

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34 - 78555; File No. SR-IEX-2016-12)

August 11, 2016

Self-Regulatory Organizations: Investors Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Conform Rules 3.260(d) and 5.110(e) to Corresponding Rules of the Financial Industry Regulatory Authority

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 August 9, 2016, the Investors Exchange LLC (“IEX” or the “Exchange”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I and II 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”) a proposed rule change to conform Rule 3.260(d) and 5.110(e) to corresponding rules of the Financial Industry Regulatory Authority (“FINRA”). The Exchange has designated

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.

this proposal as “non-controversial” and provided the Commission with the notice required by Rule 19b-4(f)(6)(iii) under the Act.⁶

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 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

Pursuant to Rule 17d-2 under the Act,⁷ and subject to Commission approval, the Exchange and FINRA has entered into an agreement to allocate regulatory responsibility for common rules (the “17d-2 Agreement”).⁸ The 17d-2 Agreement covers common members of the Exchange and FINRA and allocates to FINRA regulatory responsibility, with respect to common members, for the following: (i) examination of common members of the Exchange and FINRA for compliance with certain federal securities

⁶ 17 CFR 240.19b-4(f)(6)(iii).

⁷ 17 CFR 240.17d-2

⁸ See Securities Exchange Act Release No. 78434 (July 28, 2016) (File No. 4-700).

laws, rules and regulations and rules of the Exchange that the Exchange certifies are identical or substantially similar to FINRA rules; (ii) investigation of common members of the Exchange and FINRA for violations of certain federal securities laws, rules and regulations, or Exchange rules that the Exchange certifies as identical or substantially identical to a FINRA rule; and (iii) enforcement of compliance by common members with certain federal securities laws, rules and regulations, and the rules of the Exchange that the Exchange certifies as identical or substantially similar to FINRA rules.

The 17d-2 Agreement will include a certification by the Exchange that states that the requirements contained in certain Exchange rules are identical to, or substantially similar to, certain FINRA rules that have been identified as comparable. To conform to comparable FINRA rules for the purposes of the 17d-2 Agreement, as well as to make changes that IEX believes are appropriate, the Exchange proposes to amend Exchange Rules 3.260(d) and 5.110(e) to harmonize with FINRA Rules as described below.

IEX Rule 3.260

IEX Rule 3.260 governs discretionary accounts and contains certain prohibitions and requirements as follows:

- (a) Excessive Transactions – The rule prohibits a Member from effecting purchase or sale transactions in a customer’s account, with respect to which such member (or its agent or employee) has discretion, which are excessive in size or frequency in view of the financial resources and character of such account.
- (b) Authorization and Acceptance of Account – The rule provides that no Member or Registered Representative shall exercise any discretionary power in a customer's account unless such customer has given prior written authorization to a stated individual or individuals and the account has been accepted by the Member, as evidenced in writing by the Member or the

partner, officer or manager, duly designated by the Member, in accordance with IEX Rule 5.110.

- (c) Approval and Review of Transactions – The rule provides that the Member or the person duly designated shall approve promptly in writing each discretionary order entered and shall review all discretionary accounts at frequent intervals in order to detect and prevent transactions which are excessive in size or frequency in view of the financial resources and character of the account.
- (d) Exceptions – The rule provides an exception for discretion as to the price at which or the time when an order given by a customer for the purchase or sale of a definite amount of a specified security shall be executed, except that the authority to exercise time and price discretion will be considered to be in effect only until the end of the business day on which the customer granted such discretion, absent a specific, written contrary indication signed and dated by the customer. This limitation shall not apply to time and price discretion exercised in an institutional account, as defined in IEX Rule 5.110 pursuant to valid Good-Till-Canceled instructions issued on a "not-held" basis. Any exercise of time and price discretion must be reflected on the order ticket.

IEX Rule 3.260 is identical to NASD Rule 2510 (which is a FINRA rule) except that paragraph (d) of the IEX rule does not contain an exception contained in NASD Rule 2510(d) for bulk exchanges at net asset value of money market mutual funds utilizing negative response letters provided the bulk exchange is limited to situations involving mergers and acquisitions of funds, changes of clearing members and exchange of funds used in sweep accounts, the negative response letter contains a tabular comparison of the nature and amount of the fees charged by each fund, the negative response letter contains a comparative description of the investment objectives of each fund and a prospectus of the fund to be purchased, and the negative response feature will not be activated until at least 30 days after the date on which the letter was mailed.

