

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-85566; File No. SR-IEX-2019-03)

April 9, 2019

Self-Regulatory Organizations; Investors Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Modify the Listing Requirements Contained in Rule 14.412 to Change the Definition of Market Value for Purposes of the Shareholder Approval Rules and Eliminate the Requirement for Shareholder Approval of Issuances at a Price Less Than Book Value but Greater than Market Value

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (“Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that on March 26, 2019, Investors Exchange LLC (“IEX” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

Pursuant to the provisions of Section 19(b)(1) under the Securities Exchange Act of 1934 (“Act”),<sup>4</sup> and Rule 19b-4 thereunder,<sup>5</sup> IEX is filing with the Commission a proposed rule change to modify the listing requirements contained in IEX Rule 14.412(d) to change the definition of market value for purposes of the shareholder approval rules and to eliminate the requirement for shareholder approval of issuances at a price less than book value but greater than market value. The Exchange has designated this proposal as non-controversial and provided the Commission

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

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

<sup>4</sup> 15 U.S.C. 78s(b)(1).

<sup>5</sup> 17 CFR 240.19b-4.

with the notice required by Rule 19b-4(f)(6)(iii) under the Act.<sup>6</sup>The text of the proposed rule change is available at the Exchange’s website at [www.iextrading.com](http://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 the 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 statement may be examined at the places specified in Item IV below. The self-regulatory organization has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

IEX Rule 14.412(d) requires shareholder approval for security issuances for less than the greater of book or market value (other than in the context of a public offering) if either (a) an issuance equals 20% or more of the outstanding common stock or outstanding voting power or (b) a smaller issuance coupled with sales by officers, directors or substantial shareholders meets or exceeds the 20% threshold. IEX Rule 14.002(a)(21) defines “market value” as the consolidated closing bid price (multiplied by the measure to be valued). As described more fully below, IEX proposes to amend Rule 14.412(d) to change the definition of market value for purposes of the shareholder approval rules and to eliminate the requirement for shareholder approval of issuances at a price less than book value but greater than market value. This

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<sup>6</sup> 17 CFR 240.19b-4(f)(6)(iii).

proposed amendment is substantially similar to an amendment NASDAQ recently made to its own shareholder approval requirements.<sup>7</sup>

#### I. Definition of Market Value

IEX Rule 14.412(d) requires an IEX-listed company to obtain shareholder approval when issuing common stock or securities convertible into or exercisable for common stock, which alone or together with sales by officers, directors or Substantial Shareholders of the Company,<sup>8</sup> equals 20% or more of the common shares or 20% or more of the voting power outstanding at a price less than the greater of the book value or market value of that stock. Rule 14.002(a)(21) defines “market value” as the consolidated closing bid price (multiplied by the measure to be valued).

The Exchange believes that the consolidated closing bid price may not be transparent to companies and investors and does not always reflect an actual price at which a security has traded. The Exchange also believes that, generally speaking, the price of an executed trade is viewed as a more reliable indicator of value than a bid quotation, and the more shares executed, the more reliable the price is considered. Further, it is the Exchange’s understanding that in structuring transactions, investors and companies often rely on an average price over a prescribed period of time for pricing issuances because it can smooth out unusual fluctuations in price.<sup>9</sup> Accordingly, IEX proposes to modify the measure of market value for purposes of Rule 14.412(d) from the consolidated closing bid price to the lower of: (i) the closing price (as

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<sup>7</sup> See Exchange Act Release No. 34–84287 (September 26, 2018) (SR-NASDAQ-2018-008); 83 FR 49599 (October 2, 2018).

<sup>8</sup> See IEX Rule 14.412(e)(3).

<sup>9</sup> See, e.g., Exchange Act Release No. 84287 (September 26, 2018) (SR-NASDAQ-2018-008); 83 FR 49599 (October 2, 2018) at 49601 and Exchange Act Release No. 84821 (December 14, 2018) (SR-NYSE-2018-54); 83 FR 65378 (December 20, 2018) at 65380.

reflected on iextrading.com) immediately preceding the signing of a binding agreement; or (ii) the average closing price of the common stock (as reflected on iextrading.com) for the five trading days immediately preceding the signing of a binding agreement.

