

SECURITIES AND EXCHANGE COMMISSION
Release No. 34-78146; File No. SR-CHX-2016-09)

June 23, 2016

Self-Regulatory Organizations; Chicago Stock Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Adopt Rules to Implement the Regulation NMS Plan to Implement a Tick Size Pilot Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹, and Rule 19b-4² thereunder, notice is hereby given that on June 16, 2016, the Chicago Stock Exchange, Inc. (“CHX” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

CHX proposes to amend the Rules of the Exchange (“CHX Rules”) to adopt Article 20, Rule 13(a) to implement the quoting and trading provisions of the Regulation NMS Plan to Implement a Tick Size Pilot Program (“Plan”). The proposed rule change is substantially similar to a proposed rule change approved by the Commission by the Bats BZX Exchange, Inc. f/k/a BATS Exchange, Inc. (“BZX”) to adopt BZX Rule 11.27(a) which also implemented the quoting and trading provisions of the Plan.³ Therefore, the Exchange has designated this proposal as “non-controversial” and provided the Commission with the notice required by Rule 19b-

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 77291 (March 3, 2016), 81 FR 12543 (March 9, 2016) (order approving SR-BATS-2015-108).

4(f)(6)(iii) under the Act.⁴

The text of this proposed rule change is available on the Exchange's website at www.chx.com and in the Commission's Public Reference Room.

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 CHX included statements concerning the purpose of and basis for the proposed rule changes 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 CHX 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 Changes

1. Purpose

On August 25, 2014, NYSE Group, Inc., on behalf of the Exchange, BZX, Bats BYX Exchange, Inc. f/k/a BATS Y-Exchange, Inc., Bats EDGA Exchange, Inc. f/k/a EDGA Exchange, Inc., Bats EDGX Exchange, Inc. f/k/a EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc. ("FINRA"), NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, the Nasdaq Stock Market LLC, New York Stock Exchange LLC ("NYSE"), NYSE MKT LLC, and NYSE Arca, Inc. (collectively "Plan Participants"),⁵ filed with the Commission, pursuant to Section 11A of the Act⁶ and Rule 608 of Regulation NMS thereunder, the Plan to implement a

⁴ 17 CFR 240.19b-4(f)(6)(iii).

⁵ A "Participant" is a "member" of the Exchange for purposes of the Act. See CHX Article 1, Rule 1(s). For clarity, the Exchange proposes to utilize the term "CHX Participant" when referring to members of the Exchange and the term "Plan Participant" when referring to Participants of the Plan.

⁶ 15 U.S.C. 78k-1.

tick size pilot program (“Pilot”).⁷ The Plan Participants filed the Plan to comply with an order issued by the Commission on June 24, 2014.⁸ The Plan⁹ was published for comment in the Federal Register on November 7, 2014, and approved by the Commission, as modified, on May 6, 2015.¹⁰

The Plan is designed to allow the Commission, market participants, and the public to study and assess the impact of increment conventions on the liquidity and trading of the common stocks of small-capitalization companies. Each Plan Participant is required to comply with, and to enforce compliance by its member organizations, as applicable, with the provisions of the Plan. As is described more fully below, the proposed rules would require CHX Participants to comply with the applicable quoting and trading increments for Pilot Securities.¹¹

The Pilot will include stocks of companies with \$3 billion or less in market capitalization, an average daily trading volume of one million shares or less, and a volume weighted average price of at least \$2.00 for every trading day. The Pilot will consist of a control group of approximately 1400 Pilot Securities and three test groups with 400 Pilot Securities in each

⁷ See Letter from Brendon J. Weiss, Vice President, Intercontinental Exchange, Inc., to Secretary, Commission, dated August 25, 2014.

⁸ See Securities Exchange Act Release No. 72460 (June 24, 2014), 79 FR 36840 (June 30, 2014).

⁹ Unless otherwise specified, capitalized terms used in this rule filing are defined as set forth in the Plan. The Exchange also proposes supplementary material as part of this proposed rule change to, among other things, provide that the terms used in proposed Rule 13(a) shall have the same meaning as provided in the Plan, unless otherwise specified.

¹⁰ See Securities Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27514 (May 13, 2015) (“Approval Order”).

