SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-80223; File No. SR-IEX-2016-18)

March 13, 2017

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

I. Introduction

On November 29, 2016, the Investors Exchange LLC (“Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) and Rule 19b-4 thereunder, a proposed rule change to: (i) amend IEX Rules 11.190(a)(3) and 11.190(b)(8) to modify the operation of the primary peg order type; (ii) amend IEX Rule 11.190(h)(3)(C)(ii) and (D)(ii) regarding price sliding in locked and crossed markets to modify the price sliding process for both primary peg orders and discretionary peg orders resting on or posting to the IEX order book; and (iii) make minor technical changes to conform certain terminology. The proposed rule change was published for comment in the Federal Register on December 13, 2016. On January 26, 2017, pursuant to Section 19(b)(2) of the Act, the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute

proceedings to determine whether to approve or disapprove the proposed rule change.\textsuperscript{5} The Commission received no comment letters on the proposed rule change. This order approves the proposed rule change.

II. \textit{Description of the Proposal}

\textbf{Primary Peg Order Type Functionality}

The Exchange has proposed to amend Rules 11.190(a)(3) and 11.190(b)(8) to modify the operation of the primary peg order type offered by the Exchange. Currently, a primary peg order is a non-displayed order that the Exchange system automatically adjusts (upon entry and when posting to the Exchange order book) to be equal to and ranked at the less aggressive of the near-side primary quote (\textit{i.e.}, the national best bid ("NBB") for buy orders and the national best offer ("NBO") for sell orders) or the order’s limit price, if any.\textsuperscript{6} While resting on the Exchange’s order book, the order is automatically adjusted by the system in response to changes in the NBB (NBO) for buy (sell) orders up (down) to the order’s limit price, if any.\textsuperscript{7}

Under the proposal, the operation of the primary peg order type would be amended such that the Exchange system would automatically adjust a primary peg order, upon entry and when the order is posting to the Exchange order book, to be equal to and ranked at the less aggressive of one (1) minimum price variant ("MPV") less aggressive than the primary quote (\textit{i.e.}, one MPV below (above) the NBB (NBO) for buy (sell) orders) or the order’s limit price, as

\textsuperscript{5} See Securities Exchange Act Release No. 79883, 82 FR 9083 (February 2, 2017). The Commission designated March 13, 2017 as the date by which the Commission shall approve or disapprove, or institute proceedings to determine whether to approve or disapprove, the proposed rule change.

\textsuperscript{6} See Rules 11.190(a)(3) and (b)(8); see also Notice, \textit{supra} note 3, at 90035.

\textsuperscript{7} See \textit{id}. 

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The primary peg order would continue to be a non-displayed order type, and the Exchange’s system would continue to automatically adjust a primary peg order in response to changes in the NBB (NBO) for buy (sell) orders up (down) to the order’s limit price, if any.\(^8\)

In addition, under the proposal, in order to meet the limit price of active orders on the Exchange order book, a primary peg order would be able to exercise price discretion from its resting price to a discretionary price (defined as the primary quote), except during periods of quote instability as defined in Rule 11.190(g)\(^10\) or where the primary peg order is resting at its limit price.\(^11\)

Specifically, as set forth in proposed Rule 11.190(b)(8)(K), if the Exchange system were to determine the NBB for a particular security to be an unstable quote in accordance with

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\(^8\) See proposed Rules 11.190(a)(3) and (b)(8); see also Notice, supra note 3, at 90036. In its proposal, the Exchange noted that the BATS BZX exchange’s primary pegged order type has an offset feature that allows primary pegged orders on that exchange to rest more passively than the primary quote. See Notice, supra note 3, at 90036-37.

\(^9\) See proposed Rules 11.190(a)(3) and 11.190(b)(8). The Exchange has not proposed to amend the order modifiers and parameters currently applicable to primary peg orders as set forth in Rule 11.190(b)(8)(A)-(J), and such order modifiers and parameters would continue apply to the amended primary peg order type. See Notice, supra note 3, at 90037 and n.13.