To harmonize IEX Rule 3.260 with NASD Rule 2510, the Exchange proposes to adopt an identical exception for bulk transfers as is contained in NASD Rule 2510(d) so that it may be incorporated into the 17d-2 Agreement in its entirety. The exception was added to NASD rules in 1992 in order to eliminate an obstacle to the efficient and timely execution of bulk exchanges of money market mutual funds in the situations set forth in NASD Rule 2510. In Notice to Members 93-1 announcing the rule change,⁹ the NASD explained the reason for adoption of the exception as follows:

“The NASD recognized that it is often necessary to notify hundreds and, sometimes, several thousand money market mutual fund share-owners of an impending fund exchange. It may be an extremely difficult, if not impossible, administrative task to contact each non-replier and solicit approval of the fund exchange. At best, contacting individuals for approval results in considerable delays and added cost. The NASD determined that, by eliminating an obstacle to the efficient and timely execution of such bulk exchanges, where customers are at little or no risk, customers and NASD members would benefit.”

Although such bulk transfers cannot be effected on the Exchange, IEX believes it is appropriate to include the exception provided in NASD Rule 2510(d) to eliminate the obstacles and provide the benefits identified by the NASD in adopting the exception, as well as to enable incorporation of IEX Rule 3.260 into the 17d-2 Agreement in its entirety. Incorporating the exception into IEX Rule 3.260 would provide appropriate flexibility to allow IEX Members to perform bulk exchanges in the limited situations specified in the rule in an efficient manner that is designed to protect investors and the

⁹ See http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=1638.

public interest. Absent the exception, IEX Members would technically be prohibited from effecting bulk transfers in the manner permitted by FINRA rules.¹⁰

IEX Rule 5.110(e)

IEX Rule 5.110(e) governs the responsibility of an IEX Member to investigate applicants for registration, including that “...each member shall establish and implement written procedures reasonably designed to verify the accuracy and completeness of the information contained in an applicant’s Form U4¹¹ no later than 30 calendar days after the form is filed with IEX.” The rule is substantially identical to FINRA Rule 3110(e) except that in the sentence quoted above, FINRA Rule 3110(e) specifies that the verification requirement applies only to an applicant’s initial or transfer Form U4.¹² The Exchange inadvertently omitted the “initial or transfer” language in Rule 5.110(e). The Exchange proposes to harmonize IEX Rule 5.110(e) with FINRA Rule 3110(e) by adding the omitted language contained in the FINRA rule in order to clarify the requirement,

¹⁰ Each IEX Member subject to IEX Rule 3.260 is required to be a FINRA member, pursuant to Section 15(b)(8) of the Act, since the rule relates to customer accounts and the Member would thus be ineligible for the exemption provided in Rule 15b9-1 under the Act.

¹¹ Form U4 is the Uniform Application for Securities Industry Registration or Transfer which must be used by representatives of broker-dealers, among other entities, to become registered in the appropriate jurisdictions and/or SROs. Both FINRA and IEX, as well as all other national securities exchanges, require representatives of broker-dealer members to register on Form U4.

¹² In its proposed rule filing to adopt FINRA Rule 3110 in its current form, FINRA stated that the term “initial Form U4” refers to the Form U4 filing required when an individual is registering with a FINRA member for the first time, including in the context of dual registration, or is registering with a FINRA member after more than two years have passed since the individual was last registered with a FINRA member. The term “transfer Form U4” refers to the Form U4 filing required when a registered person transfers from one FINRA member to another FINRA member. (See, SR-FINRA-2014-038). Since FINRA administers the Form U4 filing process in its CRD system, in part on behalf of IEX, the Exchange would apply the same meanings in the application of Rule 5.110(e).

avoid confusion to IEX Members in applying the relevant provision, and enable Rule 5.110 to be incorporated into the 17d-2 Agreement in its entirety. Adding the omitted language will make clear to IEX Members that the verification requirement does not apply to updates or amendments to a registered person's Form U4¹³ if such filing is not an initial or transfer Form U4. IEX believes that in determining to require verification for initial and transfer Forms U4, FINRA imposes an appropriate requirement consistent with public interest and investor protection concerns in that FINRA requires verification at key times in a registered person's employment. In this regard, IEX notes that FINRA has substantial expertise administering the CRD system and overseeing its members (and those of its client national securities exchanges) Form U4 reporting obligations.