¹¹ The Exchange proposes to add Interpretation and Policy .03 to Rule 13(a) to provide that the Rule shall be in effect during a pilot period to coincide with the pilot period for the Plan (including any extensions to the pilot period for the Plan).

selected by a stratified sampling.¹² During the Pilot, Pilot Securities in the control group will be quoted and traded at the currently permissible increments. Pilot Securities in the first test group (“Test Group One”) will be quoted in \$0.05 minimum increments but will continue to trade at any price increment that is currently permitted.¹³ Pilot Securities in the second test group (“Test Group Two”) will be quoted in \$0.05 minimum increments and will trade at \$0.05 minimum increments subject to a midpoint exception, a retail investor order exception, and a negotiated trade exception.¹⁴ Pilot Securities in the third test group (“Test Group Three”) will be subject to the same restrictions as Test Group Two and also will be subject to the “Trade-at” requirement to prevent price matching by a market participant that is not displaying at a price of a Trading Center’s¹⁵ “Best Protected Bid” or “Best Protected Offer,” unless an enumerated exception applies.¹⁶ In addition to the exceptions provided under Test Group Two, an exception for Block Size orders and exceptions that mirror those under Rule 611 of Regulation NMS¹⁷ will apply to the Trade-at requirement.

Compliance with the Quoting and Trading Increments of the Plan

The Plan requires the Exchange to establish, maintain, and enforce written policies and procedures that are reasonably designed to comply with applicable quoting and trading

¹² See Section V of the Plan for identification of Pilot Securities, including criteria for selection and grouping.

¹³ See Section VI(B) of the Plan.

¹⁴ See Section VI(C) of the Plan.

¹⁵ The Plan incorporates the definition of “Trading Center” from Rule 600(b)(78) of Regulation NMS. Regulation NMS defines a Trading Center as “a national securities exchange or national securities association that operates an SRO trading facility, an alternative trading system, an exchange market maker, an OTC market maker, or any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent.”

¹⁶ See Section VI(D) of the Plan.

¹⁷ 17 CFR 242.611.

requirements specified in the Plan.¹⁸ Accordingly, the Exchange is proposing new paragraph (a) to Article 20, Rule 13 (Compliance with Regulation NMS Plan to Implement a Tick Size Pilot Program) to require CHX Participants to comply with the quoting and trading provisions of the Plan.

Proposed Rule 13(a) (Compliance with Quoting and Trading Restrictions) sets forth the requirements for the Exchange and CHX Participants in meeting their obligations under the Plan. Rule 13(a)(1) will require CHX Participants to establish, maintain and enforce written policies and procedures that are reasonably designed to comply with the applicable quoting and trading requirements of the Plan. Rule 13(a)(2) provides that the Matching System¹⁹ will not display, quote or trade in violation of the applicable quoting and trading requirements for a Pilot Security specified in the Plan and this Rule, unless such quotation or transaction is specifically exempted under the Plan.

Proposed Rule 13(a)(3) clarifies the treatment of Pilot Securities that drop below \$1.00 during the Pilot Period. In particular, Rule 13(a)(3) provides that, if the price of a Pilot Security drops below \$1.00 during regular trading hours on any trading day, such Pilot Security will continue to be a Pilot Security subject to the Plan. However, if the Closing Price of a Pilot Security on any given trading day is below \$1.00, such Pilot Security will be moved out of its Pilot Test Group into the Control Group, and may then be quoted and traded at any price

¹⁸ The Exchange is also required by the Plan to develop appropriate policies and procedures that provide for data collection and reporting to the Commission of data described in Appendixes B and C of the Plan. CHX Article 20, Rule 13(b) provides rules that require compliance by CHX Participants with the collection of data provisions of the Plan described in Section VII of the Plan. See Exchange Act Release No. 77469 (March 29, 2016), 81 FR 19275 (April 4, 2016) (SR-CHX-2016-03).

¹⁹ The Matching System is an automated order execution system, which is a part of the Exchange's "Trading Facilities," as defined under CHX Article 1, Rule 1(z).

increment that is currently permitted for the remainder of the Pilot Period.²⁰ Rule 13(a)(3) also provides that, notwithstanding anything contained within these rules to the contrary, Pilot Securities (whether in the Control Group or any Pilot Test Group) will continue to be subject to the data collection requirements of the Plan at all times during the Pilot Period and for the six-month period following the end of the Pilot Period.

In approving the Plan, the Commission noted that the Plan Participants had proposed additional selection criteria to minimize the likelihood that securities that trade with a share price of \$1.00 or less would be included in the Pilot, and stated that, once established, the universe of Pilot Securities should stay as consistent as possible so that the analysis and data can be accurate throughout the Pilot Period.²¹ The Exchange notes that a Pilot Security that drops below \$1.00 during regular trading hours will remain in its applicable Test Group; a Pilot Security will only be moved to the Control Group if its Closing Price on any given trading day is below \$1.00. The Exchange believes that this provision is appropriate because it will help ensure that Pilot Securities in Test Groups One, Two and Three continue to reflect the Pilot's selection criteria, helping ensure the accuracy of the resulting data. The Exchange also believes that this provision

