

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-70626; File No. SR-EDGX-2013-36)

October 8, 2013

Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend EDGX Rules 3.2, 13.3, and Adopt Rule 12.14, Front Running of Block Transactions to Conform with the Rules of Other Self-Regulatory Organizations

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 26, 2013, EDGX Exchange, Inc. (the "Exchange" or "EDGX") 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 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: (i) amend Rule 3.22, Proxy Voting; (ii) amend Rule 13.3, Forwarding of Issuer Materials; and (iii) adopt new Rule 12.14, Front Running of Block Transactions, to conform with the rules of the Financial Industry Regulatory Authority, Inc. ("FINRA") for purposes of an agreement between the Exchange and FINRA pursuant to Rule 17d-2 under the Act.<sup>3</sup> All of the changes described herein are applicable to EDGX Members. The text of the proposed rule change is available on the Exchange's Internet website at [www.directedge.com](http://www.directedge.com), at the Exchange's principal office, and at the Public Reference Room of the Commission.

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

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 17 CFR 240.17d-2.

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 received on the proposed rule change. The text of these statements 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,<sup>4</sup> the Exchange and FINRA entered into an agreement to allocate regulatory responsibility for common rules (the “17d-2 Agreement”). 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 federal securities laws, rules and regulations and rules of the Exchange that the Exchange has certified as identical or substantially similar to FINRA rules; (ii) investigation of common members of EDGX and FINRA for violations of federal securities laws, rules or regulations, or Exchange rules that the Exchange has certified as identical or substantially identical to a FINRA rule; and (iii) enforcement of compliance by common members with the federal securities laws, rules and regulations, and the rules of the Exchange that the Exchange has certified as identical or substantially similar to FINRA rules.<sup>5</sup>

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<sup>4</sup> 17 CFR 240.17d-2.

<sup>5</sup> See Securities and Exchange Release No. 61698 (March 12, 2010), 75 FR 13151 (March 18, 2010) (approving File No. 10-196).

The 17d-2 Agreement included 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 with comparable FINRA rules for purposes of the 17d-2 Agreement, the Exchange proposes to: (i) amend Rule 3.22, Proxy Voting; (ii) amend Rule 13.3, Forwarding of Issuer Materials; and (iii) adopt new Rule 12.14, Front Running of Block Transactions.

Rule 3.22, Proxy Voting and Rule 13.3, Forwarding of Issuer Materials

The Exchange proposes to amend Rules 3.22 and 13.3 concerning proxy voting and forwarding of proxy materials to align these rules with FINRA Rule 2251.<sup>6</sup> Section 957 of the Dodd-Frank Act amended Section 6(b) of the Act<sup>7</sup> to require the rules of each national securities exchange prohibit any member organization that is not the beneficial owner of a security registered under Section 12 of the Act<sup>8</sup> from granting a proxy to vote the security in connection with certain stockholder votes, unless the beneficial owner of the security has instructed the member organization to vote the proxy in accordance with the voting instructions of the beneficial owner. The stockholder votes covered by Section 957 include any vote with respect to: (i) the election of a member of the board of directors of an issuer (other than an uncontested election of a director of an investment company registered under the Investment Company Act); (ii) executive compensation; or (iii) any other significant matter, as determined by the

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<sup>6</sup> Similarly, on September 30, 2011, BATS Y-Exchange, Inc. (“BYX”) amended their Rule 13.3 to align it with FINRA Rule 2251. See Securities Exchange Act Release No. 65448 (September 30, 2011), 76 FR 62103 (October 6, 2011) (Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change to Amend BYX Rule 13.3 to Prohibit Members from Voting Uninstructed Shares on Certain Matters and to Align BYX Rule 13.3, Concerning the Forwarding of Proxy and Other Material and Proxy Voting, with FINRA Rule 2251).

<sup>7</sup> 15 U.S.C. 78f(b).

<sup>8</sup> 15 U.S.C. 78l.

