

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-74677; File No. SR-NYSEMKT-2015-23)

April 8, 2015

Self-Regulatory Organizations; NYSE MKT LLC; Notice of Filing of Proposed Rule Change Adopting a Principles-Based Approach to Prohibit the Misuse of Material Nonpublic Information by Specialists and e-Specialists by Deleting Rule 927.3NY and Section (f) of Rule 927.5NY

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934 (the “Act”)² and Rule 19b-4 thereunder,³ notice is hereby given that, on March 26, 2015, NYSE MKT LLC (the “Exchange” or “NYSE MKT”) filed with the Securities and Exchange Commission (the “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

The Exchange proposes to adopt a principles-based approach to prohibit the misuse of material nonpublic information by Specialists and e-Specialists by deleting Rule 927.3NY and section (f) of Rule 927.5NY. The text of the proposed rule change is available on the Exchange’s website at www.nyse.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

¹ 15 U.S.C.78s(b)(1).

² 15 U.S.C. 78a.

³ 17 CFR 240.19b-4.

received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

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

1. Purpose

The Exchange proposes to adopt a principles-based approach to prohibit the misuse of material nonpublic information by Specialists and e-Specialists by deleting Rule 927.3NY and section (f) of Rule 927.5NY. In so doing, the Exchange would harmonize its rules governing Specialists, e-Specialists and Market Makers relating to protecting against the misuse of material, non-public information. The Exchange believes that Rules 927.3NY and 927.5NY(f) are no longer necessary because all ATP Holders, including Specialists and e-Specialists, are subject to the Exchange’s general principles-based requirements governing the protection against the misuse of material, non-public information, pursuant to Exchange Rules, Part 1 – General Rules, Rule 3 (General Prohibitions and Duty to Report), section (j) (“Rule 3(j)”), which obviates the need for separately-prescribed requirements for a subset of market participants on the Exchange.

Background

The Exchange has three classes of registered market makers. Pursuant to Rule 920NY(a), a Market Maker is an ATP holder that is registered with the Exchange for the purpose of submitting quotes electronically and making transactions as a dealer-specialist verbally on the Trading Floor, through the System from the Trading Floor, or remotely from off the Trading Floor. As the rule further provides, a Market Maker can be either a Remote Market Maker, a Floor Market Maker, a Specialist, or an e-Specialist. All Market Makers are subject to the requirements of Rule 925NY and 925.1NY, which set forth the obligations of Market Makers,

particularly relating to quoting.

Rule 927NY(c) specifies the obligations of Specialists, which, in addition to the Market Maker obligations of Rule 925NY, must also honor guaranteed markets. Rules 927.4NY and 927.5NY specify the obligations of e-Specialists, which is a form of Specialist that operates remotely only. The quoting obligations of all Market Makers, including Specialists/e-Specialists, are set forth in Rule 925.1NY. That rule sets forth the main difference between Market Makers and Specialists/e-Specialists, namely that Specialists/e-Specialists have a heightened quoting obligation as compared to Market Makers.⁴ In addition to a heightened quoting obligation, pursuant to Rule 964NY, Specialists/e-Specialists that are participants in the Specialist Pool are eligible to receive a guaranteed participation of incoming bids and offers.⁵

Importantly, whether operating on the Trading Floor or remotely, all Market Makers, including Specialists/e-Specialists, have access to the same information in the Consolidated Book that is available to all other market participants. Moreover, none of the Exchange's Market Makers, including Specialists/e-Specialists, have agency obligations to the Exchange's Consolidated Book. As such, the distinctions between Market Makers and Specialists/e-Specialists are the quoting requirements set forth in Rule 925.1NY and allocation guarantee for the Specialist Pool set forth in Rule 964NY.