²⁰ The NYSE, on behalf of the Plan Participants, submitted a letter to Commission requesting exemption from certain provisions of the Plan related to quoting and trading. See letter from Elizabeth K. King, NYSE, to Brent J. Fields, Secretary, Commission, dated October 14, 2015 (“October Exemption Request”). FINRA, also on behalf of the Plan Participants, submitted a separate letter to Commission requesting additional exemptions from certain provisions of the Plan related to quoting and trading. See letter from Marcia E. Asquith, Senior Vice President and Corporate Secretary, FINRA, to Robert W. Errett, Deputy Secretary, Commission, dated February 23, 2016 (“February Exemption Request”). The Commission, pursuant to its authority under Rule 608(e) of Regulation NMS, granted BZX a limited exemption from the requirement to comply with certain provisions of the Plan as specified in the letter and noted herein. See letter from David Shillman, Associate Director, Division of Trading and Markets, Commission to Eric Swanson, General Counsel, BZX, dated March 3, 2016 (“Exemption Letter”). The Exchange is seeking the same exemptions as requested in the October Exemption Request and the February Exemption Request.

²¹ See Approval Order, supra note 10, 80 FR at 27535.

is appropriate because it responds to comments that the Plan address the treatment of securities that trade below \$1.00 during the Pilot Period.²²

Proposed Rule 13(a)(4) sets forth the applicable limitations for securities in Test Group One. Consistent with the language of the Plan, Rule 13(a)(4) provides that no CHX Participant may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group One in increments other than \$0.05. However, orders priced to execute at the midpoint of the national best bid and national best offer (“NBBO”) or best protected bid and best protected offer (“PBBO”)²³ and orders entered in a Plan Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05. Pilot Securities in Test Group One may continue to trade at any price increment that is currently permitted by applicable Plan Participant, SEC and Exchange rules.

Proposed Rule 13(a)(5) sets forth the applicable quoting and trading requirements for securities in Test Group Two. This provision states that no CHX Participant may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group Two in increments other than \$0.05. However, orders priced to execute at the midpoint of the NBBO or PBBO and orders entered in a

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Id.

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Regulation NMS defines a protected bid or protected offer as a quotation in an NMS stock that (1) is displayed by an automated trading center; (2) is disseminated pursuant to an effective national market system plan; and (3) is an automated quotation that is the best bid or best offer of a national securities exchange, the best bid or best offer of The Nasdaq Stock Market, Inc., or the best bid or best offer of a national securities association other than the best bid or best offer of The Nasdaq Stock Market, Inc. See 17 CFR 242.600(57). In the Approval Order, the Commission noted that the protected quotation standard encompasses the aggregate of the most aggressively priced displayed liquidity on all Trading Centers, whereas the NBBO standard is limited to the single best order in the market. See Approval Order, supra note 10, 80 FR at 27539.

Plan Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05.

Proposed Rule 13(a)(5) also sets forth the applicable trading restrictions for Test Group Two securities. Absent any of the exceptions listed in the Rule, no CHX Participant may execute orders in any Pilot Security in Test Group Two in price increments other than \$0.05. The \$0.05 trading increment will apply to all trades, including Brokered Cross Trades.

Consistent with the language of the Plan, the Rule provides that Pilot Securities in Test Group Two may trade in increments of less than \$0.05 under the following circumstances: (1) trading may occur at the midpoint between the NBBO or the PBBO; (2) Retail Investor Orders may be provided with price improvement that is at least \$0.005 better than the PBBO; and (3) Negotiated Trades may trade in increments of less than \$0.05.

The Exchange also proposes to add an exception to Rule 13(a)(5) to permit CHX Participants to fill a customer order in a Pilot Security in Test Group Two at a non-nickel increment to comply with Article 9, Rule 17 (Prohibition Against Trading Ahead of Customer Orders) under limited circumstances. Specifically, the exception would allow the execution of a customer order following a proprietary trade by the CHX Participant at an increment other than \$0.05 in the same security, on the same side and at the same price as (or within the prescribed amount of) a customer order owed a fill pursuant to Article 9, Rule 17, where the triggering proprietary trade was permissible pursuant to an exception under the Plan.²⁴

Thus, the Exchange is proposing to add a customer order protection exception to Rule 13(a)(5) that would permit CHX Participants to trade Pilot Securities in Test Group Two in

²⁴ The Commission granted BZX an exemption from Rule 608(c) related to this provision. See February Exemption Request and Exemption Letter, supra note 20. The Exchange is seeking the same exemptions as requested in the October Exemption Request and the February Exemption Request. Supra note 20.

increments less than \$0.05, and where the CHX Participant is executing a customer order to comply with Article 9, Rule 17 following the execution of a proprietary trade by the CHX Participant at an increment other than \$0.05 where such proprietary trade was permissible pursuant to an exception under the Plan. The Exchange believes that this approach best facilitates the ability of CHX Participants to continue to protect customer orders while retaining the flexibility to engage in proprietary trades that comply with an exception to the Plan.

