

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-66503; File No. SR-CHX-2012-02)

March 1, 2012

Self-Regulatory Organizations; Chicago Stock Exchange, Inc.; Order Approving a Proposed Rule Change to Add to and Amend its Rules Regarding the Obligations of Institutional Brokers Registered with the Exchange

I. Introduction

On January 6, 2012, the Chicago Stock Exchange, Inc. (“CHX” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to permit broker-dealers registered as Institutional Brokers with CHX to operate a non-Institutional Broker unit within the same Participant Firm. The proposed rule change was published for comment in the Federal Register on January 24, 2012.³ The Commission received no comment letters on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

Institutional Brokers are an elective sub-category of Exchange Participants who are subject to the obligations of Article 17 of the CHX rules. Registration as an Institutional Broker is limited to Participant Firms, and is not available to individual persons.⁴ Under current CHX rules, each individual person authorized to enter bids and offers and execute transactions on behalf of an Institutional Broker is considered an Institutional Broker Representative (“IBR”) and must be registered with the Exchange as provided in Article 6.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Securities Exchange Act Release No. 66177 (January 18, 2012), 77 FR 3527 (“Notice”).

⁴ See CHX Rules, Article 17, Rule 1, Interpretation and Policy .02.

Institutional Brokers are the successors to the floor brokers that operated within the Exchange's previous floor-based, auction trading model. The Exchange replaced its floor-based, auction trading model with its New Trading Model, which features an electronic limit order matching system as its core trading facility ("Matching System"), beginning in late 2006.⁵ Under CHX's New Trading Model, Institutional Brokers were regarded as operating on the Exchange.⁶ Recently, the Exchange amended its rules to provide that Institutional Brokers are no longer considered to be operating on the Exchange.⁷ Given this change in the status of Institutional Brokers, the Exchange stated that the instant proposal is designed to enable Institutional Brokers to engage in business activities beyond those handled by IBRs, such as over-the-counter ("OTC") market making, while ensuring that their activities as an Institutional Broker are appropriately governed by CHX rules.

The Exchange proposed to permit Institutional Brokers to operate a non-Institutional Broker unit within the same Participant Firm. A firm registered with the Exchange as Institutional Broker could maintain other lines of business separate and distinct from its Institutional Broker activities without subjecting those other areas to the requirements of Article 17, Rule 3 contingent upon the creation and maintenance of effective information barrier procedures as specified in proposed Rule 6 of Article 17. The Exchange stated that non-IBR activities of a Participant Firm registered as an Institutional Broker would remain subject to all other applicable provisions of the Exchange's rules.⁸ The non-IBR personnel at an Institutional

⁵ See Securities Exchange Act Release No. 54550 (September 29, 2006), 71 FR 59563 (October 10, 2006) (SR-CHX-2006-05).

⁶ See id.

⁷ See Securities Exchange Act Release No. 65633 (October 26, 2011), 76 FR 67509 (November 1, 2011) (SR-CHX-2011-29).

⁸ See Notice, 77 FR at 3529.

Broker could continue to send orders to the Exchange, but those orders would be regarded as standard order-sending Participant orders, not as Institutional Broker activity. The Exchange stated that it can and will distinguish between orders sent to the Matching System by IBRs and other orders sent by Institutional Brokers to the Matching System for billing and other purposes.⁹

CHX proposed to modify its rules correspondingly to redefine IBR¹⁰ and “Participant Firm,”¹¹ and amend the obligations of Institutional Brokers and IBRs.¹² Certain Institutional Broker privileges and responsibilities would apply only to the activities of those individuals registered with the Exchange as IBRs (and clerks thereto).¹³ Further, the Exchange proposed to correct typographical mistakes and to make clarifying changes.

⁹ See id.

¹⁰ See Article 1, new Rule 1(gg) (defining IBR). See also amended Interpretation and Policy .02 to Article 17, Rule 1 (redefining IBR as an individual person affiliated with an Institutional Broker who is authorized to accept orders, enter bids and offers and execute transactions on behalf of an Institutional Broker and who has registered with the Exchange as an IBR as provided in Article 6).

¹¹ See Article 17, revised Rule 2 (clarifying that only Participants Firms are eligible to register as Institutional Brokers).

¹² See Article 17, Rule 3(e) (the obligations owed by Institutional Brokers under Article 11 include the affirmative obligation to provide electronic information to the Exchange in certain circumstances); Interpretation and Policy .01(a) to Article 6, Rule 3 (all applicants seeking to register as IBRs must successfully complete an Institutional Broker exam);

¹³ See amended Article 17, Rule 3 (enumerated Institutional Broker responsibilities apply to activities by or through an affiliated IRR); amended Article 17, Rule 5(a) (the ability to make clearing submissions is limited to IBRs); new Article 17, Rule 6 (creating a duty of Institutional Brokers with a non-Institutional Broker unit to establish and maintain information barriers between the Institutional Broker unit and non-Institutional Broker unit); amended Article 17, Rule 1 (only registered IBRs are permitted to use Exchange systems provided for Institutional Brokers for handling orders and reporting transactions, i.e., Brokerplex[®]). For a description of Brokerplex[®], see Notice, 77 FR at 3528, n.9.

III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.¹⁴ Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,¹⁵ in that it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transaction in securities, to remove impediments and perfect the mechanisms of a free and open market, and, in general, to protect investors and the public interest.

As noted above, the Exchange recently amended its rules to provide that Institutional Brokers are no longer deemed to be operating on the Exchange.¹⁶ Accordingly, Institutional Brokers are now permitted to handle and execute orders otherwise than on the Exchange.¹⁷ Given this change, the Commission believes that it is appropriate and consistent with the Act for the Exchange to alter the privileges and responsibilities of Institutional Brokers to apply only to the activities of IBRs (and their clerks). The proposed changes would allow Institutional Brokers to carry out business strategies similar to those of other participants on the Exchange, while still ensuring that persons acting as IBRs are subject to the appropriate regulatory obligations. Further, the proposed rules regarding information barrier procedures should help ensure that there are adequate safeguards to prevent IBR units and non-IBR units from sharing non-public market information. As it gains experience overseeing the new multi-unit Institutional Brokers,

¹⁴ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁵ 15 U.S.C. 78f(b)(5).

¹⁶ See supra note 7.

¹⁷ See id.

the Commission expects the Exchange to assess whether any other informational barriers are necessary to prevent the flow of market information between IBR units and non-IBR units.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁸ that the proposed rule change (SR-CHX-2012-02) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁹

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Deputy Secretary

¹⁸ 15 U.S.C. 78s(b)(2).

¹⁹ 17 CFR 200.30-3(a)(12).