸⁷

Kevin M. O'Neill,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72088; File No. SR-EDGX-2014-14]

Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend EDGX Rule 11.5 Regarding the Route Peg Order

May 2, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on April 21, 2014, EDGX Exchange, Inc. ("EDGX" or "Exchange") 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 the Route Peg Order under Rule 11.5(c)(17) to permit: (i) Executions against routable orders that are equal to or less than the aggregate size of the Route Peg Order interest available at that price; and (ii) Users³ to add a minimum execution quantity instruction. 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, 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 Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend the Route Peg Order under Rule 11.5(c)(17) to permit: (i) Executions against routable orders that are equal to or less than the aggregate size of the Route Peg Order interest available at that price, which would replace the current requirement that routable orders be equal to or less than the size of an individual Route Peg Order; and (ii) Users to add a minimum execution quantity instruction.

A Route Peg Order is a non-displayed limit order that posts to the EDGX Book, and thereafter is eligible for execution at the national best bid ("NBB") for buy orders and national best offer ("NBO") for sell orders against routable orders that are equal to or less than the size of the Route Peg Order.⁴ Route Peg Orders are passive, resting orders on the EDGX Book⁵ and do not take liquidity. Route Peg Orders may be entered, cancelled, and cancelled/replaced prior to and during Regular Trading Hours.⁶ Route Peg Orders are eligible for execution in a given security during Regular Trading Hours, except that, even after the commencement of Regular Trading Hours, Route Peg Orders are not eligible for execution (1) in the opening cross, and (2) until such time that regular session orders in that security can be

posted to the EDGX Book. A Route Peg Order does not execute at a price that is inferior to a Protected Quotation, and is not permitted to execute if the NBBO is locked or crossed. Any and all remaining, unexecuted Route Peg Orders are cancelled at the conclusion of Regular Trading Hours.

Aggregate Size

As noted above, Route Peg Orders will currently only trade with routable orders that are equal to or smaller in quantity than the order quantity of an individual Route Peg Order. The Exchange proposes to amend the operation of the Route Peg Order to permit it to execute against routable orders that are equal to or less than the aggregate size of the Route Peg Order interest available at that price. The Exchange believes this change would incentivize Users seeking large size executions to route orders to the Exchange by increasing opportunities for executions against Route Peg Orders. This proposed change to the Route Peg Order is similar to the operation of the Nasdaq Stock Market LLC's ("Nasdaq") Supplemental Order and NYSE Arca, Inc.'s ("NYSE Arca") Tracking Order, which both only execute if the size of the incoming order is less than or equal to the aggregate size of Supplemental Order or Tracking Order interest available at that price.⁷

Minimum Execution Quantity

The Exchange also proposes to amend the Route Peg Order under Rule 11.5 to add optional functionality to allow Users to designate a minimum execution quantity. As proposed, a minimum execution quantity on a Route Peg order will no longer apply where the number of shares remaining after a partial execution are less than the minimum execution quantity. This proposed change is similar to the operation of NYSE Arca, Inc.'s Tracking Order, which permits Tracking Orders to include a minimum size requirement.⁸ The Exchange believes that providing Users with the option to designate a minimum quantity for Route Peg Orders will promote the entry of

⁷ See Nasdaq Rules 4751(f)(14), 4751(g) and 4757(a)(1)(D); see also NYSE Arca Rule 7.31(f).

⁸ On NYSE Arca, if the Tracking Order with a minimum size requirement is executed but not exhausted and the remaining portion of the Tracking Order is less than the minimum size requirement, NYSE Arca would cancel the Tracking Order. See NYSE Arca Rule 7.31(f). See also Securities Exchange Act Release No. 71366 (January 22, 2014), 79 FR 4515 (January 28, 2014) (SR-NYSEArca-2014-01) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change Amending NYSE Arca Equities Rule 7.31 to Add a Minimum Execution Size Designation for Tracking Orders).

⁸⁷ 17 CFR 200.30-3(a)(12); 17 CFR 200.30-3(a)(57).

¹ 15 U.S.C.78s(b)(1).

² 17 CFR 240.19B-4.

³ The term "User" is defined as "any Member or Sponsored Participant who is authorized to obtain access to the System pursuant to Rule 11.3." See Exchange Rule 1.5(ee).

⁴ See Securities Exchange Act Release No. 67726 (August 24, 2012), 77 FR 52771 (August 30, 2012) (Order Approving the Route Peg Order).

⁵ The "EDGX Book" is defined as "the System's electronic file of orders." See Exchange Rule 1.5(d).

⁶ "Regular Trading Hours" is defined as "the time between 9:30 a.m. and 4:00 p.m. Eastern Time." See Exchange Rule 1.5(y).