\(^10\) As set forth in Rule 11.190(g), the Exchange utilizes real time relative quoting activity of protected quotations and a proprietary mathematical calculation (the “quote instability calculation”) to assess the probability of an imminent change to the current protected NBB to a lower price or protected NBO to a higher price for a particular security (“quote instability factor”). See Rule 11.190(g); see also Notice, supra note 3, at 90036 n.12. When the quoting activity meets predefined criteria and the quote instability factor calculated is greater than the Exchange’s defined threshold (“quote instability threshold”), the system treats the quote as not stable (“quote instability” or “crumbling quote”). See id. During all other times, the quote is considered stable (“quote stability”). The system independently assesses the quote stability of the protected NBB and protected NBO for each security. See id. When the system determines that a quote, either the protected NBB or the protected NBO, is unstable, the determination remains in effect at that price level for ten (10) milliseconds. See id. The system will only treat one side of the protected NBBO as unstable in a particular security at any given time. See id.

\(^11\) See proposed Rules 11.190(a)(3) and (b)(8). In its proposal, the Exchange represented that the manner in which a primary peg order would exercise discretion is similar to the manner in which the Exchange’s discretionary peg order exercises discretion. See Notice, supra note 3, at 90036.
Rule 11.190(g), it would restrict buy primary peg orders in that security from exercising price discretion to trade against interest at the NBB (and thus they would be executable only at their resting price one MPV less aggressive than the NBB, subject to any limit price); likewise, if the Exchange system were to determine the NBO for a particular security to be an unstable quote in accordance with Rule 11.190(g), it would restrict sell primary peg orders in that security from exercising price discretion to trade against interest at the NBO (and thus they would be executable only at their resting price one MPV less aggressive than the NBO, subject to any limit price).\textsuperscript{12}

Further, as proposed, when exercising price discretion, a primary peg order would maintain its time priority position among non-displayed orders (and behind any displayed orders) at its resting price and would be prioritized behind any non-displayed (and displayed) interest resting at the discretionary price for the duration of that book processing action.\textsuperscript{13} If multiple primary peg orders were to exercise price discretion during the same book processing action, they would maintain their relative time priority at the discretionary price.\textsuperscript{14}

According to the Exchange, the primary peg order type, as proposed, is designed to offer Exchange members an opportunity to rest orders one MPV less aggressive than the primary quote but remain eligible to exercise price discretion up (down) to the NBB (NBO) for buy (sell) orders, and to protect such orders from unfavorable executions by preventing the exercise of

\textsuperscript{12} See proposed Rule 11.190(b)(8)(K).

\textsuperscript{13} See proposed Rule 11.190(b)(8); see also Notice, supra note 3, at 90036. Displayed orders have precedence over non-displayed orders at a given price level in the IEX order book. See Rule 11.220(a)(1)(B).

\textsuperscript{14} See proposed Rule 11.190(b)(8); see also Notice, supra note 3, at 90036. In its proposal, the Exchange represented that the proposed priority rules for the primary peg order are identical to those for the Exchange’s discretionary peg order. See Notice, supra note 3, at 90037.
such price discretion when the Exchange has determined that the market is moving against the
order (i.e., a crumbling quote is detected).\textsuperscript{15}

**Price Sliding in Locked or Crossed Markets**

The Exchange also has proposed to amend Rule 11.190(h)(3)(C)(ii) and (D)(ii) regarding
the price sliding process for both primary peg and discretionary peg orders in locked and crossed
markets. Currently, in the event the NBBO becomes locked or crossed, primary peg and
discretionary peg orders resting on or posting to the order book are priced to the less aggressive
of either: (i) the prior non-locked or non-crossing near side quote (i.e., the prior unlocked or
uncrossed NBB (NBO) for buy (sell) orders), or (ii) one MPV less aggressive than the locking or
crossing price.\textsuperscript{16} Under the proposal, the first alternative under the current rule would be
eliminated such that in locked or crossed markets, primary peg and discretionary peg orders
would slide to one MPV less aggressive than the locking or crossing price rather than remaining
at the prior non-locked or non-crossed price when such price is less aggressive.\textsuperscript{17}

Specifically, proposed Rule 11.190(h)(3)(C)(ii) would provide that in the event the
market becomes locked, primary peg orders and discretionary peg orders resting on or posting to
the order book would be priced one MPV less aggressive than the locking price.\textsuperscript{18} Proposed
Rule 11.190(h)(3)(D)(ii) would provide that in the event that the market becomes crossed,
primary peg orders and discretionary peg orders resting on or posting to the order book would be
priced one MPV less aggressive than the crossing price, i.e., the lowest protected offer for buy

\textsuperscript{15} See Notice, supra note 3, at 90036.

