

distribution to its shareholders, based on net asset value. Expenses of \$3,500 incurred in connection with the liquidation were paid by KA Fund Advisors, LLC, applicant's investment adviser.

**Filing Dates:** The application was filed on September 18, 2012, and amended on October 9, 2012 and November 20, 2012.

**Applicant's Address:** 717 Texas Ave., Suite 3100, Houston, TX 77002.

**Defined Asset Funds Corporate Income Fund 10th Insured Series [File No. 811-2295]; Uncommon Values Unit Trust 1985 Series & Subsequent & Similar Series [File No. 811-4281]; Penn State Tax Exempt Investment Trust Series 1 [File No. 811-2787]; Shearson Lehman Brothers Unit Trusts High Yield Municipal Series 1 [File No. 811-5208]; Equity Opportunity Trust Growth Stock Series 1 [File No. 811-3722]**

**Summary:** Each applicant, a unit investment trust, seeks an order declaring that it has ceased to be an investment company. On January 26, 2010, June 6, 2009, July 8, 2010, June 13, 2011 and August 30, 2011, respectively, each applicant made a liquidating distribution to its unit holders, based on net asset value. Applicants' incurred no expenses in connection with the liquidations.

**Filing Dates:** The applications were filed on September 5, 2012 and amended on November 20, 2012.

**Applicants' Address:** 18925 Base Camp Rd., Suite 203, Monument, CO 80132.

**Hatteras Sector Select Fund [File No. 811-22614]; Hatteras Sector Select Institutional Fund [File No. 811-22615]**

**Summary:** Each applicant, a closed-end investment company, seeks an order declaring that it has ceased to be an investment company. Applicants have never made a public offering of their securities and do not propose to engage in business of any kind.

**Filing Dates:** The applications were filed on August 21, 2012 and amended on November 15, 2012.

**Applicant's Address:** 8540 Colonnade Center Dr., Suite 401, Raleigh, NC 27615.

**Genworth Variable Insurance Trust [File No. 811-22205]**

**Summary:** Applicant, an open-end management company, seeks an order declaring that it has ceased to be an investment company. As of January 27, 2012, pursuant to a plan of substitution, applicant's shareholders tendered their shares for redemption, based on net asset value. Expenses of \$217,001

incurred in connection with the liquidation were paid by Genworth Financial Wealth Management, Inc., and later reimbursed by the sponsor of the substituting portfolios.

**Filing Dates:** The application was filed on September 25, 2012, and amended on October 23, 2012.

**Applicant's Address:** 2300 Contra Costa Boulevard, Suite 600, Pleasant Hill, CA 94523.

For the Commission, by the Division of Investment Management, pursuant to delegated authority.

**Kevin M. O'Neill,**

*Deputy Secretary.*

[FR Doc. 2012-29570 Filed 12-6-12; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. IC-30290]

### Notice of Applications for Deregistration Under Section 8(f) of the Investment Company Act of 1940

December 4, 2012.

The following is a notice of applications for deregistration under section 8(f) of the Investment Company Act of 1940. A copy of each application may be obtained via the Commission's Web site by searching for the file number, or for an applicant using the Company name box, at <http://www.sec.gov/search/search.htm> or by calling (202) 551-8090. An order granting each application will be issued unless the SEC orders a hearing. Interested persons may request a hearing on any application by writing to the SEC's Secretary at the address below and serving the relevant applicant with a copy of the request, personally or by mail. Hearing requests should be received by the SEC by 5:30 p.m. on December 26, 2012, and should be accompanied by proof of service on the applicant, in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Secretary, U.S. Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.

#### FOR FURTHER INFORMATION CONTACT:

Diane L. Titus at (202) 551-6810, SEC, Division of Investment Management, Office of Investment Company Regulation, 100 F Street NE., Washington, DC 20549-8010.

**EM Capital Management, LLC [File No. 811-22687]; Global Investor Trust [File No. 811-22694]**

**Summary:** Each applicant seeks an order declaring that it has ceased to be an investment company. Applicants have never made a public offering of their securities and do not propose to make a public offering. EM Capital Management, LLC represents that it filed to register as an investment company in error and that it is not, and does not intend to operate as, an investment company. EM Capital Management, LLC will continue to operate as an investment adviser. Global Investor Trust will continue to operate as a private investment fund in reliance on section 3(c)(1) or 3(c)(7) of the Act.

**Filing Dates:** The applications were filed on October 31, 2012. Global Investor Trust filed an amended application on November 30, 2012. EM Capital Management, LLC filed amended applications on December 3, 2012 and December 4, 2012.

