

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-79502; File No. SR-IEX-2016-18)

December 7, 2016

Self-Regulatory Organizations; Investors Exchange LLC; Notice of Filing of Proposed Rule Change to: (i) Amend Rules 11.190(a)(3) and 11.190(b)(8) to Modify the operation of the Primary Peg Order Type; (ii) Amend Rule 11.190(h)(C)(ii) and (D)(ii) Regarding Price Sliding in Locked and Crossed Markets to Simplify the Price Sliding Process for Both Primary Peg Orders and Discretionary Peg Orders Resting on or Posting to the Order Book; and (iii) Make Minor Housekeeping Changes to Conform Certain Terminology

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934² and Rule 19b-4 thereunder,³ notice is hereby given that, on November 29, 2016, the Investors Exchange LLC filed with the Securities and Exchange Commission the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. 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

Pursuant to the provisions of Section 19(b)(1) under the Securities Exchange Act of 1934 (“Act”),⁴ and Rule 19b-4 thereunder,⁵ Investors Exchange LLC (“IEX” or “Exchange”) is filing with the Securities and Exchange Commission (“Commission”) proposed rule changes to (i) amend Rules 11.190(a)(3) and 11.190(b)(8) to modify the operation of the primary peg order type; (ii) amend Rule 11.190(h)(C)(ii) and (D)(ii) [sic] regarding price sliding in locked and crossed markets to simplify the price sliding process for both primary peg orders and

¹ 15 U.S.C. 78s(b)(1).

² 15 U.S.C. 78a.

³ 17 CFR 240.19b-4.

⁴ 15 U.S.C. 78s(b)(1).

⁵ 17 CFR 240.19b-4.

Discretionary Peg orders resting on or posting to the Order Book; and (iii) make minor housekeeping changes to conform certain terminology.

The text of the proposed rule change is available at the Exchange's website at www.iextrading.com, at the principal office of the Exchange, and at 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 self-regulatory organization included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

Background

The purpose of the proposed rule change is to amend Rules 11.190(a)(3) and 11.190(b)(8) to modify the operation of the primary peg order type offered by the Exchange, and to amend Rule 11.190(h)(C)(ii) and (D)(ii) [sic] regarding price sliding in locked and crossed markets to simplify the price sliding process for both primary peg orders and Discretionary Peg orders resting on or posting to the Order Book.

Currently, the Exchange offers three types of pegged orders – primary peg, midpoint peg and discretionary peg – each of which are non-displayed orders that upon entry into the System and while resting on the Order Book, are pegged to a reference price based on the national best

bid and offer (“NBBO”) and the price of the order is automatically adjusted by the System in response to changes in the NBBO. As set forth in Rule 11.190(b)(8), a primary peg order is a pegged order that upon entry and when posting to the Order Book, the price of the order is automatically adjusted by the System to be equal to and ranked at the less aggressive of the primary quote (i.e., the national best bid (“NBB”) for buy orders and the national best offer (“NBO”) for sell orders) or the order’s limit price, if any. While resting on the Order Book, the order is automatically adjusted by the System in response to the changes in the NBB (NBO) for buy (sell) orders up (down) to the order’s limit price, if any.

In the event the NBBO becomes locked or crossed, primary peg orders, as well as Discretionary Peg orders, resting on or posting to the Order Book are priced to the less aggressive of either the prior non-locked or non-crossing near side quote (i.e., the prior unlocked or uncrossed NBB (NBO) for buy (sell) orders), or one (1) MPV less aggressive than the locking or crossing price.⁶

Overview

The Exchange proposes to modify the operation of the primary peg order type. The order type as revised is a non-displayed order designed to enable a Member (or customer thereof) to rest trading interest on the Order Book at a price inferior to the primary quote and remain available to execute against an incoming order seeking to cross the spread and execute at prices equal to or more aggressive (from the taker’s perspective) than such quote, while avoiding adverse selection when the market appears to be moving against the resting primary peg order (i.e., moving lower in the case of a buy order or higher in the case of a sell order). As described more fully below, the primary peg order as proposed combines the offset feature of the Primary

⁶ See, Rule 11.190(h)(C)(ii) and (D)(ii) [sic].