In addition, the ability of an IEX-listed company to issue securities in a private placement without shareholder approval will continue to be limited by other important IEX rules.<sup>10</sup> For example, any discounted issuance of stock to a company's officers, directors, employees, or consultants would require shareholder approval under the Exchange's equity compensation rules.<sup>11</sup> In addition, shareholder approval would be required if the issuance resulted in a change of control and for the acquisition of stock or assets of another company, including where an issuance increases voting power or common shares by 5% or more and an officer or director or substantial security holder has a 5% direct or indirect interest (or collectively 10%) in the company or assets to be acquired.<sup>12</sup>

#### A. Closing Price

The closing price reported on iextrading.com is the IEX Official Closing Price.<sup>13</sup> In the case of an IEX-listed security, the IEX Official Closing Price is the price of the Closing Auction.<sup>14</sup> The IEX closing auction is designed to gather the maximum liquidity available for execution at the close of trading, and to maximize the number of shares executed at a single price

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<sup>10</sup> See, e.g., IEX Rule 14.412(a), (b) and (c). If shareholder approval is not required under IEX Rule 14.412(d) it could still be required under one of the other shareholder approval provisions of IEX Rule 14.412 since these provisions apply independently of each other.

<sup>11</sup> See IEX Rule 14.412(c).

<sup>12</sup> See IEX Rule 14.412(a) and (b).

<sup>13</sup> See IEX Rules 1.160(v) and 11.350(d)(2)(B).

<sup>14</sup> In the event that there is no Closing Auction, the IEX Official Closing Price will be the price of the Final Last Sale Eligible Trade. See IEX Rule 11.350(d)(2)(B). See also, IEX Rule 11.350(a)(7) which defines "Final Last Sale Eligible Trade".

at the close of the trading day. The closing auction promotes accurate closing prices by offering specialized orders available only during the closing auction and integrating those orders with regular orders submitted during the trading day that are still available at the close. The closing auction is made highly transparent to all investors through the widespread dissemination of stock-by-stock information about the closing auction, including the potential price and size of the closing auction. IEX believes its closing auction is a valuable pricing tool for issuers, traders, and investors alike. For these reasons, IEX believes that the closing price reported on [iextrading.com](http://iextrading.com) is a better reflection of the market price of a security than the closing bid price. This proposal is consistent with the approach of other exchanges.<sup>15</sup>

Further, IEX believes it is appropriate to codify in Rule 14.412(d) that [iextrading.com](http://iextrading.com) is the appropriate source for closing price information in view of the variety of available market data sources.<sup>16</sup>

#### B. Five-day Average Price

As noted above, the Exchange understands that in structuring transactions involving the issuance of securities of a listed company, investors and companies often rely on an average price over a prescribed period of time for pricing issuances because it can smooth out unusual fluctuations in price on a single day. However, there are potential negative consequences to using a five-day average as the sole measure of whether shareholder approval is required. For

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<sup>15</sup> See Nasdaq Rule 5635(d)(1) and Section 312.04(i) of the New York Stock Exchange Listed Company Manual, each of which utilize the closing price for purposes of determining market value for purposes of comparable shareholder approval requirements.

