

Adviser will (a) set a Subadvised Series' overall investment strategies, (b) evaluate, select, and recommend Subadvisers to manage all or a portion of a Subadvised Series' assets, and (c) implement procedures reasonably designed to ensure that Subadvisers comply with a Subadvised Series' investment objective, policies and restrictions. Subject to review by the Board, the Adviser will (a) when appropriate, allocate and reallocate a Subadvised Series' assets among multiple Subadvisers; and (b) monitor and evaluate the performance of Subadvisers.

4. A Subadvised Series will not make any Ineligible Subadviser Changes without such agreement, including the compensation to be paid thereunder, being approved by the shareholders of the applicable Subadvised Series.

5. Subadvised Series will inform shareholders of the hiring of a new Subadviser within 90 days after the hiring of the new Subadviser pursuant to the Modified Notice and Access Procedures.

6. At all times, at least a majority of the Board will be Independent Board Members, and the selection and nomination of new or additional Independent Board Members will be placed within the discretion of the then-existing Independent Board Members.

7. Independent Legal Counsel, as defined in rule 0-1(a)(6) under the Act, will be engaged to represent the Independent Board Members. The selection of such counsel will be within the discretion of the then-existing Independent Board Members.

8. The Adviser will provide the Board, no less frequently than quarterly, with information about the profitability of the Adviser on a per Subadvised Series basis. The information will reflect the impact on profitability of the hiring or termination of any Subadviser during the applicable quarter.

9. Whenever a Subadviser is hired or terminated, the Adviser will provide the Board with information showing the expected impact on the profitability of the Adviser.

10. Whenever a Subadviser change is proposed for a Subadvised Series with an Affiliated Subadviser or a Wholly-Owned Subadviser, the Board, including a majority of the Independent Board Members, will make a separate finding, reflected in the Board minutes, that such change is in the best interests of the Subadvised Series and its shareholders, and does not involve a conflict of interest from which the Adviser or the Affiliated Subadviser or Wholly-Owned Subadviser derives an inappropriate advantage.

11. No Board member or officer of a Subadvised Series, or partner, director, manager, or officer of the Adviser, will own directly or indirectly (other than through a pooled investment vehicle that is not controlled by such person), any interest in a Subadviser, except for (i) ownership of interests in the Adviser or any entity, other than a Wholly-Owned Subadviser, that controls, is controlled by, or is under common control with the Adviser, or (ii) ownership of less than 1% of the outstanding securities of any class of equity or debt of a publicly traded company that is either a Subadviser or an entity that controls, is controlled by, or is under common control with a Subadviser.

12. Each Subadvised Series will disclose the Aggregate Fee Disclosure in its registration statement.

13. In the event the Commission adopts a rule under the Act providing substantially similar relief to that requested in the application, the requested order will expire on the effective date of that rule.

14. Any new Sub-Advisory Agreement or any amendment to a Subadvised Series' existing Investment Advisory Agreement or Sub-Advisory Agreement that directly or indirectly results in an increase in the aggregate advisory fee rate payable by the Subadvised Series will be submitted to the Subadvised Series' shareholders for approval.

For the Commission, by the Division of Investment Management, under delegated authority.

**Kevin M. O'Neil,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72666; File No. SR-NYSEArca-2013-122]

### Self-Regulatory Organizations; NYSE Arca, Inc.; Order Granting Approval of Proposed Rule Change as Modified by Amendment No. 2 Thereto Relating to the Use of Derivative Instruments by PIMCO Total Return Exchange Traded Fund

July 24, 2014.

#### I. Introduction

On November 6, 2013, 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")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend the description of the means of achieving the investment objective applicable to the PIMCO Total Return Exchange Traded Fund ("Fund") relating to its use of derivative instruments. The proposed rule change was published for comment in the **Federal Register** on November 26, 2013.<sup>3</sup> On January 9, 2014, the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.<sup>4</sup> On February 24, 2014, the Commission instituted proceedings to determine whether to approve or disapprove the proposed rule change.<sup>5</sup> On April 15, 2014, the Exchange submitted Amendments No. 1 and 2 to the proposed rule change.<sup>6</sup> On May 21, 2014, pursuant to Section 19(b)(2) of the Act,<sup>7</sup> the Commission designated a longer period within which to issue an order approving or disapproving the proposed rule change.<sup>8</sup> The Commission received no comments

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

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

<sup>3</sup> See Securities Exchange Act Release No. 70905 (November 20, 2013), 78 FR 70610 ("Notice").