\textsuperscript{16} See Rule 11.190(h)(3)(C)(ii) and (D)(ii); see also Notice, supra note 3, at 90035-36.

\textsuperscript{17} See proposed Rule 11.190(h)(3)(C)(ii) and (D)(ii); see also Notice, supra note 3, at 90036.

\textsuperscript{18} See proposed Rule 11.190(h)(3)(C)(ii).
orders and the highest protected bid for sell orders, before posting.\textsuperscript{19} In addition, proposed Rule 11.190(h)(3)(D)(ii) would specify that if a primary peg order is submitted to the Exchange while the market is crossed, the order would post to the order book priced one MPV less aggressive than the crossing price.\textsuperscript{20} In its proposal, the Exchange noted that its goal with respect to its rules for price sliding primary peg and discretionary peg orders in locked or crossed markets is to ensure that such orders do not rest at locking or crossing prices.\textsuperscript{21}

**Technical Change**

Lastly, the Exchange has proposed to make a technical change to Rule 11.190(h)(3)(D)(ii) to refer to the “crossing price” rather than the “crossed quote” in order to be consistent with other references within the rule.\textsuperscript{22}

### III. Discussion and Commission Findings

After careful review, 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.\textsuperscript{23} In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,\textsuperscript{24} which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect

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\textsuperscript{19} See proposed Rule 11.190(h)(3)(D)(ii).

\textsuperscript{20} See id.; see also Notice, supra note 3, at 90036-37.

\textsuperscript{21} See Notice, supra note 3, at 90037.

\textsuperscript{22} See proposed Rule 11.190(h)(3)(D)(ii); see also Notice, supra note 3, at 90037.

\textsuperscript{23} 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)

\textsuperscript{24} 15 U.S.C. 78f(b)(5)
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 has described the proposed amendments to its primary peg order type as combining an offset feature offered by another exchange that allows primary pegged orders on that exchange to rest more passively than the primary quote, with the discretionary feature of the Exchange’s discretionary peg order type.\(^{25}\) As noted above, according to the Exchange, its amended primary peg order type would be designed to enable a member (or customer thereof) to rest non-displayed trading interest on the Exchange order book at a price inferior to the primary quote and remain available to execute against an incoming order seeking to cross the spread and execute at prices equal to or more aggressive (from the taker’s perspective) than such quote, while minimizing adverse selection to the poster (if its resting order were to “jump” to the primary quote) when the market appears to be moving against the resting primary peg order (i.e., moving lower in the case of a buy order or higher in the case of a sell order).\(^{26}\) The Exchange believes that adding to its primary peg order type both an offset feature and the discretionary functionality that currently is applied to the discretionary peg order type would incentivize members and their customers to post more passive resting liquidity on the Exchange that is priced to execute at the primary quote during periods of quote stability, and consequently may result in greater execution opportunities at the far side quote for members entering spread-crossing orders.\(^{27}\)

The Commission does not believe that the Exchange’s proposed amendments to its primary peg order type raise any novel issues that the Commission has not previously

\(^{25}\) See Notice, supra note 3, at 90036-37.

\(^{26}\) See id.

\(^{27}\) See Notice, supra note 3, at 90036.
considered, and notes in this regard that the Commission received no comments on the Exchange’s proposed rule change. The Commission’s approval of IEX’s Form 1 application included, among other things, approval of IEX’s discretionary peg order type, which utilizes the same discretionary feature (though a different discretionary price) that the Exchange proposes to apply to its primary peg order type.\textsuperscript{28} As with the Exchange’s discretionary peg order type, the amended primary peg order type would be eligible to exercise price “discretion” to move itself to a price that is more aggressive than its resting/ranked price (subject to the constraints of a limit price, if any), except during periods of “quote instability” as defined in Rule 11.190(g).\textsuperscript{29} Rule 11.190(g) sets forth the formula that the Exchange utilizes for determining quote stability for purposes of exercising discretion to move a resting order to a more aggressive price, and is the same formula that the Exchange already utilizes for the quote stability determinations relative to its discretionary peg order type.\textsuperscript{30} In the IEX Form 1 Approval, the Commission stated that Rule 11.190(g) delineates the specific conditions under which IEX discretionary peg orders are eligible to exercise discretion by setting forth the mathematical formula that IEX uses to determine quote stability.\textsuperscript{31} The Commission believes that, as with the Exchange’s discretionary peg order, the Exchange has set forth in its rule the totality of the discretionary feature of the proposed primary peg order type, and that it is hardcoded conditionality based on pre-