Accordingly, IEX believes that it is appropriate to harmonize with FINRA's approach on what triggers should be required for Members to verify the accuracy and completeness of Form U4 information for their registered personnel, and that the triggers are consistent with investor protection and the public interest. Moreover, for IEX Members that are also FINRA members, the proposed change will align IEX rules with FINRA rules thereby alleviating potential confusion.

2. Statutory Basis

IEX believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,¹⁴ in general and furthers the objectives of Sections 6(b)(5) of the

¹³ The instructions to the Form U4, state that the "individual is under a continuing obligation to amend and update information required by Form U4 as changes occur." See, Form U4 Uniform Application for Securities Industry Registration or Transfer, available at <http://www.finra.org/sites/default/files/AppSupportDoc/p015111.pdf>.

¹⁴ 15 U.S.C. 78f.

Act,¹⁵ 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, and 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.

With respect to the proposed change to add an exception to Rule 3.260 to permit bulk transfers under the specified circumstances, the Exchange believes that the exception is consistent with Section 6(b)(5) of the Act¹⁶ because the exception is narrowly drawn and includes protections designed to help prevent fraudulent and manipulative acts and protect investors and the public interest. The exception is limited to situations involving mergers and acquisitions of funds, changes of clearing members and exchange of funds used in sweep accounts. The Exchange does not believe that these situations raise concerns regarding abuse of discretion in customer accounts by the Member, but rather are more administrative in nature. In addition, and as described above, the exception to permit negative response letters in lieu of prior written authorization from customers for bulk exchanges includes four requirements that are designed to protect customers – the negative response letter must contain a tabular comparison of the nature and amount of the fees charged by each fund, the negative response letter must contain a comparative description of the investment objectives of each fund, a prospectus of the fund to be purchased must be included with the negative response letter, and the negative response feature may not be activated until at least 30 days after the date on which the letter was mailed. These protections provide relevant

¹⁵ 15 U.S.C. 78f(b)(5).

¹⁶ 15 U.S.C. 78f(b)(5).

disclosures to customers regarding the bulk exchange and 30 days to potentially contact the Member to object to the exchange. Based on these considerations, IEX believes it is appropriate to include the exception provided in NASD Rule 2510(d) to eliminate the obstacles and provide the benefits identified by the NASD in adopting the exception. Incorporating the exception into IEX Rule 3.260 would provide appropriate flexibility to allow IEX Members to perform bulk exchanges in the limited situations specified in the rule in an efficient manner that is designed to protect investors and the public interest, as well as to remove impediments to and perfect the mechanism of a free and open market and a national market system.

Further, as noted above, each IEX Member subject to Rule 3.260 must also be a FINRA member. In this regard, the Exchange believes that the proposed rule change will further the objectives of Section 6(b)(5) of the Act¹⁷ by providing greater harmonization between IEX and FINRA rules of similar purpose, enable IEX to incorporate IEX Rule 3.260 in its entirety into the pending 17d-2 Agreement between the Exchange and FINRA (subject to SEC approval), resulting in less burdensome and more efficient regulatory compliance. As such, the proposed rule change would foster cooperation and coordination with persons engaged in facilitating transactions in securities and would remove impediments to and perfect the mechanism of a free and open market and a national market system in accordance with Section 6(b)(5) of the Act.¹⁸

IEX believes that the proposed change to Rule 5.110(e) is consistent with Section 6(b)(5) of the Act¹⁹ because it will serve to correct an inadvertent omission in the rule

¹⁷ 15 U.S.C. 78f(b)(5).

¹⁸ 15 U.S.C. 78f(b)(5).