Proposed Rule 13(a)(6) sets forth the applicable quoting and trading restrictions for Pilot Securities in Test Group Three. The rule provides that no CHX Participant may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group Three in increments other than \$0.05. However, orders priced to execute at the midpoint of the NBBO or PBBO and orders entered in a Plan Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05. The rule also states that, absent any of the applicable exceptions, no CHX Participant that operates a Trading Center may execute orders in any Pilot Security in Test Group Three in price increments other than \$0.05. The \$0.05 trading increment will apply to all trades, including Brokered Cross Trades.²⁵

Proposed Rule 13(a)(6)(C) sets forth the exceptions pursuant to which Pilot Securities in Test Group Three may trade in increments of less than \$0.05. First, trading may occur at the midpoint between the NBBO or PBBO. Second, Retail Investor Orders may be provided with price improvement that is at least \$0.005 better than the PBBO. Third, Negotiated Trades may trade in increments of less than \$0.05.

²⁵ A brokered cross trade is a trade that a broker-dealer that is a member of a Plan Participant executes directly by matching simultaneous buy and sell orders for a Pilot Security. See Section I(G) of the Plan.

Similar to that proposed under Rule 13(a)(5) described above, the Exchange also proposes to add an exception to Rule 13(a)(6) to permit CHX Participants to fill a customer order in a Pilot Security in Test Group Three at a non-nickel increment to comply with Article 9, Rule 17 (Prohibition Against Trading Ahead of Customer Orders) under limited circumstances. Specifically, the exception would allow the execution of a customer order following a proprietary trade by the CHX Participant at an increment other than \$0.05 in the same security, on the same side and at the same price as (or within the prescribed amount of) a customer order owed a fill pursuant to Article 9, Rule 17, where the triggering proprietary trade was permissible pursuant to an exception under the Plan.²⁶ Thus, the Exchange is proposing to add a customer order protection exception to Rule 13(a)(6) that would permit CHX Participants to trade Pilot Securities in Test Group Three in increments less than \$0.05, and where the CHX Participant is executing a customer order to comply with Article 9, Rule 17 following the execution of a proprietary trade by the CHX Participant at an increment other than \$0.05 where such proprietary trade was permissible pursuant to an exception under the Plan.

Proposed Rule 13(a)(6)(D) sets forth the “Trade-at Prohibition,” which is the prohibition against executions by a CHX Participant that operates a Trading Center of a sell order for a Pilot Security in Test Group Three at the price of a Protected Bid or the execution of a buy order for a Pilot Security in Test Group Three at the price of a Protected Offer during regular trading hours, absent any of the exceptions set forth in Rule 13(a)(6)(D). Consistent with the Plan, the rule reiterates that a CHX Participant that operates a Trading Center that is displaying a quotation, via either a processor or an SRO quotation feed that is a Protected Bid or Protected Offer is permitted to execute orders at that level, but only up to the amount of its displayed size. A CHX

²⁶ See supra note 24. The Exchange is seeking the same exemptions as requested in the October Exemption Request and the February Exemption Request. Supra note 20.

Participant that operates a Trading Center that was not displaying a quotation that is the same price as a Protected Quotation, via either a processor or an SRO quotation feed, is prohibited from price-matching protected quotations unless an exception applies.

Consistent with the Plan, proposed Rule 13(a)(6)(D) also sets forth the exceptions to the Trade-at prohibition, pursuant to which a CHX Participant that operates a Trading Center may execute a sell order for a Pilot Security in Test Group Three at the price of a Protected Bid or execute a buy order for a Pilot Security in Test Group Three at the price of a Protected Offer. The first exception to the Trade-at Prohibition is the “display exception,” which allows a trade to occur at the price of the Protected Quotation, up to the Trading Center’s full displayed size, if the order “is executed by a trading center that is displaying a quotation.”²⁷

In Rule 13(a)(6)(D), the Exchange proposes that a CHX Participant that utilizes the independent aggregation unit concept may satisfy the display exception only if the same independent aggregation unit that displays interest via either a processor or an SRO Quotation Feed also executes an order in reliance upon this exception. The rule provides that “independent aggregation unit” has the same meaning as provided under Rule 200(f) of SEC Regulation SHO.²⁸ This provision also recognizes that not all CHX Participants may utilize the independent aggregation unit concept as part of their regulatory structure, and still permits such CHX Participants to utilize the display exception if all the other requirements of that exception are

²⁷ See Section VI(D)(1) of the Plan.