Commission, by rule. The Exchange carries out the requirements of Section 957 of the Dodd-Frank Act under paragraph (a) to Exchange Rule 3.22 which prohibits a Member from giving a proxy to vote stock that is registered in its name, unless: (i) such Member is the beneficial owner of such stock; (ii) such proxy is given pursuant to the written instructions of the beneficial owner; or (iii) such proxy is given pursuant to the rules of any national securities exchange or association of which it is a member provided that the records of the Member clearly indicate the procedure it is following.

Similarly, the Exchange proposes to add new paragraph (c) to Rule 3.22, based entirely on FINRA Rule 2251(d), to explicitly state that a Member may give a proxy to vote any stock registered in its name if such Member holds such stock as executor, administrator, guardian, trustee, or in a similar representative or fiduciary capacity with authority to vote. Proposed paragraph (c) would also state that a Member that has in its possession or within its control stock registered in the name of another Member and that desires to transmit signed proxies pursuant to the provisions of Rule 13.3, shall obtain the requisite number of signed proxies from such holder of record. Lastly, proposed paragraph (c) would also state that, notwithstanding the foregoing: (1) any Member designated by a named Employee Retirement Income Security Act of 1974 (as amended) (“ERISA”) Plan fiduciary as the investment manager of stock held as assets of the ERISA Plan may vote the proxies in accordance with the ERISA Plan fiduciary responsibilities if the ERISA Plan expressly grants discretion to the investment manager to manage, acquire, or dispose of any plan asset and has not expressly reserved the proxy voting right for the named ERISA Plan fiduciary; and (2) any designated investment adviser may vote such proxies.

To promote consistency with FINRA Rule 2251, the Exchange proposes to add language to the existing text of Rule 13.3 to state that for beneficial owners, the proxy materials or other

materials to be forwarded on behalf of an issuer can be sent to the beneficial owner's designated investment adviser, if applicable. In conjunction with this change, the Exchange proposes to adopt the definition of "designated investment adviser" set forth in FINRA Rule 2251(f) as Interpretation and Policy .01 to Rule 3.22.

The Exchange also proposes modifying the text of Rule 13.3, which currently would require forwarding of proxy material but which does not explicitly reference such material, to add such an explicit reference. The Exchange further proposes to modify the text of Rule 13.3 to reference "security holders," rather than stockholders, in the initial sentence, to ensure that the coverage of the rule applies to all securities, including debt securities to the extent applicable, and not just equity securities. The Exchange also proposes to incorporate certain language from FINRA Rule 2251 that provides additional detail regarding the material that must be provided to beneficial owners in the event of a proxy solicitation. Specifically, Rule 13.3 as amended would state that in the event of a proxy solicitation, materials provided pursuant to the Rule shall include a signed proxy indicating the number of shares held for such beneficial owner and bearing a symbol identifying the proxy with proxy records maintained by the Member, and a letter informing the beneficial owner (or the beneficial owner's designated investment adviser) of the time limit and necessity for completing the proxy form and forwarding it to the person soliciting proxies prior to the expiration of the time limit in order for the shares to be represented at the meeting. The Rule would also require a Member to furnish a copy of the symbols to the person soliciting the proxies and shall also retain a copy thereof pursuant to the provisions of Exchange Act Rule 17a-4. Finally, the Exchange proposes to modify the title of Rule 13.3 to include a reference to proxy voting.

The Exchange believes that these changes will help to avoid confusion among Members of the Exchange that are also members of FINRA by further aligning the Exchange's rules with FINRA Rule 2251. The proposed changes to Rules 3.22 and 13.3 are designed to enable the Exchange to incorporate Rules 3.22 and 13.3 into the 17d-2 Agreement, further reducing duplicative regulation of Members that are also members of FINRA.