<sup>4</sup> See Securities Exchange Act Release No. 71271 (January 9, 2014), 79 FR 2736 (January 15, 2014). The Commission determined that it was appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider the proposed rule change. Accordingly, the Commission designated February 24, 2014 as the date by which it should approve, disapprove, or institute proceedings to determine whether to disapprove the proposed rule change.

<sup>5</sup> See Securities Exchange Act Release No. 71606, 79 FR 11486 (February 28, 2014).

<sup>6</sup> The Exchange submitted and subsequently withdrew Amendment No. 1 to the proposed rule change. In Amendment No. 2, the Exchange provided additional details describing how the contents of the portfolio composition of the Fund would be disclosed on a daily basis. Specifically, the Fund will disclose on the Fund's Web site the following information regarding each portfolio holding, as applicable to the type of holding: ticker symbol, CUSIP number or other identifier, if any; a description of the holding (including the type of holding, such as the type of swap); the identity of the security, commodity, index or other asset or instrument underlying the holding, if any; for options, the option strike price; quantity held (as measured by, for example, par value, notional value or number of shares, contracts or units); maturity date, if any; coupon rate, if any; effective date, if any; market value of the holding; and the percentage weighting of the holding in the Fund's portfolio. It also confirms that all other facts and representations made in the Prior Release remain unchanged. See *infra*, note 9. Amendment No. 2 provides clarification to the proposed rule change, and because it does not materially affect the substance of the proposed rule change, Amendment No. 2 does not require notice and comment.

<sup>7</sup> 15 U.S.C. 78s(b)(1).

<sup>8</sup> See Securities Exchange Act Release No. 72216, 79 FR 30680 (May 28, 2014).

on the proposal. This order grants approval of the proposed rule change.

## II. Description of the Proposed Rule Change

The Commission previously approved the listing and trading of shares (“Shares”) of the Fund under NYSE Arca Equities Rule 8.600, which governs the listing and trading of Managed Fund Shares on the Exchange.<sup>9</sup> The Shares are offered by PIMCO ETF Trust (“Trust”), a statutory trust organized under the laws of the State of Delaware and registered with the Commission as an open-end management investment company.<sup>10</sup> The investment manager to the Fund is Pacific Investment Management Company LLC (“PIMCO” or “Adviser”).

In the Prior Release, the Exchange stated that, consistent with the Trust’s Exemptive Order, the Fund would not invest in options contracts, futures contracts, or swap agreements.<sup>11</sup> In view

<sup>9</sup> See Securities Exchange Act Release No. 66321 (February 3, 2012), 77 FR 6850 (February 9, 2012) (SR-NYSEArca-2011-95) (“Prior Order”). See also Securities Exchange Act Release No. 65988 (December 16, 2011), 76 FR 79741 (December 22, 2011) (SR-NYSEArca-2011-95) (“Prior Notice,” and together with the Prior Order, collectively, “Prior Release”).

<sup>10</sup> The Exchange represents that the Trust is registered under the Investment Company Act of 1940 (“1940 Act”). On October 29, 2012 the Trust filed with the Commission the most recent post-effective amendment to its registration statement under the Securities Act of 1933 and under the 1940 Act relating to the Fund (File Nos. 333-155395 and 811-22250) (“Registration Statement”). The Exchange further represents that the Trust has obtained certain exemptive relief under the 1940 Act. See Investment Company Act Release No. 28993 (November 10, 2009) (File No. 812-13571) (“Exemptive Order”).

<sup>11</sup> On December 6, 2012, the staff of the Commission’s Division of Investment Management (“IM”) issued a no-action letter (“No-Action Letter”) relating to the use of derivatives by actively-managed exchange traded funds (“ETFs”). See No-Action Letter dated December 6, 2012 from Elizabeth G. Osterman, Associate Director, Office of Exemptive Applications, IM. The No-Action Letter stated that IM staff would no longer defer consideration of exemptive requests under the 1940 Act relating to actively-managed ETFs that make use of derivatives provided that they include representations to address some of the concerns expressed in the Commission’s March 2010 press release. These representations are: (i) That the ETF’s board periodically will review and approve the ETF’s use of derivatives and how the ETF’s investment adviser assesses and manages risk with respect to the ETF’s use of derivatives; and (ii) that the ETF’s disclosure of its use of derivatives in its offering documents and periodic reports is consistent with relevant Commission and staff guidance. The No-Action Letter stated that IM would not recommend enforcement action to the Commission under sections 2(a)(32), 5(a)(1), 17(a), 22(d), and 22(e) of the 1940 Act, or rule 22c-1 under the 1940 Act if actively-managed ETFs operating in reliance on specified orders (which include the Trust’s Exemptive Order) invest in options contracts, futures contracts, or swap agreements; provided that they comply with the representations stated in the No-Action Letter, as noted above.