²⁸ 17 CFR 242.200. Treatment as an independent aggregation unit is available if traders in an aggregation unit pursue only the particular trading objective(s) or strategy(ies) of that aggregation unit and do not coordinate that strategy with any other aggregation unit. Therefore, one independent aggregation unit within a Trading Center cannot execute trades pursuant to the display exception in reliance on quotations displayed by a different independent aggregation unit. As an example, an agency desk of a Trading Center cannot rely on the quotation of a proprietary desk in a separate independent aggregation unit at that same Trading Center.

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As initially proposed by the Plan Participants, the Plan contained an additional condition to the display exception, which would have required that, where the quotation is displayed through a national securities exchange, the execution at the size of the order must occur against the displayed size on that national securities exchange; and where the quotation is displayed through the Alternative Display Facility or another facility approved by the Commission that does not provide execution functionality, the execution at the size of the order must occur against the displayed size in accordance with the rules of the Alternative Display Facility of such approved facility (“venue limitation”).²⁹ Some commenters stated that this provision was anti-competitive, as it would have forced off-exchange Trading Centers to route orders to the venue on which the order was displayed.³⁰

In approving the Plan, the Commission modified the Trade-At Prohibition to remove the venue limitation.³¹ The Commission noted that the venue limitation was not prescribed in its Order mandating the filing of the Plan.³² The Commission also noted that the venue limitation would have unnecessarily restricted the ability of off-exchange market participants to execute orders in Test Group Three Securities, and that removing the venue limitation should mitigate concerns about the cost and complexity of the Pilot by reducing the need for off-exchange Trading Centers to route to the exchange.³³ The Commission also stated that the venue limitation did not create any additional incentives to display liquidity in furtherance of the

²⁹ See Securities Exchange Act Release No. 73511 (November 3, 2014), 79 FR 66423, 66437 (November 7, 2014).

³⁰ See Approval Order, *supra* note 10, 80 FR at 27540.

³¹ Id.

³² Id.

³³ Id.

purposes of the Trade-At Prohibition, because the requirement that a Trading Center could only trade at a protected quotation up to its displayed size should be sufficient to incentivize displayed liquidity.³⁴

Consistent with Plan and the SEC's determination to remove the venue limitation, the Exchange is making clear that the display exception applies to trades done by a Trading Center otherwise than on an exchange where the Trading Center has previously displayed a quotation in either an agency or a principal capacity. As part of the display exception, the Exchange also proposes that a Trading Center that is displaying a quotation as agent or riskless principal may only execute as agent or riskless principal, while a Trading Center displaying a quotation as principal (excluding riskless principal) may execute either as principal or agent or riskless principal. The Exchange believes this is consistent with the Plan and the objective of the Trade-at Prohibition, which is to promote the display of liquidity and generally to prevent any Trading Center that is not quoting from price-matching Protected Quotations. Providing that a Trading Center may not execute on a proprietary basis in reliance on a quotation representing customer interest (whether agency or riskless principal) ensures that the Trading Center cannot avoid compliance with the Trade-at Prohibition by trading on a proprietary basis in reliance on a quotation that does not represent such Trading Center's own interest. Where a Trading Center is displaying a quotation at the same price as a Protected Quotation in a proprietary capacity, transactions in any capacity at the price and up to the size of such Trading Center's displayed quotation would be permissible. Transactions executed pursuant to the display exception may occur on the venue on which such quotation is displayed or over the counter.

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Id.

The proposal also excepts Block Size orders³⁵ and permits Trading Centers to trade at the price of a Protected Quotation, provided that the order is of Block Size at the time of origin and is not an aggregation of non-block orders, broken into orders smaller than Block Size prior to submitting the order to a Trading Center for execution; or executed on multiple Trading Centers.³⁶ The Plan only provides that Block Size orders shall be exempted from the Trade-At Prohibition. In requiring that the order be of Block Size at the time of origin and not an aggregation of non-block orders, or broken into orders smaller than Block Size prior to submitting the order to a Trading Center for execution; or executed on multiple Trading Centers, the Exchange believes that it is providing clarity as to the circumstances under which a Block Size order will be excepted from the Trade-At Prohibition.

Consistent with the Plan, the proposal also excepts an order that is a Retail Investor Order that is executed with at least \$0.005 price improvement.