#### Rule 12.14, Front Running of Block Transactions

The Exchange proposes to adopt new Rule 12.14, Front Running of Block Transactions, which would require that Members and persons associated with a Member shall comply with FINRA Rule 5270 as if such Rule were part of the Exchange's Rules. The proposed rule text is substantially the same as IM-2110-3 of the Nasdaq Stock Market LLC ("Nasdaq"), which has been approved by the Commission.<sup>9</sup> FINRA Rule 5270 states that no FINRA member or person associated with a member shall cause to be executed an order to buy or sell a security or a related financial instrument<sup>10</sup> when such member or person associated with a member has material, non-public market information concerning an imminent block transaction<sup>11</sup> in that security, a related financial instrument or a security underlying the related financial instrument.

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<sup>9</sup> See Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006) (order approving Nasdaq's application for registration as a national securities exchange). See also Securities Exchange Act Release No. 58069 (June 30, 2008), 73 FR 39360 (July 9, 2008) (SR-Nasdaq-2008-054) (Notice of Filing and Immediate Effectiveness). Securities Exchange Act Release No. 34-67774 (September 4, 2012), 77 FR 55519 (September 12, 2012) (Approval Order).

<sup>10</sup> FINRA Rule 5270 defines the term "related financial instrument" as "any option, derivative, security-based swap, or other financial instrument overlying a security, the value of which is materially related to, or otherwise acts as a substitute for, such security, as well as any contract that is the functional economic equivalent of a position in such security."

<sup>11</sup> Under FINRA Rule 5270, a transaction involving 10,000 shares or more of a security, an underlying security, or a related financial instrument overlying such number of shares, is generally deemed to be a block transaction, although a transaction of fewer than 10,000 shares could be considered a block transaction. A block transaction that has been agreed

FINRA Rule 5270 includes exceptions to the general prohibitions of the rule where a member can demonstrate that a transaction is unrelated to the material, non-public market information received in connection with the customer order. The Supplementary Material to FINRA Rule 5270 includes an illustrative list of potentially permitted transactions as examples of transactions that, depending upon the circumstances, may be unrelated to the customer block order. These types of transactions may include: where the member has information barriers established to prevent internal disclosure of such information; actions in the same security related to a prior customer order in that security; transactions to correct bona fide errors; or transactions to offset odd-lot orders.

In addition, Rule 5270 does not preclude transactions undertaken for the purpose of fulfilling, or facilitating the execution of, the customer block order. However, when engaging in trading activity that could affect the market for the security that is the subject of the customer block order, the member must minimize any potential disadvantage or harm in the execution of the customer's order, must not place the member's financial interests ahead of those of its customer, and must obtain the customer's consent to such trading activity. A member may obtain its customers' consent through affirmative written consent or through the use of a negative consent letter. The negative consent letter must clearly disclose to the customer the terms and conditions for handling the customer's orders; if the customer does not object, then the member may reasonably conclude that the customer has consented and the member may rely on such letter for all or a portion of the customer's orders. In addition, a member may provide clear and comprehensive oral disclosure to and obtain consent from the customer on an order-by-order

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upon does not lose its identity as such by arranging for partial executions of the full transaction in portions which themselves are not of block size if the execution of the full transaction may have a material impact on the market.

basis, provided that the member documents who provided such consent and such consent evidences the customer's understanding of the terms and conditions for handling the customer's order.

The Exchange also proposes to state in new Rule 12.14 that although the prohibitions in Rule 5270 are limited to imminent block transactions, the front running of other types of orders that place the financial interests of the Member or persons associated with a Member ahead of those of its customer or the misuse of knowledge of an imminent customer order may violate other Exchange rules, including Rule 3.1 and Rule 12.6, or provisions of the federal securities laws.

## 2. Statutory Basis

The Exchange believes that proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>12</sup> which requires, among other things, that the Exchange's rules be 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. The Exchange believes that the proposed rule change will further these requirements by eliminating duplicative and unnecessary rules and advancing the development of a more efficient and effective Exchange Rulebook. The proposed rule change would provide greater harmonization between Exchange and FINRA rules of similar purpose, resulting in greater uniformity and less burdensome and more efficient regulatory compliance. As such, the proposed rule change would foster cooperation and coordination with persons

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<sup>12</sup> 15 U.S.C. 78f(b)(5).



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.