Notwithstanding that Market Makers, Specialists, and e-Specialists have access to the same Exchange trading information as all other market participants on the Exchange, the

⁴ Compare Rule 925.1NY(b) (“Specialists must provide continuous two-sided quotations throughout the trading day in its appointed issues [sic] 90% of the time the Exchange is open for trading in each issue.”) with Rule 925.1NY(c) (“A Market Maker must provide continuous two-sided quotations throughout the trading day in its appointed issues for 60% of the time the Exchange is open for trading in each issue.”)

⁵ See Rule 964NY(b)(2)(C).

Exchange has distinct, prescriptive rules governing how Specialists and e-Specialists may operate. Rule 927.3NY prohibits ATP Holders affiliated with a Specialist from purchasing or selling any option to which the Specialist is appointed, except to reduce or liquidate positions after appropriate identification and floor official approval of the transaction. The rule further provides an exemption from the prohibition for affiliated firms that implement specified Exchange-approved procedures to restrict the flow of material, non-public information. Rules 927.3NY(e) – (j) outline the “Exemption Guidelines” with which an affiliated firm must comply to obtain an exemption from the restriction in Rule 927.3NY. These specified “Exemption Guidelines” are meant to ensure that a Specialist will not have access to material, non-public information possessed by its affiliated ATP Holder, and that a firm will not misuse its affiliated Specialist’s material, non-public information. The Exchange notes that the current rule is based on requirements from when specialists on the American Stock Exchange had agency obligations to the Exchange’s book.

Rule 927.5NY(f) requires e-Specialists to maintain information barriers that are reasonably designed to prevent the misuse of material, non-public information with any affiliates that may conduct a brokerage business in option classes allocated to the e-Specialist or act as specialist or Market Maker in any security underlying options allocated to the e-Specialist (but does not require prior Exchange approval and does not set forth proscribed “Exemption Guidelines”).

Proposed Rule Change

The Exchange believes that the particularized guidelines in Rule 927.3NY and 927.5NY(f) for Specialists and e-Specialists, respectively, are no longer necessary and proposes to delete them. Rather, the Exchange believes that Rule 3(j) governing the misuse of material,

non-public information provides for an appropriate, principles-based approach to prevent the market abuses Rules 927.3NY and 927.5(f) are designed to address. Specifically, Rule 3(j) requires every Exchange member to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material, non-public information by such member or associated persons. For purposes of this requirement, the misuse of material, non-public information includes, but is not limited to, the following:

- a) trading in any securities issued by a corporation, or in any related securities or related options or other derivative securities, while in possession of material, non-public information concerning that issuer;
- b) trading in a security or related options or other derivative securities, while in possession of material, non-public information concerning imminent transactions in the security or related securities; or
- c) disclosing to another person or entity any material, non-public information involving a corporation whose shares are publicly traded or an imminent transaction in an underlying security or related securities for the purpose of facilitating the possible misuse of such material, non-public information.

Because Specialists and e-Specialists are already subject to the requirements of Rule 3(j), the Exchange does not believe that it is necessary to separately require specific limitations on dealings between Specialists/e-Specialists and their affiliates. Deleting Rule 927.3NY and 927.5NY(f) and requirements for specific procedures would provide Specialists/e-Specialists and ATP Holders with the flexibility to adapt their policies and procedures as appropriate to reflect changes to their business model, business activities, or the securities market in a manner similar to how Market Makers on the Exchange currently operate and consistent with Rule 3(j).

As noted above, Exchange Specialists and e-Specialists are distinguished under Exchange rules from other types of Market Makers only to the extent that Specialists and e-Specialists have heightened obligations and allocation guarantees. However, none of these heightened obligations provides [sic] different or greater access to nonpublic information than any other market participant on the Exchange.⁶ Specifically, whether on the Trading Floor or remotely, neither Specialists nor e-Specialists on the Exchange have access to trading information provided by the Exchange, either at, or prior to, the point of execution, that is not made available to all other market participants on the Exchange in a similar manner. Further, as noted above, Specialists/e-Specialists on the Exchange do not have any agency responsibilities for orders in the Consolidated Book. Accordingly, because Specialists, e-Specialists and Market Makers do not have any trading advantages at the Exchange due to their market role, the Exchange believes that they should be subject to the same rules regarding the protection against the misuse of material non-public information, which in this case, is existing Rule 3(j).⁷

The Exchange notes that its proposed approach to use a principles-based approach to protecting against the misuse of material non-public information for all of its registered market makers is consistent with recent approved rule changes for NYSE Arca Equities, Inc. (“NYSE Arca”), BATS Exchange, Inc.’s (“BATS”), and New York Stock Exchange LLC (“NYSE”) rules

⁶ See Rules 927NY(c) and 927.5NY.