The exceptions set forth in proposed Rule 13(a)(6)(D)(ii)(d) through (n) are based on the exceptions found in Rule 611 of Regulation NMS.³⁷ The subparagraph (d) exception applies when the order is executed when the Trading Center displaying the Protected Quotation that was traded at was experiencing a failure, material delay, or malfunction of its systems or equipment. The subparagraph (e) exception applies to an order that is executed as part of a transaction that was not a “regular way” contract. The subparagraph (f) exception applies to an order that is

³⁵ “Block Size” is defined in the Plan as an order (1) of at least 5,000 shares or (2) for a quantity of stock having a market value of at least \$100,000.

³⁶ Once a Block Size order or portion of such Block Size order is routed from one Trading Center to another Trading Center in compliance with Rule 611 of Regulation NMS, the Block Size order would lose the proposed Trade-at exemption, unless the Block Size remaining after the first route and execution meets the Block Size definition under the Plan.

³⁷ See 17 CFR 242.611.

executed as part of a single-priced opening, reopening, or closing transaction by the Trading Center. The subparagraph (g) exception applies to an order that is executed when a Protected Bid was priced higher than a Protected Offer in a Pilot Security.

The subparagraph (h) exception applies when the order is identified as a Trade-at Intermarket Sweep Order. The subparagraph (i) exception applies when the order is executed by a Trading Center that simultaneously routed Trade-at Intermarket Sweep Orders to execute against the full displayed size of a Protected Quotation with a price that is better than or equal to the limit price of the limit order identified as a Trade-at Intermarket Sweep Order. Depending on whether Rule 611 or the Trade-at requirement applies, an ISO may mean that the sender of the ISO has swept better-priced protected quotations, so that the recipient of that ISO may trade through the price of the protected quotation (Rule 611), or it could mean that the sender of the ISO has swept protected quotations at the same price that it wishes to execute at (in addition to any better-priced quotations), so the recipient of that ISO may trade at the price of the protected quotation (Trade-at). Given that the meaning of an ISO may differ under Rule 611 and Trade-at, the Exchange proposes Rule 13(a)(6)(D)(ii)(h) so that the recipient of an ISO in a Test Group Three security would know, upon receipt of that ISO, that the Trading Center that sent the ISO had already executed against the full size of displayed quotations at that price, e.g., the recipient of that ISO could permissibly trade at the price of the protected quotation.

The Exchange proposes to further clarify the use of an ISO in connection with the Trade-at requirement by adopting, as part of proposed Rule 13(a)(7), a definition of “Trade-at Intermarket Sweep Order.” As set forth in the Plan and as noted above, the definition of a Trade-at ISO does not distinguish ISOs that are compliant with Rule 611 from ISOs that are compliant with Trade-at. The Exchange therefore proposes to define a Trade-at ISO as a limit order for a

Pilot Security that meets the following requirements: (1) when routed to a Trading Center, the limit order is identified as a Trade-at Intermarket Sweep Order; (2) simultaneously with the routing of the limit order identified as a Trade-at Intermarket Sweep Order, one or more additional limit orders, as necessary, are routed to execute against the full displayed size of any protected bid, in the case of a limit order to sell, or the full displayed size of any protected offer, in the case of a limit order to buy, for the Pilot Security with a price that is better than or equal to the limit price of the limit order identified as a Trade-at Intermarket Sweep Order. These additional routed orders also must be marked as Trade-at Intermarket Sweep Orders. The Exchange believes that this proposed change will further clarify to recipients of ISOs in Group Three securities whether the ISO satisfies the requirements of Rule 611 or Trade-at.

The exception under subparagraph (j) of proposed Rule 13(a)(6)(D)(ii) applies when the order is executed as part of a Negotiated Trade. The subparagraph (k) exception applies when the order is executed when the Trading Center displaying the Protected Quotation that was traded at had displayed, within one second prior to execution of the transaction that constituted the Trade-at, a Best Protected Bid or Best Protected Offer, as applicable, for the Pilot Security with a price that was inferior to the price of the Trade-at transaction.

The exception proposed in subparagraph (l) applies to a “stopped order.” The stopped order exemption in Rule 611 of SEC Regulation NMS applies where “[t]he price of the trade-through transaction was, for a stopped buy order, lower than the national best bid in the NMS stock at the time of execution or, for a stopped sell order, higher than the national best offer in the NMS stock at the time of execution.”³⁸ The Trade-at stopped order exception applies where “the price of the Trade-at transaction was, for a stopped buy order, equal to the national best bid

³⁸ See 17 CFR 242.611(b)(9).

in the Pilot Security at the time of execution or, for a stopped sell order, equal to the national best offer in the Pilot Security at the time of execution.”³⁹

To illustrate the application of the stopped order exemption as it currently operates under Rule 611 of SEC Regulation NMS and as it is currently proposed for Trade-at, assume the NBB is \$10.00 and another protected quote is at \$9.95. Under Rule 611 of SEC Regulation NMS, a stopped order to buy can be filled at \$9.95 and the firm does not have to send an ISO to access the protected quote at \$10.00 since the price of the stopped order must be lower than the NBB. For the stopped order to also be executed at \$9.95 and satisfy the Trade-at requirements, the Trade-at exception would have to be revised to allow an order to execute at the price of a protected quote which, in this case, could be \$9.95.