Rule 3.22, Proxy Voting and Rule 13.3, Forwarding of Issuer Materials

The Exchange believes that proposed amendments to Rules 3.22 and 13.3 are consistent with Section 6(b)(5) of the Act,<sup>13</sup> because they remove impediments to, and perfect the mechanism of, a free and open market and a national market system by providing for consistent regulation for Members of the Exchange that are members of other SROs with analogous rules.<sup>14</sup> The proposed changes to Rules 3.22 and 13.3 and proposed Interpretation and Policy .01 are consistent with FINRA Rule 2251. Accordingly, the Exchange believes that the proposal fosters cooperation because, to the extent the Exchange is able to incorporate Rule 13.3 into the 17d-2 Agreement as a rule in common between the Exchange and FINRA, then FINRA will conduct a review for compliance with the common rule to the extent a Member of the Exchange is also a member of FINRA, and the Exchange will not conduct a duplicative review of the same activity by that Member. Finally, the Exchange believes that the proposal will contribute to investor protection by defining important requirements to which Members must abide with respect to proxy solicitation, proxy voting and delivery of proxy materials.

Rule 12.14, Front Running of Block Transactions

The Exchange believes that new Rule 12.14 is consistent with Section 6(b)(5) of the Act<sup>15</sup> which requires, among other things, that the Exchange rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade,

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<sup>13</sup> Id.

<sup>14</sup> See, e.g., FINRA Rule 2251, BYX Rule 13.3, ISE Rule 421, NYSE Arca Rule 9.4, and Nasdaq Rule 2251.

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

and, in general, to protect investors and the public interest. By incorporating FINRA Rule 5270, new Rule 12.14 prohibits front running trading activity that the Exchange believes is inconsistent with just and equitable principles of trade while also ensuring that Members may continue to engage in transactions that do not present the risk of abusive trading practices that the rule is intended to prevent. The Exchange believes that Rule 12.14 would enhance the protection of customer orders by addressing various types of abusive trading that may be intended to take advantage of customer orders. As previously noted, the proposed rule text is substantially similar to Nasdaq's IM-2110-3, which has been approved by the Commission.<sup>16</sup> By adopting Rule 12.14, the Exchange believes that imminent customer block orders would be better protected and that the proposed rule change will prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, and better protect investors and the public interest.

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

The Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is not designed to address any competitive issues but rather is designed 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 functions under the 17d-2 Agreement.

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<sup>16</sup> See Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006) (order approving Nasdaq's application for registration as a national securities exchange). See also Securities Exchange Act Release No. 58069 (June 30, 2008), 73 FR 39360 (July 9, 2008) (SR-Nasdaq-2008-054) (Notice of Filing and Immediate Effectiveness). Securities Exchange Act Release No. 34-67774 (September 4, 2012), 77 FR 55519 (September 12, 2012) (Approval Order).

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

The Exchange has neither solicited nor received written comments on the proposed rule change.

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

Because the foregoing proposed rule change does not: (1) significantly affect the protection of investors or the public interest; (2) impose any significant burden on competition; and (3) by its terms does not become operative for 30 days after the date of this filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>17</sup> and Rule 19b-4(f)(6) thereunder.<sup>18</sup>

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative for 30 days after the date of filing. However, Rule 19b-4(f)(6)(iii) permits the Commission to 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 proposal may become operative immediately upon filing. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because it will help foster consistency between the rulebooks of the self-regulatory

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<sup>17</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>18</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires a self-regulatory organization to provide the Commission with written notice of its intent to file the proposed rule change, along with a brief description and text of 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 met this requirement.

organizations.<sup>19</sup> Accordingly, the Commission hereby grants the Exchange's request and designates the proposal operative upon filing.

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.

#### 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-EDGX-2013-36 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-EDGX-2013-36. 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

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<sup>19</sup> For purposes only of waiving the 30-day operative delay, the Commission has also considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

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 also will be available for inspection and copying at the principal office of the Exchange. 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-EDGX-2013-36 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>20</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>20</sup> 17 CFR 200.30-3(a)(12).