<sup>16</sup> The closing price in each IEX-listed security is published on [iextrading.com](http://iextrading.com) in near real time and is available without registration or a fee. IEX does not currently intend to charge a fee for access to closing price information or otherwise restrict availability of this information. In the event that IEX subsequently determines to do so, it will file a proposed rule change under Section 19(b) of the Act with respect to such change and address any impact to compliance with Rule 14.412(d) thereto.

example, in a declining market, the five-day average price will always be above the current market price, thus making it difficult for companies to close transactions because investors could buy shares in the market at a price below the five-day average price. Conversely, in a rising market, the five-day average price will appear to be a discount to the closing price. In addition, if material news is announced during the five-day period, the average could be a worse reflection of the market value than the closing price after the news is disclosed. Nonetheless, IEX believes that these risks are already accepted in the market, as evidenced by the use of an average price in transactions that do not require shareholder approval under other exchanges' listing rules,<sup>17</sup> such as where less than 20% of the outstanding shares are issuable in the transaction, notwithstanding the risk of possible unfavorable price movements borne by both the issuer and the purchaser of the securities during the time between when the agreement is executed and the closing of the transaction. However, the Exchange believes that concerns regarding the use of solely a five-day average price are valid, and as such, proposes to amend Rule 14.412(d) to define market value as the lower of the closing price immediately preceding the signing of the binding agreement or the five-day average of the closing price as the measure of market value for purposes of the shareholder approval rules. Thus, an issuance would not require an approval by the company's shareholders, so long as it is at a price that is greater than the lower of those measures.<sup>18</sup> To improve the readability of the rule, IEX proposes to define this new concept as the "Minimum Price" and eliminate references to book value and market value from Rule 14.412(d).

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<sup>17</sup> See e.g., Nasdaq Rule 5635 and Section 312.03 of the NYSE Listed Company Manual.

<sup>18</sup> Issuances below Market Value to officers, directors, employees, or consultants are, and will continue to be, subject to the requirements of Rule 14.412(c). IEX will continue to use the definition of Market Value in Rule 14.002(a)(21), which provides that Market Value means the consolidated closing bid price multiplied by the measure to be valued, for purposes of Rule 14.412(c) as well as other IEX listing rules that include a Market Value component.

## II. Book Value

Consistent with the proposed use of the Minimum Price to determine whether shareholder approval is required for an issuance of securities under Rule 14.412, IEX proposes to eliminate the requirement for shareholder approval of issuances at a price less than book value but greater than market value. Book value is an accounting measure and its calculation is based on the historic cost of assets, not their current value. As such, the Exchange does not believe it is an appropriate measure of whether a transaction is dilutive or should otherwise require shareholder approval. IEX understands that when the market price is below the book value, the book value test can appear arbitrary and have a disproportionate impact on companies in certain industries and at certain times. For example, during the financial crisis in 2008 and 2009, many banks and finance-related companies temporarily traded below book value. Similarly, companies that make large investments in infrastructure may trade below the accounting carrying value of those assets. In these circumstances, the Exchange believes that companies are precluded based on purely accounting reasons from quickly raising capital on terms that are at or above the market price. Further, the Exchange is not aware that shareholders of listed companies consider book value to be a material factor when they are asked to vote to approve a proposed transaction.

## III. Other Changes

To improve the readability of Rule 14.412(d) IEX proposes to define “20% Issuance” as “a transaction, other than a public offering as defined in Supplementary Material .03, involving the sale, issuance or potential issuance by the Company of common stock (or securities convertible into or exercisable for common stock), which alone or together with sales by officers, directors or Substantial Shareholders of the Company, equals 20% or more of the common stock or 20% or more of the voting power outstanding before the issuance.” This definition combines

the situations described in existing Rule 14.412(d)(1) and (d)(2) and makes no substantive change but for the change to the pricing tests, as described above, such that shareholder approval would be required under the same circumstances for a 20% Issuance as under existing Rule 14.412(d).

IEX also proposes to amend the title of Rule 14.412(d) and the preamble to Rule 14.412 to replace references to “private placements” to “transactions other than public offerings” to conform the language in the title of Rule 14.412(d) and the preamble to the language in the rule text and that of Supplementary Material .03, which provides the definition of a public offering. Of course, private placements would continue to be considered “transactions other than public offerings.”

Finally, IEX proposes to amend Supplementary Material .03 and .04, which describe how IEX applies the shareholder approval requirements, to conform references to book and market value with the new definition of Minimum Price, as described above, and to utilize the newly defined term “20% Issuance.”