⁷ The Exchange notes that by deleting Rule 927.3NY, the Exchange would no longer require specific information barriers for Specialists or require pre-approval of any information barriers that a Specialist would erect for purposes of protecting against the misuse of material non-public information. However, as is the case today with Market Makers, information barriers of new entrants, including new Specialists, would be subject to review as part of a new firm application. Moreover, the policies and procedures of Specialists and e-Specialists, including those relating to information barriers, would be subject to review by FINRA, on behalf of the Exchange, pursuant to a Regulatory Services Agreement.

governing cash equity market makers on those respective exchanges.⁸ Except for prescribed rules relating to floor-based designated market makers on the NYSE, who have access to specified non-public trading information, each of these exchanges have moved to a principles-based approach to protecting against the misuse of material non-public information. In connection with approving those rule changes, the Commission found that eliminating prescriptive information barrier requirements should not reduce the effectiveness of exchange rules requiring its members to establish and maintain systems to supervise the activities of its members, including written procedures reasonably designed to ensure compliance with applicable federal securities law and regulations, and with the rules of the applicable exchange.⁹

Comparable to members of cash equity markets, the Exchange believes that a principles-based rule applicable to members of options markets would be equally effective in protecting against the misuse of material non-public information. Indeed, Exchange Rule 3(j) is currently applicable to Exchange Market Makers other than Specialists and e-Specialists and already requires all ATP Holders to have policies and procedures reasonably designed to protect against the misuse of material nonpublic information, which is similar to the respective NYSE Arca Equities, BATS and NYSE rules governing cash equity market makers. The Exchange believes

⁸ See Securities Exchange Act Release Nos. 60604 (Sept. 2, 2009), 76 FR 46272 (Sept. 8, 2009) (SR-NYSEArca-2009-78) (Order approving elimination of NYSE Arca rule that required market makers to establish and maintain specifically prescribed information barriers, including discussion of NYSE Arca and Nasdaq rules) (“Arca Approval Order”); 61574 (Feb. 23, 2010), 75 FR 9455 (Mar. 2, 2010) (SR-BATS-2010-003) (Order approving amendments to BATS Rule 5.5 to move to a principles-based approach to protecting against the misuse of material, non-public information, and noting that the proposed change is consistent with the approaches of NYSE Arca and Nasdaq) (“BATS Approval Order”); and 72534 (July 3, 2014), 79 FR 39440 (July 10, 2014), SR-NYSE-2014-12) (Order approving amendments to NYSE Rule 98 governing designated market makers to move to a principles-based approach to prohibit the misuse of material non-public information) (“NYSE Approval Order”).

⁹ See, e.g., BATS Approval Order, *supra* note 8 at 9458.

Rule 3(j) provides appropriate protection against the misuse of material nonpublic information by Specialists and e-Specialists on the Exchange and there is no longer a need for prescriptive information barrier requirements in Rules 927.3NY and 927.5NY(f).

The Exchange notes that even with this proposed rule change, pursuant to Rule 3(j), a Specialist or e-Specialist would still be obligated to ensure that its policies and procedures reflect the current state of its business and continue to be reasonably designed to achieve compliance with applicable federal securities law and regulations, and with applicable Exchange rules, including being reasonably designed to protect against the misuse of material, non-public information. While information barriers would not specifically be required under the proposal, Rule 3(j) already requires that an ATP Holder consider its business model or business activities in structuring its policies and procedures, which may dictate that an information barrier or a functional separation be part of the appropriate set of policies and procedures that would be reasonably designed to achieve compliance with applicable securities law and regulations, and with applicable Exchange rules.