Pegged Order offered by BATS BZX Exchange, Inc (“BZX”)⁷ with the price improvement opportunities and protections offered by the Exchange’s existing Discretionary Peg order.⁸ Specifically, the primary peg order as proposed offers Members an opportunity to rest one (1) MPV less aggressive than the primary quote (i.e., one (1) MPV below the NBB for buy orders or one (1) MPV above the NBO for sell orders) but remain eligible to exercise price discretion up (down) to the NBB (NBO) for buy (sell) orders, and is designed to protect such orders from unfavorable executions by preventing the exercise of such price discretion when the Exchange has determined that the market is moving against the order (i.e., a crumbling quote is detected). In addition, the Exchange proposes to simplify the price sliding process for both primary peg orders and Discretionary Peg orders resting on or posting to the Order Book so that such orders will slide to one MPV less aggressive than the locking or crossing price (i.e., higher for a sell order and lower for a buy order) rather than remaining at the prior non-locked or non-crossed price when such price is less aggressive.

The Exchange notes that the primary peg order type has received modest usage by Members, and at the same time, the Exchange has observed that spread crossing interest entered on the Exchange is sometimes unable to find sufficient resting interest willing to trade at the far-side primary quote. The Exchange believes (based in part on informal discussions with liquidity providing Members) that the primary peg order type as revised, which is designed to prevent adverse selection in unstable market conditions, will incentivize passive resting liquidity priced to execute at the primary quote on the Exchange, and consequently may result in greater execution opportunities at the far side quote for Members entering spread crossing orders.

⁷ See BZX Rule 11.9(c)(8).

⁸ See, Rule 11.190(b)(10).

Description of Proposed Rule Change

As proposed, Rule 11.190(b)(8) provides that (i) a primary peg order will, upon entry and when posting to the Order Book, be automatically adjusted by the System to be equal to and ranked at the less aggressive of one (1) minimum price variant (“MPV”)⁹ less aggressive than the primary quote (i.e., one MPV below (above) the NBB (NBO) for buy (sell) orders) or the order’s limit price, as applicable; (ii) exercise price discretion up (down) to the NBB (NBO) for buy (sell) orders, except during periods of quote instability as defined in Rule 11.190(g); and (iii) in locked and crossed markets, slide one MPV less aggressive than the locking price or crossing price (i.e., the lowest Protected Offer for buy orders and the highest Protected Bid for sell orders).¹⁰

As is the case with Discretionary Peg orders, Rule 11.190(b)(8) would provide that a primary peg order would maintain time priority at its resting price, and be prioritized behind any non-displayed interest resting at the NBB (NBO) for buy (sell) orders (i.e., the “primary quote”) for the duration of the book processing action in which it is exercising discretion. If multiple primary peg orders are exercising discretion during the same book processing action, they would maintain their relative time priority when executing at the primary quote.

As proposed, the manner in which a primary peg order will exercise price discretion is similar to the manner in which a Discretionary Peg order exercises price discretion. As set forth in Rule 11.190(b)(10), a Discretionary Peg order pegs to the less aggressive of the primary quote (i.e., NBB for buy orders and NBO for sell orders) or the order’s limit price, if any, but, in order to meet the limit price of an active order, will exercise price discretion up to the less aggressive

⁹ See, Rule 11.210.

¹⁰ The proposed changes to the price sliding process in locked and crossed markets would also apply to Discretionary Peg orders.

of the Midpoint Price¹¹ or the order's limit price, if any. However, a Discretionary Peg order will not exercise such price discretion during periods of quote instability as defined in Rule 11.190(g).¹² Similarly, as proposed a primary peg order will exercise discretion in order to meet the limit price of an active order up to the NBB (for buy orders) or down to the NBO (for sell orders), except during periods of quote instability as defined in Rule 11.190(g), or if the order is resting at its limit price, if any.

The Exchange also proposes to amend Rule 11.190(h)(C)(ii) and (D)(ii) [sic] regarding price sliding in locked and crossed markets to simplify the price sliding process for both primary peg orders and Discretionary Peg orders resting on or posting to the Order Book. As proposed,

¹¹ See, Rule 1.160(t).