## 2. Statutory Basis

IEX believes that the proposed rule change is consistent with Section 6(b)<sup>19</sup> of the Act in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>20</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in 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

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<sup>19</sup> 15 U.S.C. 78f.

<sup>20</sup> 15 U.S.C. 78f(b)(5).



interest; and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

#### Definition of Market Value

The proposed rule change will modify the minimum price at which a 20% Issuance would not need shareholder approval from the closing bid price to the lower of: (i) the closing price (as reflected on iextrading.com) immediately preceding the signing of a binding agreement; or (ii) the average closing price of the common stock (as reflected on iextrading.com) for the five trading days immediately preceding the signing of the binding agreement.

IEX believes that allowing issuers to price transactions at the closing price (as reflected on iextrading.com) rather than closing consolidated bid price will perfect the mechanism of a free and open market, and protect investors and the public interest because the closing price will represent an actual sale at the most liquid time of the day, which generally occurs at the same or greater price than the bid price.<sup>21</sup> As discussed in the Purpose section, the closing price is generally derived from the IEX closing auction, which is designed to gather the maximum liquidity available for execution at the close of trading, and to maximize the number of shares executed at a single price at the close of the trading day. The closing auction is made highly transparent to all investors through the widespread dissemination of stock-by-stock information about the closing auction, including the potential price and size of the closing auction. IEX thus believes its closing auction is a valuable pricing tool for issuers, traders, and investors alike. For these reasons, IEX believes that the closing price reported on iextrading.com is a better reflection of the market price of a security than the closing bid price, for purposes of determining whether a

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<sup>21</sup> Sales typically take place between the bid and ask prices.

20% Issuance requires shareholder approval, and is thus consistent with perfecting the mechanism of a free and open market, and protection of investors and the public interest.

Allowing share issuances to be priced at the five-day average of the closing price will further align IEX's requirements with how many transactions are structured, such as transactions where Rule 14.412(d) is not implicated because the issuance is for less than 20% of the common stock and the parties rely on the five-day average for pricing to smooth out unusual fluctuations in price. In so doing, the proposed rule change will perfect the mechanism of a free and open market. Further, allowing a five-day average price continues to protect investors and the public interest because it will allow companies and investors to price transactions in a manner designed to eliminate aberrant pricing resulting from unusual transactions on the day of a transaction. Maintaining the allowable average at just a five-day period also protects investors by ensuring the period is not too long, such that it would result in the price being distorted by ordinary past market movements and other outdated events. In a market that rises each day of the period, the five-day average will be less than the price at the end of the period, but would still be higher than the price at the start of such period. Further, IEX understands that when selecting the appropriate price for a transaction, company officers and directors also have to consider their state law structural safeguards, including fiduciary responsibilities, intended to protect shareholder interests.

In addition, because prices could be displayed from numerous data sources on different web sites, to provide certainty about the appropriate price, IEX proposes to codify within the rule that [iextrading.com](http://iextrading.com) is the appropriate source of the closing price information, which is available in near real time and without registration or fee. Because the closing bid price is not included in many public data feeds, this requirement will promote just and equitable principles of trade and

remove impediments to and perfect the mechanism of a free and open market because it will improve the transparency of the rule and provide additional certainty to all market participants about the appropriate price to be used in determining if shareholder approval is required.

Additionally, IEX believes that where two alternative measures of value exist that both reasonably approximate the value of listed securities, defining the Minimum Price as the lower of those values allows issuers the flexibility to use either measure because they can also sell securities at a price greater than the Minimum Price without needing shareholder approval. In the Exchange's view, this flexibility, and the certainty that a transaction can be structured at either value in a manner that will not require shareholder approval, further perfects the mechanism of a free and open market without diminishing the existing investor protections of the Rule 14.412(d).