of the No-Action Letter issued by staff in the Commission’s Division of Investment Management on December 6, 2012, the Exchange proposes to change this representation to permit the Fund to use derivative instruments, as described below, and makes the following representations and statements.<sup>12</sup>

The Prior Release stated that the Fund will invest under normal market circumstances at least 65% of its total assets in a diversified portfolio of Fixed Income Instruments of varying maturities.<sup>13</sup> “Fixed Income Instruments” include bonds, debt securities and other similar instruments issued by various U.S. and non-U.S. public- or private-sector entities.<sup>14</sup> The Exchange proposes to revise this statement to provide that the Fund will invest under normal market circumstances at least 65% of its total assets in a diversified portfolio of Fixed Income Instruments of varying maturities, which may be represented by derivatives related to Fixed Income Instruments (“65% policy”).

The Prior Release stated that the Fund’s investment would not be used to enhance leverage. In view of the Exchange’s proposal to permit the Fund to use derivative instruments, as described below, the Fund’s

<sup>12</sup> The Adviser represents that the Fund, in connection with its use of derivative instruments, will comply with the representations stated in the No-Action Letter, as noted above. See *id.*

<sup>13</sup> As stated in the Prior Release, the term “under normal market circumstances” includes, but is not limited to, the absence of extreme volatility or trading halts in the fixed income markets or the financial markets generally; operational issues causing dissemination of inaccurate market information; or force majeure type events such as systems failure, natural or man-made disaster, act of God, armed conflict, act of terrorism, riot or labor disruption, or any similar intervening circumstance.

<sup>14</sup> As noted in the Prior Release, “Fixed Income Instruments,” as such term is used generally in the Registration Statement, include: Debt securities issued or guaranteed by the U.S. Government, its agencies or government-sponsored enterprises; corporate debt securities of U.S. and non-U.S. issuers, including convertible securities and corporate commercial paper; mortgage-backed and other asset-backed securities; inflation-indexed bonds issued both by governments and corporations; structured notes, including hybrid or “indexed” securities and event-linked bonds; bank capital and trust preferred securities; loan participations and assignments; delayed funding loans and revolving credit facilities; bank certificates of deposit, fixed time deposits and bankers’ acceptances; repurchase agreements on Fixed Income Instruments and reverse repurchase agreements on Fixed Income Instruments; debt securities issued by states or local governments and their agencies, authorities and other government-sponsored enterprises; obligations of non-U.S. governments or their subdivisions, agencies and government-sponsored enterprises; and obligations of international agencies or supranational entities. Securities issued by U.S. Government agencies or government-sponsored enterprises may not be guaranteed by the U.S. Treasury.

investments in derivative instruments may be used to enhance leverage. However, as noted in the Prior Release, the Fund’s investments will not be used to seek performance that is the multiple or inverse multiple (*e.g.*, 2Xs and 3Xs) of the Fund’s broad-based securities market index.

### *The Fund’s Use of Derivatives*

The Exchange states that, with respect to the Fund, derivative instruments primarily will include forwards, exchange-traded and over-the-counter (“OTC”) options contracts, exchange-traded futures contracts, options on futures contracts, and swap agreements. Generally, derivatives are financial contracts whose values depend upon, or are derived from, the values of an underlying asset, reference rate, or index, and may relate to stocks, bonds, interest rates, currencies or currency exchange rates, commodities, and related indexes. The Fund may, but is not required to, use derivative instruments for risk management purposes or as part of its investment strategies.<sup>15</sup>

The Exchange represents that the Fund’s investments in derivative instruments will be made in accordance with the 1940 Act and consistent with the Fund’s investment objective and policies. As described further below, the Fund will typically use derivative instruments as a substitute for taking a position in the underlying asset or as part of a strategy designed to reduce exposure to other risks, such as interest rate or currency risk. The Fund may also use derivative instruments to enhance returns. To limit the potential risk associated with such transactions, the Fund will segregate or “ earmark ” assets determined to be liquid by PIMCO in accordance with procedures established by the Trust’s Board of Trustees and in accordance with the 1940 Act (or, as permitted by applicable regulation, enter into certain offsetting positions) to cover its obligations under derivative instruments. These procedures have been adopted consistent with Section 18 of the 1940 Act and related Commission guidance. In addition, the Fund will