\begin{footnotesize}
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\item See proposed Rule 11.190(b)(8); Rule 11.190(b)(10). See also Notice, supra note 3, at 90036. In addition, as the Exchange has noted, the priority scheme that would be applied to the proposed primary peg order when it exercises discretion is identical to that applied to the Exchange’s discretionary peg order when it exercises discretion. See proposed Rule 11.190(b)(8); Rule 11.190(b)(10). See also Notice, supra note 3, at 90037.
\item Compare proposed Rule 11.190(b)(8) and Rule 11.190(b)(10).
\item See IEX Form 1 Approval, supra note 28, at 41153.
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determined, objective factors. In addition, as the Commission observed in the IEX Form 1 Approval, other exchanges offer both discretion and pegging functionalities, including the combination of both of those functionalities in a single order type, and thus an order type that offers both discretion and pegging features is not novel.

Importantly, the Commission notes that the Exchange’s amended primary peg order type would remain a non-displayed order type, like all of the Exchange’s pegged order types, including the discretionary peg order type. Thus, the proposed amended primary peg order type, with its added discretionary and crumbling quote determination functionalities, should not impact the Exchange’s dissemination of a protected quotation, which must be displayed, or market participants’ ability to execute against the Exchange’s protection quotation, and does not appear otherwise designed to impede the mechanism of a free and open market. Accordingly, the Commission believes that the proposed amendments to the Exchange’s primary peg order type are consistent with the Act and, in particular, the Section 6(b)(5) requirement that a national securities exchange’s rules be designed to promote just and equitable principles of trade, remove

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32 See proposed Rule 11.190(b)(8) and Rule 11.190(g); see also IEX Form 1 Approval, supra note 28, at 41153.

33 See IEX Form 1 Approval, supra note 28, at 41153; see also, e.g., Nasdaq Rule 4703(g); NYSE Arca Equities Rule 7.31P(h)(3). In addition, as the Exchange has noted, primary pegged orders on other exchanges may be pegged to prices less aggressive than the near-side primary quote. See Notice, supra note 3, at 90036-37; see also, e.g., BZX Rule 11.9(c)(8)(A).

34 See Rules 11.190(a)(3) and (b)(8)(H). The Commission also notes that primary pegged orders on other exchanges may be non-displayed. See, e.g., BZX Rule 11.9(c)(8)(A).

35 See 17 CFR 242.600(b)(57) and (58).
impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.  

The Commission also believes that the proposed amendments to the Exchange’s price sliding process for primary peg orders and discretionary peg orders in locked or crossed markets are consistent with the Act. The Exchange has stated that its existing approach to price sliding for such orders in locked or crossed markets is unnecessarily complicated, without any material benefit, and that the proposed amendments to the approach would remove the variability of a primary peg order’s booked price in locked or crossed market situations, and make the Exchange’s rules more clear and transparent. The Commission believes these changes should help lessen the complexity in the Exchange’s price sliding rules, which may reduce the potential for investor confusion as to how primary peg and discretionary peg orders would price slide in locked or crossed markets, and thereby help protect investors and the public interest consistent with Section 6(b)(5) of the Act. In addition, the proposed amendments appear to be consistent with the requirements of Rule 610(d) of Regulation NMS which, among other things, requires that the rules of a national securities exchange be reasonably designed to assure the reconciliation of locked or crossed quotations in an NMS stock.  

Lastly, the Commission believes that the Exchange’s proposed technical change to conform certain terminology in its proposed rules is intended to enhance the clarity of its rules, which should reduce the potential for investor confusion, and thereby help protect investors and the public interest consistent with Section 6(b)(5) of the Act.

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36 The Commission notes that the Exchange would be required to submit a proposed rule change pursuant to Section 19(b) of the Act prior to implementing any changes to the proposed primary peg order type.

37 See Notice, 81 FR at 90037.

38 See 17 CFR 242.610(d).
IV.  **Conclusion**

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,\(^3^9\) that the proposed rule change (SR-IEX-2016-18) be and hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.\(^4^0\)

Eduardo A. Aleman  
Assistant Secretary

\(^{4^0}\) 17 CFR 200.30-3(a)(12).