#### Book Value

IEX also believes that eliminating the requirement for shareholder approval of issuances at a price less than book value but greater than market value does not diminish the existing investor protections of Rule 14.412(d). Book value is primarily an accounting measure calculated based on historic cost and is generally perceived as an inappropriate measure of the current value of a stock. IEX also understands that the existing book value test can appear arbitrary and have a disproportionate impact on companies in certain industries and at certain times. For example, during the financial crisis in 2008 and 2009, many banks and finance-related companies traded below book value. Similarly, companies that make large investments in infrastructure may trade below the accounting carrying value of those assets. Because the Exchange believes that book value is not an appropriate measure of the current value of a stock, the elimination of the requirement for shareholder approval of issuances at a price less than book value but greater than market value will remove an impediment to, and perfect the mechanism of, a free and open

market, which currently unfairly burdens companies in certain industries, without meaningfully diminishing the investor protections of Rule 14.412(d).

#### Other Changes

To improve the readability of Rule 14.412(d), IEX proposes to define “20% Issuance” as “a transaction, other than a public offering as defined in Supplementary Material .03 to Rule 14.412(d), involving the sale, issuance or potential issuance by the Company of common stock (or securities convertible into or exercisable for common stock), which alone or together with sales by officers, directors or Substantial Shareholders of the Company, equals 20% or more of common stock or 20% or more of the voting power outstanding before the issuance.” This definition combines the situations described in existing Rule 14.412(d)(1) and (d)(2) but makes no substantive change to the meaning of the rule. Under the proposed rule, but for the separate change to the pricing test, shareholder approval would be required under the same circumstances for a 20% Issuance as under existing Rule 14.412(d). IEX believes that the improved readability of the rule will perfect the mechanism of a free and open market by making the rule easier to understand and apply.

IEX also believes that amending the title of Rule 14.412(d) and the preamble to Rule 14.412 to replace references to “private placements” to “transactions other than public offerings” to conform to the language in the rule text and Supplementary Material .03 to Rule 14.412(d), which provides the definition of a public offering, will perfect the mechanism of a free and open market by making the rule easier to understand and apply. Finally, IEX believes that amending Supplementary Material .03 and .04 to Rule 14.412, which describe how IEX applies the shareholder approval requirements, to conform references to book and market value with the new definition of Minimum Price, as described above, and to utilize the newly defined term “20%

Issuance” will perfect the mechanism of a free and open market by eliminating confusion caused by references to a measure that is no longer applicable and by making the rule easier to understand and apply.

The Exchange also notes that the proposed rule change is substantially identical to existing Nasdaq rules that were approved by the Commission.<sup>22</sup> The Exchange believes that the same factors and analysis that led to the Commission’s approval of the comparable Nasdaq rule change are applicable to IEX’s proposed rule change. Consequently, the Exchange does not believe that the proposed rule change raises any new or novel issues.

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 rule change is designed to promote consistent and fair regulation, rather than for any competitive purpose. The proposed rule change would revise requirements that could burden issuers by unnecessarily limiting the circumstances where they can sell securities without shareholder approval. With respect to intramarket competition, all listed companies would be affected in the same manner by these changes. With respect to intermarket competition, the Exchange does not believe that the proposed change will result in a burden on competition since other listing exchanges have comparable rules and listed companies have a choice of where to list. As such, these changes are neither intended to, nor expected to, impose any burden on competition.

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.

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<sup>22</sup> See supra note 7.

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

The Exchange has filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>23</sup> and Rule 19b-4(f)(6) thereunder.<sup>24</sup> Because the proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(6) thereunder.<sup>25</sup>

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

### 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](mailto:rule-comments@sec.gov). Please include File Number SR-IEEX-2019-03 on the subject line.

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<sup>23</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>24</sup> 17 CFR 240.19b-4(f)(6).

<sup>25</sup> In addition, Rule 19b-4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

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-IEEX-2019-03. 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 such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to

make available publicly. All submissions should refer to File Number SR-IEX-2019-03, 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.<sup>26</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>26</sup> 17 CFR 200.30-3(a)(12).