The Exchange further notes that under Rule 3(j), an ATP Holder would be able [sic] structure its firm to provide for its options Specialists, e-Specialists, or Market Makers, as applicable, to be structured with its equities and customer-facing businesses, provided that any such structuring would be done in a manner reasonably designed to protect against the misuse of material, non-public information. For example, pursuant to Rule 3(j), a Specialist on the Exchange could be in the same independent trading unit, as defined in Rule 200(f) of Regulation SHO,¹⁰ as an equities market maker and other trading desks within the firm, including options trading desks, so that the firm could share post-trade information to better manage its risk across

¹⁰ 17 CFR Part 242.200(f).

related securities. The Exchange believes it is appropriate, and consistent with Rule 3(j) and Section 15(g) of the Act¹¹ for a firm to share options position and related hedging position information (e.g., equities, futures, and foreign currency) within a firm to better manage risk on a firm-wide basis. The Exchange notes, however, that if so structured, a firm would need to have appropriate policies and procedures, including information barriers as applicable, to protect against the misuse of material non-public information, and specifically customer information, consistent with Rule 3(j).

The Exchange believes that the proposed reliance on the principles-based Rule 3(j) would ensure that an ATP Holder that operates a Specialist or e-Specialist would be required to protect against the misuse of any material non-public information. As noted above, Rule 3(j) already requires that firms refrain from trading while in possession of material non-public information concerning imminent transactions in the security or related product. The Exchange believes that moving to a principles-based approach rather than prescribing how and when to wall off a Specialist or e-Specialist from the rest of the firm would provide ATP Holders operating Specialists or e-Specialists with appropriate tools to better manage risk across a firm, including integrating options positions with other positions of the firm or, as applicable, by the respective independent trading unit. Specifically, the Exchange believes that it is appropriate for risk management purposes for a member operating a Specialist or e-Specialist to be able to consider both options Specialist/e-Specialist traded positions for purposes of calculating net positions consistent with Rule 200 of Regulation SHO, calculating intra-day net capital positions, and managing risk both generally as well as in compliance with Rule 15c3-5 under the Act (the

¹¹ 15 U.S.C. 78o(g).

“Market Access Rule”).¹² The Exchange notes that any risk management operations would need to operate consistent with the requirement to protect against the misuse of material non-public information.

The Exchange further notes that if Specialists or e-Specialists are integrated with other market making operations, they would be subject to existing rules that prohibit ATP Holders from disadvantaging their customers or other market participants by improperly capitalizing on a member organization’s access to the receipt of material, non-public information. As such, a member organization that integrates its Specialist/e-Specialist operations together with equity market making would need to protect customer information consistent with existing obligations to protect such information. The Exchange has rules prohibiting members from disadvantaging their customers or other market participants by improperly capitalizing on the members’ [sic] access to or receipt of material, non-public information. For example, Rule 320 requires members to establish, maintain, enforce, and keep current a system of compliance and supervisory controls, reasonably designed to achieve compliance with applicable securities laws and Exchange rules. Additionally, Rule 995NY(c) prevents an ATP Holder or person associated with an ATP Holder, who has knowledge of an originating order, a solicited order, or a facilitation order, to enter, based on such knowledge, an order to buy or sell an option on the underlying securities of any option that is the subject of the order, an order to buy or sell the security underlying any option that is the subject of the order, or any order to buy or sell any related instrument unless certain circumstances are met.

The Exchange proposes to make a conforming amendment to remove the section referencing Rule 927.3NY in Rule 927.6NY.