¹⁹ 15 U.S.C. 78f(b)(5).

thereby clarifying the applicable verification requirement for IEX Members. As discussed above in the Purpose section, IEX believes that the FINRA Form U4 verification requirements are designed to protect investors and the public interest by requiring verification at key times in a registered person's employment. In addition, and as noted above, FINRA has substantial expertise administering the CRD system and overseeing its members (and those of its client national securities exchanges) Form U4 reporting obligations through SEC approved rules.²⁰ Accordingly, IEX believes that the proposed rule change would further the objectives of Section 6(b)(5) of the Act²¹ by imposing appropriately balanced Form U4 verification requirements that are designed to prevent fraudulent and manipulative acts and practices and to promote just and equitable principles of trade. Further, the Exchange believes that providing greater harmonization between IEX and FINRA rules of similar purpose will result in less burdensome and more efficient regulatory compliance for IEX Members that are also FINRA members, and facilitate FINRA's performance of its regulatory performance under the pending 17d-2 Agreement (subject to SEC approval), thereby removing impediments to and perfecting the mechanism of a free and open market and a national market system, consistent with the objectives of Section 6(b)(5). In addition, alignment of IEX rules with FINRA rules will alleviate any confusion among market participants regarding the applicable verification requirements, including for IEX Members that are not FINRA members.

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

²⁰ See Release No. 34-73966, File No. SR-FINRA-2014-038 (December 30, 2014); 80 FR 546 (January 6, 2015).

²¹ 15 U.S.C. 78f(b)(5).

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, as amended. The proposed rule change is not designed to address any competitive issues but rather to provide greater harmonization among Exchange and FINRA rules of similar purpose, resulting in less burdensome and more efficient regulatory compliance for common members and facilitating FINRA's performance of its regulatory performance on the pending 17d-2 Agreement (subject to SEC approval). Moreover, harmonization of the specified IEX's rules with FINRA rules will promote competition by removing disparate requirements between IEX Members and FINRA members.

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

The Exchange has designated this rule filing as non-controversial under Section 19(b)(3)(A)²² of the Act and Rule 19b-4(f)(6)²³ thereunder. Because the foregoing rule 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 if consistent with the protection of investors and the public interest, provided that the self-regulatory organization has given 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

²² 15 U.S.C. 78s(b)(3)(A).

²³ 17 CFR 240.19b-4(f)(6).

such shorter time as designated by the Commission,²⁴ the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act²⁵ and Rule 19b-4(f)(6) thereunder.²⁶

A proposed rule change filed under Rule 19b-4(f)(6)²⁷ normally does not become operative prior to 30 days after the date of the filing. However, pursuant to Rule 19b-4(f)(6)(iii),²⁸ the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the Exchange may harmonize its rules with FINRA to coincide with IEX's launch of exchange operations during a security-by-security phase-in period scheduled to begin on August 19, 2016. The Exchange represents that the proposed changes do not present any new or novel issues as IEX is harmonizing these two rules to the comparable rules of FINRA. The Exchange also represents that further harmonizing them now will allow them to coincide with the recently effective bilateral 17d-2 plan, which should reduce burdens on members while the increased coordination should promote investor protection. Because IEX's proposal does not raise any new or novel issues and seeks only to harmonize two IEX rules to the corresponding rules of FINRA that are covered by the FINRA-IEX bilateral 17d-2 plan, the Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest because it will allow IEX to update those

²⁴ The Exchange has fulfilled this requirement.

²⁵ 15 U.S.C. 78s(b)(3)(A).

²⁶ 17 CFR 240.19b-4(f)(6).

²⁷ 17 CFR 240.19b-4(f)(6).

²⁸ 17 CFR 240.19b-4(f)(6)(iii).

two rules to coincide with the operation of the bilateral 17d-2 plan, which the Commission recently declared effective, as IEX begins operations as an exchange.²⁹

At any time within 60 days of the filing of the 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. If the Commission takes such action, the Commission shall institute proceedings under Section 19(b)(2)(B)³⁰ of the Act to determine whether the proposed rule change should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the 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 email to rule-comments@sec.gov. Please include File Number SR-IEX-2016-12 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.

²⁹ For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

³⁰ 15 U.S.C. 78s(b)(2)(B).

All submissions should refer to File Number SR-IEX-2016-12. This file number should be included in the subject line if email 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, D.C. 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 IEX's principal office and on its Internet website at www.iextrading.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-IEX-

2016-12 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.³¹

Robert W. Errett
Deputy Secretary

³¹ 17 CFR 200.30-3(a)(12).