Based on the fact that a stopped order would be treated differently under the Regulation NMS Rule 611 exception than under the proposed Trade-at exception, the Exchange believes that it is appropriate to amend the Trade-at stopped order exception to ensure that the application of this exception will produce a consistent result under both Regulation NMS and the Plan. The Exchange therefore proposes to amend the stopped order exception to allow a transaction to satisfy the Trade-at requirement if the stopped order price, for a stopped buy order, is equal to or less than the NBB, and for a stopped sell order, is equal to or greater than the NBO, as long as such order is priced at an acceptable increment.

Proposed subparagraph (1) to Rule 13(a)(6)(D)(ii) would define a “stopped order” as an order that is executed by a Trading Center which, at the time of order receipt, the Trading Center had guaranteed an execution at no worse than a specified price, where (1) the stopped order was for the account of a customer; (2) the customer agreed to the specified price on an order-by-order

³⁹ See Plan, Section VI(D)(12).

basis; and (3) the price of the Trade-at transaction was, for a stopped buy order, equal to or less than the National Best Bid in the Pilot Security at the time of execution or, for a stopped sell order, equal to or greater than the National Best Offer in the Pilot Security at the time of execution as long as such order is priced at an acceptable increment.⁴⁰

The subparagraph (m) exception applies where the order is for a fractional share of a Pilot Security, provided that such fractional share order was not the result of breaking an order for one or more whole shares of a Pilot Security into orders for fractional shares or was not otherwise effected to evade the requirements of the Trade-at Prohibition or any other provisions of the Plan

The subparagraph (n) exception applies to bona fide errors transactions. Following the adoption of Rule 611 and its exceptions, the Commission issued exemptive relief that created exceptions from Rule 611 for certain error correction transactions.⁴¹ The Exchange has determined that it is appropriate to incorporate the error correction exception to the Trade-at prohibition, as this exception is equally applicable in the Trade-at context. Accordingly, the Exchange is proposing to exempt certain transactions to correct bona fide errors in the execution of customer orders from the Trade-at prohibition, subject to the conditions set forth by the SEC's order exempting these transactions from Rule 611 of SEC Regulation NMS.⁴²

⁴⁰ The Commission granted BZX an exemption from Rule 608(c) related to this provision. See Exemption Letter, supra note 20. The Exchange is seeking the same exemptions as requested in the October Exemption Request and the February Exemption Request. Supra note 20.

⁴¹ See Securities Exchange Act Release No. 55884 (June 8, 2007), 72 FR 32926 (June 14, 2007).

⁴² The Commission granted BZX an exemption from Rule 608(c) related to this provision. See February Exemption Request and Exemption Letter, supra note 20. The Exchange is seeking the same exemptions as requested in the October Exemption Request and the February Exemption Request. Supra note 20.

As with the corresponding exception under Rule 611 of SEC Regulation NMS, the Exchange proposes to define a “bona fide error” as: (i) the inaccurate conveyance or execution of any term of an order including, but not limited to, price, number of shares or other unit of trading; identification of the security; identification of the account for which securities are purchased or sold; lost or otherwise misplaced order tickets; short sales that were instead sold long or vice versa; or the execution of an order on the wrong side of a market; (ii) the unauthorized or unintended purchase, sale, or allocation of securities, or the failure to follow specific client instructions; (iii) the incorrect entry of data into relevant systems, including reliance on incorrect cash positions, withdrawals, or securities positions reflected in an account; or (iv) a delay, outage, or failure of a communication system used to transmit market data prices or to facilitate the delivery or execution of an order. The bona fide error must be evidenced by objective facts and circumstances, the Trading Center must maintain documentation of such facts and circumstances, and the Trading Center must record the transaction in its error account. To avail itself of the exemption, the Trading Center must establish, maintain, and enforce written policies and procedures that are reasonably designed to address the occurrence of errors and, in the event of an error, the use and terms of a transaction to correct the error in compliance with this exemption. Finally, the Trading Center must regularly surveil to ascertain the effectiveness of its policies and procedures to address errors and transactions to correct errors and take prompt action to remedy deficiencies in such policies and procedures.⁴³

Consistent with the Plan, the final exception to the Trade-At Prohibition and its accompanying supplementary material applies to an order that is for a fractional share of a Pilot Security. The supplementary material provides that such fractional share orders may not be the