<sup>15</sup> The Exchange represents that the Fund will seek, where possible, to use counterparties whose financial status is such that the risk of default is reduced; however, the risk of losses resulting from default is still possible. PIMCO’s Counterparty Risk Committee evaluates the creditworthiness of counterparties on an ongoing basis. In addition to information provided by credit agencies, PIMCO credit analysts evaluate each approved counterparty using various methods of analysis, including company visits, earnings updates, the broker-dealer’s reputation, PIMCO’s past experience with the broker-dealer, market levels for the counterparty’s debt and equity, the counterparty’s liquidity, and its share of market participation.

include appropriate risk disclosure in its offering documents, including leveraging risk. Leveraging risk is the risk that certain transactions of the Fund, including the Fund's use of derivatives, may give rise to leverage, causing the Fund to be more volatile than if it had not been leveraged.<sup>16</sup> Because the markets for certain securities, or the securities themselves, may be unavailable or cost prohibitive as compared to derivative instruments, suitable derivative transactions may be an efficient alternative for the Fund to obtain the desired asset exposure.

The Exchange states that the Adviser believes derivatives can be an economically attractive substitute for an underlying physical security that the Fund would otherwise purchase. For example, the Fund could purchase Treasury futures contracts instead of physical Treasuries or could sell credit default protection on a corporate bond instead of buying a physical bond. Economic benefits include potentially lower transaction costs or attractive relative valuation of a derivative versus a physical bond (e.g., differences in yields).

The Exchange states the Adviser further believes that derivatives can be used as a more liquid means of adjusting portfolio duration as well as targeting specific areas of yield curve exposure, with potentially lower transaction costs than the underlying securities (e.g., interest rate swaps may have lower transaction costs than physical bonds). Similarly, money market futures can be used to gain exposure to short-term interest rates in order to express views on anticipated changes in central bank policy rates. In addition, derivatives can be used to protect client assets through selectively hedging downside (or "tail risks") in the Fund.

The Exchange states that the Fund also can use derivatives to increase or decrease credit exposure. Index credit default swaps (CDX) can be used to gain exposure to a basket of credit risk by "selling protection" against default or other credit events, or to hedge broad market credit risk by "buying protection." Single name credit default swaps (CDS) can be used to allow the Fund to increase or decrease exposure to specific issuers, saving investor capital through lower trading costs. The Fund can use total return swap contracts to obtain the total return of a reference asset or index in exchange for

paying a financing cost. A total return swap may be much more efficient than buying underlying securities of an index, potentially lowering transaction costs.

The Exchange states that the Adviser believes that the use of derivatives will allow the Fund to selectively add diversifying sources of return from selling options. Options purchases and sales can also be used to hedge specific exposures in the portfolio, and can provide access to return streams available to long-term investors such as the persistent difference between implied and realized volatility. Options strategies can generate income or improve execution prices (i.e., covered calls).

#### *Other Investments*

In addition to the Fund's use of derivatives in connection with the 65% policy, under the proposal, the Fund would seek to invest in derivative instruments not based on Fixed Income Instruments, consistent with the Fund's investment restrictions relating to exposure to those asset classes.

The Prior Release stated that the Fund may invest in debt securities and instruments that are economically tied to foreign (non-U.S.) countries. The Prior Release stated further that PIMCO generally considers an instrument to be economically tied to a non-U.S. country if the issuer is a foreign government (or any political subdivision, agency, authority or instrumentality of such government), or if the issuer is organized under the laws of a non-U.S. country. In the case of applicable money market instruments, such instruments will be considered economically tied to a non-U.S. country if either the issuer or the guarantor of such money market instrument is organized under the laws of a non-U.S. country.

The Exchange proposes to add to this representation that, with respect to derivative instruments, as proposed to be used, PIMCO generally will consider such instruments to be economically tied to non-U.S. countries if the underlying assets are foreign currencies (or baskets or indexes of such currencies), or instruments or securities that are issued by foreign governments (or any political subdivision, agency, authority, or instrumentality of such governments) or issuers organized under the laws of a non-U.S. country (or if the underlying assets are money market instruments, as applicable, if either the issuer or the guarantor of such money market instruments is organized under the laws of a non-U.S. country).

The Fund's investments, including investments in derivative instruments,

are subject to all of the restrictions under the 1940 Act, including restrictions with respect to illiquid securities. The Fund may hold up to an aggregate amount of 15% of its net assets in illiquid securities (calculated at the time of investment), including Rule 144A securities deemed illiquid by the Adviser, consistent with Commission guidance. The Fund will monitor its portfolio liquidity on an ongoing basis to determine whether, in light of current circumstances, an adequate level of liquidity is being maintained, and will consider taking appropriate steps in order to maintain adequate liquidity if, through a change in values, net assets, or other circumstances, more than 15% of the Fund's net assets are held in illiquid securities. Illiquid securities include securities subject to contractual or other restrictions on resale and other instruments that lack readily available markets as determined in accordance with Commission staff guidance.