¹² As set forth in Rule 11.190(g), in determining whether a crumbling quote exists, the Exchange utilizes real time relative quoting activity of Protected Quotations and a proprietary mathematical calculation (the "quote instability calculation") to assess the probability of an imminent change to the current Protected NBB to a lower price or Protected NBO to a higher price for a particular security ("quote instability factor"). When the quoting activity meets predefined criteria and the quote instability factor calculated is greater than the Exchange's defined threshold ("quote instability threshold"), the System treats the quote as not stable ("quote instability" or a "crumbling quote"). During all other times, the quote is considered stable ("quote stability"). The System independently assesses the quote stability of the Protected NBB and Protected NBO for each security. When the System determines that a quote, either the Protected NBB or the Protected NBO, is unstable, the determination remains in effect at that price level for ten (10) milliseconds. The System will only treat one side of the Protected NBBO as unstable in a particular security at any given time. By not permitting resting Discretionary Peg orders to execute at a price that is more aggressive than the near-side protected NBB or NBO (as applicable) during periods of quote instability, the Exchange System is intended to attempt to protect such orders from unfavorable executions when the market is moving against them. Once the market has moved and the Exchange System deems the near-side Protected NBB or NBO (as applicable) to be stable (pursuant to a pre-determined, objective set of conditions as described below), Discretionary Peg orders are permitted to exercise discretion up to (for buy orders) or down to (for sell orders) the midpoint of the NBBO in order to meet the limit price of active orders on the order book and thereby potentially provide price improvement to such active orders. Quote stability or instability (also referred to as a crumbling quote) is an assessment that the Exchange System makes on a real-time basis, based on a pre-determined, objective set of conditions specified in Rule 11.190(g)(1).

such orders will slide to one MPV less aggressive than the locking or crossing price (i.e., higher for a sell order and lower for a buy order) rather than remaining at the prior non-locked or non-crossed price when such price is less aggressive. If a primary peg order is submitted while the market is crossed, the order would post to the Order Book priced one (1) MPV less aggressive than the crossing price, the lowest Protected Offer for buy orders and the highest Protected Bid for sell orders. The Exchange notes that the goal of this provision is to ensure that primary peg and Discretionary Peg orders do not rest at locking or crossing prices. The Exchange believes that the variability of the existing approach is unnecessarily complicated, without any material benefit, and requires both the Exchange System and Member systems to keep track of the prior non-locked/non-crossed price. Therefore, the Exchange believes that simplifying the price sliding processing for primary peg and Discretionary Peg orders is appropriate in this respect since it would accomplish the goal of sliding such orders to a non-locked/non-crossed price.

The Exchange does not propose to amend the order modifiers and parameters currently applicable to primary peg orders as set forth in Rule 11.190(b)(8)(A)-(J), and such order modifiers and parameters would apply to primary peg orders as revised. Specifically, currently and as proposed, a primary peg order: (i) must be a pegged order; (ii) must have a time-in-force (“TIF”) of DAY, GTT, GTX, or SYS;¹³ (iii) is not eligible for routing;¹⁴ (iv) may not be an intermarket sweep order;¹⁵ (v) may be submitted with a limit price, or without a limit price; (vi) is eligible to trade only during the Regular Market Session; (vii) may be a minimum quantity

¹³ See, Rule 11.190(a)(3). A primary peg order with a TIF of GTT, GTX or SYS entered before the opening of the Regular Market Session will be rejected. A primary peg order with a TIF of DAY entered before the opening of the Regular Market Session will be queued in the System until the start of the Regular Market Session.

¹⁴ See, Rules 11.230(b) and (c)(2).

¹⁵ See, Rule 11.190(b)(12).

order;¹⁶ (viii) is not eligible to be displayed by the System; (ix) may be an odd lot, round lot, or mixed lot; and (x) is not eligible to be invited by the System to Recheck, as described in Rule 11.230(a)(4)(D).

Finally, the Exchange proposes to make a minor conforming housekeeping change to Rule 11.190(h)(D)(ii) [sic] to refer to the “crossing price” rather than “crossed quote” to be consistent with other references within the rule.

Implementation

The Exchange plans to implement the proposed changes during the first quarter of 2017 pending completion of necessary technology changes and subject to Commission approval. The Exchange will announce the implementation date of the proposed changes by Trader Alert at least 5 business days in advance of such implementation date and within 90 days of approval of this proposed rule change.

2. Statutory Basis

IEX believes that the proposed rule change is consistent with Section 6(b)¹⁷ of the Act in general, and furthers the objectives of Section 6(b)(5) of the Act,¹⁸ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in 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.

¹⁶ See, Rule 11.190(b)(11).

¹⁷ 15 U.S.C. 78f.

¹⁸ 15 U.S.C. 78f(b)(5).