¹² 17 CFR Part 240.15c3-5.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act¹³ in general, and furthers the objectives of Section 6(b)(5) of the Act¹⁴ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Exchange believes that the proposed rule change would remove impediments to and perfect the mechanism of a free and open market by adopting a principles-based approach to permit an ATP Holder operating a Specialist or e-Specialist to maintain and enforce policies and procedures to, among other things, prohibit the misuse of material non-public information and eliminating restrictions on how an ATP Holder structures its Specialist or e-Specialist operations. The Exchange notes that the proposed rule change is based on an approved rule of the Exchange to which Specialists and e-Specialists are already subject – Rule 3(j) – and harmonizes the rules governing Specialists, e-Specialists, and Market Makers. Moreover, ATP Holders operating Specialists and e-Specialists would continue to be subject to federal and Exchange requirements for protecting material non-public order information.¹⁵ The Exchange believes that the proposed rule change would remove impediments to and perfect the mechanism of a free and open market because it would harmonize the Exchange’s approach to protecting against the misuse of material nonpublic information and no longer subject Specialists/e-Specialists to prescriptive requirements. The Exchange does not believe that the existing prescriptive requirements

¹³ 15 U.S.C. § 78f(b).

¹⁴ 15 U.S.C. § 78f(b)(5).

¹⁵ See 15 U.S.C. 78o(g) and Rule 3(j).

applicable to Specialists/e-Specialists are narrowly tailored to their respective roles because neither market participant has access to Exchange trading information in a manner different from any other market participant on the Exchange and they do not have agency responsibilities to the Consolidated Book.

The Exchange further believes the proposal is designed to prevent fraudulent and manipulative acts and practices and to promote just and equitable principles of trade because existing rules make clear to Specialists, e-Specialists and ATP Holders the type of conduct that is prohibited by the Exchange. While the proposal eliminates prescriptive requirements relating to the misuse of material non-public information, Specialists, e-Specialists and ATP Holders would remain subject to existing Exchange rules requiring them to establish and maintain systems to supervise their activities, and to create, implement, and maintain written procedures that are reasonably designed to comply with applicable securities laws and Exchange rules, including the prohibition on the misuse of material, nonpublic information.

The Exchange notes that the proposed rule change would still require that ATP Holders operating Specialists and e-Specialists maintain and enforce policies and procedures reasonably designed to ensure compliance with applicable federal securities laws and regulations and with Exchange rules. Even though there would no longer be pre-approval of Specialist information barriers, any Specialist/e-Specialist written policies and procedures would continue to be subject to oversight by the Exchange and therefore the elimination of prescribed restrictions should not reduce the effectiveness of the Exchange rules to protect against the misuse of material non-public information. Rather, ATP Holders will be able to utilize a flexible, principles-based approach to modify their policies and procedures as appropriate to reflect changes to their business model, business activities, or to the securities market itself. Moreover, while specified

information barriers may no longer be required, an ATP Holder's business model or business activities may dictate that an information barrier or functional separation be part of the appropriate set of policies and procedures that would be reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable Exchange rules. The Exchange therefore believes that the proposed rule change will maintain the existing protection of investors and the public interest that is currently applicable to Specialists and e-Specialists, while at the same time removing impediments to and perfecting a free and open market by moving to a principles-based approach to protect against the misuse of material non-public information.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. To the contrary, the Exchange believes that the proposal will enhance competition by allowing Specialists, e-Specialists and Market Makers to comply with applicable Exchange rules in a manner best suited to their business models, business activities, and the securities markets, thus reducing regulatory burdens while still ensuring compliance with applicable securities laws and regulations and Exchange rules. The Exchange believes that the proposal will foster a fair and orderly marketplace without being overly burdensome upon Specialists and e-Specialists.

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

No written comments were solicited or received with respect to the proposed rule change.

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 up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and

publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the 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 Number SR-NYSEMKT-2015-23 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-NYSEMKT-2015-23. 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 will also be available for inspection and copying at the NYSE's principal office and on its Internet website at www.nyse.com. 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-NYSEMKT-2015-23 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.¹⁶

Brent J. Fields
Secretary

¹⁶ 17 CFR 200.30-3(a)(12).