The Exchange states that this proposal would become effective upon (i) the effectiveness of an amendment to the Trust's Registration Statement disclosing the Fund's intended use of derivative instruments and (ii) when this proposed rule change has become operative. The Exchange further states that the Adviser has managed and will continue to manage the Fund in the manner described in the Prior Release, and will not implement the proposed changes until this proposed rule change has become operative. In addition, the Exchange represents that there is no change to the Fund's investment objective and that the Fund will continue to comply with all initial and continued listing requirements under NYSE Arca Equities Rule 8.600. Except for the changes noted above, the Exchange represents that all other facts presented and representations made in the Prior Release remain unchanged.

#### *Derivatives Valuation Methodology for Purposes of Determining Net Asset Value*

According to the Exchange, the net asset value ("NAV") of the Fund's Shares is determined by dividing the total value of the Fund's portfolio investments and other assets, less any liabilities, by the total number of Shares outstanding. Fund Shares are valued as of the close of regular trading (normally 4:00 p.m. Eastern time ("E.T.)) ("NYSE Close") on each day NYSE Arca is open ("Business Day"). Information that becomes known to the Fund or its agents after the NAV has been calculated on a particular day will not generally be used to retroactively adjust

<sup>16</sup>To mitigate leveraging risk, the Adviser will segregate or "earmark" liquid assets or otherwise cover the transactions that may give rise to such risk.

the price of a portfolio asset or the NAV determined earlier that day. The Fund reserves the right to change the time its NAV is calculated if the Fund closes earlier, or as permitted by the Commission.

The Exchange states that for purposes of calculating NAV, portfolio securities and other assets for which market quotes are readily available are valued at market value. Market value is generally determined on the basis of last reported sales prices, or if no sales are reported, based on quotes obtained from a quotation reporting system, established market makers, or pricing services. Domestic and foreign fixed income securities and non-exchange-traded derivatives will normally be valued on the basis of quotes obtained from brokers and dealers or pricing services using data reflecting the earlier closing of the principal markets for those assets. Prices obtained from independent pricing services use information provided by market makers or estimates of market values obtained from yield data relating to investments or securities with similar characteristics. Exchange-traded options, futures, and options on futures will generally be valued at the settlement price determined by the applicable exchange. Derivatives for which market quotes are readily available will be valued at market value. Local closing prices will be used for all instrument valuation purposes. For the Fund's 4:00 p.m. E.T. futures holdings, estimated prices from Reuters will be used if any cumulative futures margin impact is greater than \$0.005 to the NAV due to futures movement after the fixed income futures market closes (3:00 p.m. E.T.) and up to the NYSE Close (generally 4:00 p.m. E.T.). Swaps traded on exchanges such as the Chicago Mercantile Exchange or the Intercontinental Exchange will use the applicable exchange closing price where available.

#### *Derivatives Valuation Methodology for Purposes of Determining Intra-Day Indicative Value*

According to the Exchange, on each Business Day, before commencement of trading in Fund Shares on NYSE Arca, the Fund discloses on its Web site the identities and quantities of the portfolio instruments and other assets held by the Fund that will form the basis for the Fund's calculation of NAV at the end of the Business Day.

In order to provide additional information regarding the intra-day value of Shares of the Fund, NYSE Arca or a market data vendor disseminates every 15 seconds through the facilities of the Consolidated Tape Association or

other widely disseminated means an updated Intra-day Indicative Value ("IIV") for the Fund as calculated by an information provider or market data vendor.

The Exchange states that a third party market data provider is currently calculating the IIV for the Fund. For the purposes of determining the IIV, the third party market data provider's valuation of derivatives is expected to be similar to their valuation of all securities. The third party market data provider may use market quotes if available or may fair value securities against proxies (such as swap or yield curves).

According to the Exchange, with respect to specific derivatives:

- Foreign currency derivatives may be valued intraday using market quotes, or another proxy as determined to be appropriate by the third party market data provider.
- Futures may be valued intraday using the relevant futures exchange data, or another proxy as determined to be appropriate by the third party market data provider.
- Interest rate swaps may be mapped to a swap curve and valued intraday based on changes of the swap curve, or another proxy as determined to be appropriate by the third party market data provider.
- CDX/CDS may be valued using intraday data from market vendors, or based on underlying asset price, or another proxy as determined to be appropriate by the third party market data provider.
- Total return swaps may be valued intraday using the underlying asset price, or another proxy as determined to be appropriate by the third party market data provider.
- Exchange listed options may be valued intraday using the relevant exchange data, or another proxy as determined to be appropriate by the third party market data provider.
- OTC options may be valued intraday through option valuation models (e.g., Black-Scholes) or using exchange traded options as a proxy, or another proxy as determined to be appropriate by the third party market data provider.