Specifically, IEX believes that the proposal is consistent with protection of investors and the public interest in that the primary peg order type is designed to assist Members in obtaining best execution for their customers (and proprietary orders) by providing an opportunity to execute at the NBBO, but limiting executions at the NBBO when the NBBO is not stable, thereby reducing the potential to execute at a stale price. Moreover, as discussed above, the primary peg order, as proposed, combines key attributes of the Primary Pegged Order offered by BZX, in that both order types offer Members an opportunity to rest more passively than the primary quote, and the discretionary price improvement attributes of the Exchange's Discretionary Peg order type. Thus, IEX does not believe that the primary peg order type raises any new or novel issues that have not already been considered by the Commission in connection with existing order types of IEX and BZX.¹⁹ In particular, IEX notes that, in connection with its grant of IEX's application for registration as a national securities exchange under Sections 6 and 19 of the Act, the Commission specifically found IEX's order type rules, including those providing for a Discretionary Peg order to exercise price discretion only when the quote appears to be stable, to be consistent with the Act and, in particular, the Section 6(b)(5) requirement that the Exchange's rules be designed to promote just and equitable principles of trade, remove impediments to and perfect the mechanisms of a free and open market and a national market system, and protect investors and the public interest.²⁰ Accordingly, the Exchange believes that providing the same price discretion to primary peg orders is similarly consistent with the protection of investors and the public interest.

¹⁹ See also NYSE Arca Equities Rule 7.31P(h) [sic] which provides for a Discretionary Pegged order type based on IEX's Discretionary Peg order type.

²⁰ See Securities Exchange Act Release No. 34-78101 at 47 (June 17, 2016), 81 FR 41142 (June 23, 2016) (File No. 10-222).

The Exchange also believes that the proposed priority rules for primary peg orders are designed to protect investors and the public interest because the proposed priority rules are identical to those for Discretionary Peg orders.²¹ As noted above, the Commission has already considered the Exchange's Discretionary Peg order type in connection with its grant of IEX's application for registration as a national securities exchange under Sections 6 and 19 of the Act, and specifically found IEX's order type rules to be consistent with the Act and, in particular, the Section 6(b)(5) requirement that the exchange's rules be designed to promote just and equitable principles of trade, remove impediments to and perfect the mechanisms of a free and open market and a national market system, and protect investors and the public interest.²² Accordingly, the Exchange does not believe that applying these priority rules to primary peg orders raises any new or novel issues that have not already been considered by the Commission, and is thus consistent with the protection of investors and the public interest.

The Exchange also believes that simplifying the operation of price sliding primary peg orders in a locked or crossed market is consistent with the protection of investors and the public interest by making the Exchange's rules more clear and transparent, and removing the variability of a primary peg orders booked price in situations where the market becomes locked or crossed. Specifically, rather than price sliding such orders at the less aggressive of either the prior unlocked or uncrossed near side quotation, or one MPV less aggressive than the locking or crossing price, the Exchange will simply slide such orders one MPV less aggressive than the locking or crossing price, creating a simple, transparent process for price sliding such orders.

Finally, the Exchange believes that the minor conforming housekeeping change to Rule 11.190(h)(D)(ii) [sic] to refer to "crossing price" rather than "crossed quote" is consistent with

²¹ See IEX Rule 11.190(b)(10).

²² See supra, note 20.

the protection of investors and the public interest because it will make the applicable rule text more clear by eliminating inconsistent verbiage to describe the same concept.

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

IEX 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 proposed change will offer the primary peg order type equally to all IEX Members. Furthermore, the Exchange does not believe that allowing primary peg orders to exercise discretion in stable markets, using the formula set forth in IEX Rule 11.190(g), will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Commission has already considered the Exchange's Discretionary Peg order type in connection with its grant of IEX's application for registration as a national securities exchange under Sections 6 and 19 of the Act.²³ The proposed rule change is designed to extend the benefits of the quote stability calculation to Members using the primary peg order type to prevent unfavorable executions in crumbling markets; therefore, no new burdens are being proposed.

The Exchange also does not believe that the proposed primary peg order type will result in any burden on Members seeking to cross the spread and execute at the far side quote (the NBO (NBB) for buy (sell) orders), because the benefits and protections offered by the proposed primary peg order type, which is designed to prevent adverse selection in unstable market conditions, is intended to incentivize passive resting liquidity priced to execute at the primary quote on the Exchange, and consequently may result in greater execution opportunities at the far side quote for Members entering spread crossing orders.

²³ See supra, note 20.

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

Written comments were neither solicited nor received.

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

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

IV. Solicitation of Comments

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

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File SR-IEX-2016-18 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-IEX-2016-18. 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 change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-IEX-2016-18 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.²⁴

Eduardo A. Aleman
Assistant Secretary

²⁴ 17 CFR 200.30-3(a)(12).