⁴³ See Securities Exchange Act Release No. 55884 (June 8, 2007), 72 FR 32926 (June 14, 2007).

result of breaking an order for one or more whole shares of a Pilot Security into orders for fractional shares or that otherwise were effected to evade the requirements of the Trade-at Prohibition or any other provisions of the Plan. In approving the Plan, the Commission noted that this exception was appropriate, as there could be potential difficulty in the routing and executing of fractional shares.⁴⁴

The proposed rule change will become operative upon the commencement of the Pilot Period.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act⁴⁵ in general, and furthers the objectives of Section 6(b)(5) of the Act⁴⁶ in particular, in that it is designed 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 Exchange believes that this proposal is consistent with the Act because it implements, interprets, and clarifies the provisions of the Plan, and is designed to assist the Exchange and CHX Participants in meeting regulatory obligations pursuant to the Plan. In approving the Plan, the SEC noted that the Pilot was an appropriate, data-driven test that was designed to evaluate the impact of a wider tick size on trading, liquidity, and the market quality of securities of smaller capitalization companies, and was therefore in furtherance of the purposes of the Act. To the extent that this proposal implements, interprets, and clarifies the Plan

⁴⁴ See Approval Order, *supra* note 10, 80 FR at 27541.

⁴⁵ 15 U.S.C. 78f(b).

⁴⁶ 15 U.S.C. 78f(b)(5).

and applies specific requirements to CHX Participants, the Exchange believes that this proposal is in furtherance of the objectives of the Plan, as identified by the SEC, and is therefore consistent with the Act.

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

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange notes that the proposed rule change implements the provisions of the Plan, and is designed to assist the Exchange in meeting its regulatory obligations pursuant to the Plan. The Exchange also notes that the quoting and trading requirements of the Plan will apply equally to all CHX Participants that trade Pilot Securities.

C. Self-Regulatory Organization's Statement on Comments Regarding the Proposed Rule Changes Received from Members, Participants or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Changes and Timing for Commission Action

The Exchange has designated this rule filing as non-controversial under Section 19(b)(3)(A) of the Act⁴⁷ and paragraph (f)(6) of Rule 19b-4 thereunder.⁴⁸ The Exchange asserts that the proposed rule change: (1) will not significantly affect the protection of investors or the public interest, (2) will not impose any significant burden on competition, (3) and will not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate. In addition, the Exchange provided the Commission with written notice of its intent to file the proposed rule change, along with a brief description and text of the

⁴⁷ 15 U.S.C. 78s(b)(3)(A).

⁴⁸ 17 C.F.R. 240.19b-4.

proposed rule change, at least five business days prior to the date of filing.⁴⁹

The Exchange believes that the proposed rule change meets the criteria of subparagraph (f)(6) of Rule 19b-4⁵⁰ because it would not significantly affect the protection of investors or the public interest; rather, the proposed rule change will benefit investors because it implements, interprets, and clarifies the provisions of the Plan, and is designed to assist the Exchange and CHX Participants in meeting regulatory obligations pursuant to the Plan. To the extent that this proposal implements, interprets, and clarifies the Plan and applies specific requirements to CHX Participants, the Exchange believes that this proposal is in furtherance of the objectives of the Plan, as identified by the SEC, and is therefore consistent with the Act, the protection of investors and the public interest. In addition, the proposed rule change is substantially similar to a proposed rule change by BZX that was approved by the Commission.⁵¹ Therefore, the proposed rule change does not present any unique issues not previously considered by the Commission. Based on the foregoing, the Exchange has designated this rule filing as “non-controversial” under Section 19(b)(3)(A) of the Act⁵² and paragraph (f)(6) of Rule 19b-4 thereunder.⁵³

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily temporarily suspend such rule change if it appears to the Commission that such action is: (1) necessary or appropriate in the public interest; (2) for the protection of investors; or (3) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the

⁴⁹ 17 C.F.R. 240.19b-4(f)(6)(iii).

⁵⁰ 17 CFR 240.19b-4(f)(6).

⁵¹ See supra note 3.

⁵² 15 U.S.C. 78s(b)(3)(A).

⁵³ 17 CFR 240.19b-4.

Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File No. SR-CHX-2016-09 on the subject line.

Paper Comments:

- Send paper comments in triplicate to [Name of Secretary], Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File No. SR-CHX-2016-09. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<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 changes between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549-1090 on official business days between the hours of 10:00

a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the CHX. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR-CHX-2016-09 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁵⁴

Brent J. Fields
Secretary

⁵⁴ 17 CFR 200.30-3(a)(12).