#### *Disclosed Portfolio*

The Exchange states that the Fund's disclosure of derivative positions in the Disclosed Portfolio will include information that market participants can use to value these positions intraday. On a daily basis, the Fund will disclose on the Fund's Web site the following information regarding each portfolio holding, as applicable to the type of

holding: Ticker symbol, CUSIP number or other identifier, if any; a description of the holding (including the type of holding, such as the type of swap); the identity of the security, commodity, index or other asset or instrument underlying the holding, if any; for options, the option strike price; quantity held (as measured by, for example, par value, notional value or number of shares, contracts or units); maturity date, if any; coupon rate, if any; effective date, if any; market value of the holding; and the percentage weighting of the holding in the Fund's portfolio.

#### *Impact on Arbitrage Mechanism*

The Exchange states that the Adviser believes there will be minimal, if any, impact to the arbitrage mechanism as a result of the use of derivatives. Market makers and participants should be able to value derivatives as long as the positions are disclosed with relevant information. The Exchange states that the Adviser believes that the price at which Shares trade will continue to be disciplined by arbitrage opportunities created by the ability to purchase or redeem creation Shares at their NAV, which should ensure that Shares will not trade at a material discount or premium in relation to their NAV.

The Exchange states that, according to the Adviser, there will not be any significant impacts to the settlement or operational aspects of the Fund's arbitrage mechanism due to the use of derivatives. Because derivatives generally are not eligible for in-kind transfer, they will typically be substituted with a "cash in lieu" amount when the Fund processes purchases or redemptions of creation units in-kind.

#### *Surveillance*

The Exchange represents that trading in the Shares will be subject to the existing trading surveillances, administered by the Financial Industry Regulatory Authority ("FINRA") on behalf of the Exchange, which are designed to detect violations of Exchange rules and applicable federal securities laws.<sup>17</sup> The Exchange represents that these procedures are adequate to properly monitor Exchange trading of the Shares in all trading sessions and to deter and detect violations of Exchange rules and applicable federal securities laws.

The surveillances referred to above generally focus on detecting securities trading outside their normal patterns,

<sup>17</sup> FINRA surveils trading on the Exchange pursuant to a regulatory services agreement. The Exchange is responsible for FINRA's performance under this regulatory services agreement.

which could be indicative of manipulative or other violative activity. When such situations are detected, surveillance analysis follows and investigations are opened, where appropriate, to review the behavior of all relevant parties for all relevant trading violations.

FINRA, on behalf of the Exchange, will communicate as needed regarding trading in the Shares, exchange traded options, futures, and options on futures with other markets or other entities that are members of the Intermarket Surveillance Group (“ISG”), and FINRA may obtain trading information regarding trading in the Shares, exchange traded options, futures, and options on futures from such markets or entities. In addition, the Exchange may obtain information regarding trading in the Shares, exchange traded options, futures, and options on futures from markets or other entities that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement.<sup>18</sup> In addition, FINRA, on behalf of the Exchange, is able to access, as needed, trade information for certain fixed income securities held by the Fund reported to FINRA’s Trade Reporting and Compliance Engine (“TRACE”). The Exchange also states that it has a general policy prohibiting the distribution of material, non-public information by its employees.

Additional information regarding the Trust, the Fund, and the Shares, including investment strategies, risks, NAV calculation, creation and redemption procedures, fees, portfolio holdings, disclosure policies, distributions and taxes is included in the Prior Release, Notice, and the Registration Statement, as applicable.<sup>19</sup>

### III. Discussion and Commission’s Findings

The Commission has carefully reviewed the proposed rule change and finds that it is consistent with the requirements of Section 6 of the Act<sup>20</sup> and the rules and regulations thereunder applicable to a national securities exchange.<sup>21</sup> In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the

Act,<sup>22</sup> which requires, among other things, that the Exchange’s rules be 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 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 Commission notes that the Fund and the Shares must comply with the requirements of NYSE Arca Equities Rule 8.600 to continue to be listed and traded on the Exchange.

The Commission notes that, with respect to its proposed investments in derivatives, the Fund will seek, where possible, to use counterparties whose financial status is such that the risk of default is reduced. The Exchange states that PIMCO’s Counterparty Risk Committee will evaluate the creditworthiness of counterparties on an ongoing basis. In addition to information provided by credit agencies, PIMCO credit analysts will evaluate each approved counterparty using various methods of analysis, including company visits, earnings updates, the broker-dealer’s reputation, PIMCO’s past experience with the broker-dealer, market levels for the counterparty’s debt and equity, the counterparty’s liquidity, and its share of market participation.

In addition, according to the Exchange, the proposed investments in derivative instruments will be made in accordance with the 1940 Act and consistent with the Fund’s investment objective and policies. To further limit the potential risk associated with such transactions, the Fund will segregate or “ earmark ” assets determined to be liquid by PIMCO in accordance with procedures established by the Trust’s Board of Trustees and in accordance with the 1940 Act (or, as permitted by applicable regulation, enter into certain offsetting positions) to cover its obligations under the proposed derivative instruments. The Exchange represents that these procedures have been adopted consistent with Section 18 of the 1940 Act and related Commission guidance. In addition, with respect to the proposed investments in derivative instruments, the Exchange states that appropriate risk disclosures will be provided in the Fund’s offering documents, including leveraging risk. The Exchange further represents that the Fund’s investments, including the proposed investments in derivative instruments, are subject to all of the

restrictions under the 1940 Act, including restrictions with respect to illiquid securities.

Further, the Commission notes that the Fund’s disclosure of derivative positions in the Disclosed Portfolio will include information that market participants can use to value these positions intraday. This information will include, as applicable to the type of holding: Ticker symbol, CUSIP number or other identifier, if any; a description of the holding (including the type of holding, such as the type of swap); the identity of the security, commodity, index or other asset or instrument underlying the holding, if any; for options, the option strike price; quantity held (as measured by, for example, par value, notional value or number of shares, contracts or units); maturity date, if any; coupon rate, if any; effective date, if any; market value of the holding; and the percentage weighting of the holding in the Fund’s portfolio.

The Exchange states that there will be minimal, if any, impact to the arbitrage mechanism as a result of the use of derivatives. Market makers and participants should be able to value derivatives as long as the positions are disclosed with relevant information. The Exchange notes that the price at which Shares trade will continue to be disciplined by arbitrage opportunities created by the ability to purchase or redeem creation Shares at their NAV, which should ensure that Shares will not trade at a material discount or premium in relation to their NAV. In addition, the Exchange notes that there will not be any significant impacts to the settlement or operational aspects of the Fund’s arbitrage mechanism due to the use of derivatives.

In support of this proposal, the Exchange has made additional representations, including:

(1) The Adviser has managed and will continue to manage the Fund in the manner described in the Prior Release.

(2) There is no change to the Fund’s investment objective.

(3) The Fund will continue to comply with all initial and continued listing requirements under NYSE Arca Equities Rule 8.600.

(4) FINRA, on behalf of the Exchange, will communicate as needed regarding trading in the Shares, exchange traded options, futures, and options on futures with other markets or other entities that are members of the ISG, and FINRA may obtain trading information regarding trading in the Shares, exchange traded options, futures, and options on futures from such markets or entities. In addition, the Exchange may obtain information regarding trading in the

<sup>18</sup> For a list of the current members of ISG, see [www.isgportal.org](http://www.isgportal.org). The Exchange notes that not all components of the Disclosed Portfolio for the Fund may trade on markets that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement.

<sup>19</sup> See *supra* notes 9, 3, and 10.

<sup>20</sup> 15 U.S.C. 78f.

<sup>21</sup> In approving this proposed rule change, the Commission has considered the proposed rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>22</sup> 15 U.S.C. 78f(b)(5).

Shares, exchange traded options, futures, and options on futures from markets or other entities that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement. In addition, FINRA, on behalf of the Exchange, is able to access, as needed, trade information for certain fixed income securities held by the Fund reported to FINRA's TRACE.

(5) The Fund will comply with the representations as prescribed in the No-Action Letter.

(6) Except for the proposed changes, all other facts presented and representations made in the Prior Release remain unchanged.

This approval order is based on the Exchange's representations and description of the Fund, including those set forth above and in the Notice. For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 2, is consistent with Section 6(b)(5) of the Act<sup>23</sup> and the rules and regulations thereunder applicable to a national securities exchange.

#### IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>24</sup> that the proposed rule change (SR-NYSEArca-2013-122) as modified by Amendment No. 2 thereto be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>25</sup>

**Kevin M. O'Neill,**  
Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72668; File No. SR-CBOE-2014-048]

### Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Granting Approval of a Proposed Rule Change Relating to the Give Up of a Clearing Trading Permit Holder

July 24, 2014.

#### I. Introduction

On May 23, 2014, Chicago Board Options Exchange, Incorporated ("CBOE" or the "Exchange") filed with the Securities and Exchange

Commission ("Commission"), 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> a proposed rule change relating to the "give up" process, the process by which a Trading Permit Holder ("TPH") "gives up" or selects and indicates the Clearing Trading Permit Holder ("CTPH") responsible for the clearance of an Exchange transaction. The proposed rule change was published for comment in the **Federal Register** on June 11, 2014.<sup>3</sup> The Commission received no comment letters on the proposal. This order approves the proposed rule change.

#### II. Description of the Proposal

##### A. Background

CBOE proposes to amend Rules 6.21 and 6.50 that govern the give up of a CTPH by a TPH on Exchange transactions. In order to enter transactions on the Exchange, a TPH must either be a CTPH or have a CTPH agree to accept financial responsibility for the TPH's transactions. Current CBOE Rule 6.21 provides that for each transaction in which a TPH participates, the TPH must give up the name of the CTPH (the "give up") through which the transaction will be cleared. CBOE Rule 6.50 further provides that every CTPH will be responsible for the clearance of Exchange transactions of each TPH that gives up the CTPH's name pursuant to a letter of authorization, letter of guarantee, or other authorization given by the CTPH to the executing TPH.<sup>4</sup> CBOE proposes to amend Rules 6.21 and 6.50 to address the give up process, including procedures governing that process, in greater detail.

##### B. Designated Give Ups and Guarantors

CBOE proposes to amend Rule 6.21 to provide that a TPH that is not a market maker may only give up (i) a CTPH that has previously been identified and processed by the Exchange as a "designated give up" for that TPH, or (ii) a guarantor of the TPH. The Exchange proposes to introduce and define the term "designated give up" as a CTPH that a TPH (other than a market maker) identifies in advance to the Exchange, in writing, as a CTPH that the TPH would like the ability to give up on its trades.<sup>5</sup> A TPH will be required to identify to CBOE any designated give ups in advance of giving up any CTPH

that is not a guarantor for the TPH. The Exchange has proposed a standardized form ("Notification Form") that a TPH will be required to submit to the Exchange's Registration Services Department in order to identify its designated give ups. If a TPH no longer wants the ability to give up a particular designated give up, the TPH must notify the Exchange in writing by submitting a Notification Form. CBOE proposes to allow a TPH to submit a Notification Form identifying any CTPH as a designated give up and does not propose any minimum or maximum number of designated give ups that a TPH may identify.<sup>6</sup>

The Exchange will notify a CTPH, in writing and as soon as practicable, of each TPH that has identified the CTPH as one of its designated give ups. In its proposal, CBOE noted that it will disregard any instructions from a CTPH not to permit a particular TPH to designate the CTPH as a designated give up and will not perform any subjective evaluation of a TPH's list of proposed designated give ups.<sup>7</sup> Rather, the Exchange will only ensure that the CTPHs that a TPH identifies on the Notification Form as designated give ups are current CBOE CTPHs and will review the Notification Form for completeness and accuracy.<sup>8</sup>

CBOE proposes to define the term "guarantor" for purposes of proposed Rule 6.21 as a CTPH that has issued a letter of guarantee or a letter of authorization for the executing TPH under the rules of the Exchange that are in effect at the time of the execution of the trade.<sup>9</sup> An executing TPH may give up its guarantor without identifying the guarantor as a designated give up (*i.e.*, the guarantor accepts clearing responsibility for all trades of its guarantee TPH pursuant to its role as the default CTPH for that TPH, unless the TPH indicates an alternate CTPH to be the designed give up on a particular trade), and the TPH therefore would not need to submit a Notification Form to the Exchange before indicating its guarantor as a designated give up. Because CBOE Rule 8.5 requires that a letter of guarantee be issued and filed with the Exchange by each CTPH through which a market maker desires to clear transactions, the Exchange proposes that a TPH that is a market

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

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

<sup>3</sup> See Securities Exchange Act Release No. 72325 (June 5, 2014), 79 FR 33614 (June 11, 2014) ("Notice").

<sup>4</sup> See Notice, *supra* note 3, at 33614.

<sup>5</sup> See proposed Rule 6.21(b)(i).

<sup>6</sup> See Notice, *supra* note 3, at 33614.

<sup>7</sup> See *id.* The ability of a CTPH to reject a trade on which it was indicated as the designated give up is discussed below.

<sup>8</sup> See *id.*

<sup>9</sup> See proposed Rule 6.21(b)(ii).

<sup>23</sup> 15 U.S.C. 78f(b)(5).

<sup>24</sup> 15 U.S.C. 78s(b)(2).

<sup>25</sup> 17 CFR 200.30-3(a)(12).