**Applicants' Address:** 920 Country Club Dr., Suite 1E, Moraga, CA 94556.

For the Commission, by the Division of Investment Management, pursuant to delegated authority.

**Jill M. Peterson,**

*Assistant Secretary.*

[FR Doc. 2012-29624 Filed 12-6-12; 8:45 am]

**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-68341; File No. 10-207]

### In the Matter of the Application of Miami International Securities Exchange, LLC for Registration as a National Securities Exchange: Findings, Opinion, and Order of the Commission

December 3, 2012.

#### I. Introduction

On April 26, 2012, Miami International Securities Exchange, LLC ("MIAX Exchange" or "MIAX") submitted to the Securities and Exchange Commission ("Commission") an Application for Registration as a National Securities Exchange ("Form 1 Application") under Section 6 of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of MIAX's Form 1 Application was published for comment in the **Federal Register** on August 20, 2012.<sup>2</sup> The Commission received two

<sup>1</sup> 15 U.S.C. 78f.

<sup>2</sup> See Securities Exchange Act Release No. 67660 (August 15, 2012), 77 FR 50814 ("Notice").

comment letters concerning MIAX's Form 1 Application.<sup>3</sup> MIAX submitted a detailed response to comments on November 30, 2012.<sup>4</sup> On November 30, 2012, MIAX submitted Amendment No. 1 to its Form 1 Application.<sup>5</sup>

## II. Statutory Standards

Under Sections 6(b) and 19(a) of the Act,<sup>6</sup> the Commission shall by order grant an application for registration as a national securities exchange if the Commission finds, among other things, that the proposed exchange is so organized and has the capacity to carry out the purposes of the Act and can comply, and can enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulations thereunder, and the rules of the exchange.

As discussed in greater detail below, the Commission finds that MIAX's application for exchange registration meets the requirements of the Act and the rules and regulations thereunder. Further, the Commission finds that the

proposed rules of MIAX are consistent with Section 6 of the Act in that, among other things, they are designed to: (1) Assure fair representation of the exchange's members in the selection of its directors and administration of its affairs and provide that, among other things, one or more directors shall be representative of investors and not be associated with the exchange, or with a broker or dealer;<sup>7</sup> (2) prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, and remove impediments to and perfect the mechanisms of a free and open market and a national market system;<sup>8</sup> (3) not permit unfair discrimination between customers, issuers, or dealers;<sup>9</sup> and (4) protect investors and the public interest.<sup>10</sup> Finally, the Commission finds that MIAX's proposed rules do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.<sup>11</sup>

## III. Discussion

### A. Governance of MIAX Exchange

#### 1. MIAX Exchange Board of Directors

The board of directors of MIAX Exchange ("Exchange Board") will be its governing body and will possess all of the powers necessary for the management of its business and affairs, including governance of MIAX Exchange as a self-regulatory organization ("SRO").<sup>12</sup>

Under the By-Laws of MIAX Exchange ("MIAX Exchange By-Laws"),<sup>13</sup>

- The Exchange Board will be composed of not less than ten directors;<sup>14</sup>
- One director will be the Chief Executive Officer of MIAX Exchange;<sup>15</sup>
- The number of Non-Industry Directors,<sup>16</sup> including at least one

Independent Director,<sup>17</sup> will equal or exceed the sum of the number of Industry Directors<sup>18</sup> and Member Representative Directors;<sup>19</sup> and

- At least twenty percent of the directors on the Exchange Board will be Member Representative Directors.<sup>20</sup>

For the interim board (discussed below), and subsequently at the first annual meeting and each annual meeting thereafter, Miami Holdings, as the sole LLC Member of MIAX Exchange, will elect the MIAX Exchange Board pursuant to the MIAX By-Laws.<sup>21</sup> In addition, Miami Holdings will appoint the initial Nominating Committee<sup>22</sup> and Member Nominating Committee,<sup>23</sup> consistent with each

who would not be an Industry Director. See MIAX Exchange By-Laws Article I(y).

<sup>17</sup> "Independent Director" means a "Director who has no material relationship with the [MIAX Exchange] or any affiliate of the [MIAX Exchange], or any [MIAX member] or any affiliate of any such [MIAX member]; provided, however, that an individual who otherwise qualifies as an Independent Director shall not be disqualified from serving in such capacity solely because such Director is a Director of the [MIAX Exchange] or [Miami International Holdings, Inc.]." See MIAX Exchange By-Laws Article I(n).

<sup>18</sup> An "Industry Director" is, among other things, a Director that is or has served within the prior three years as an officer, director, employee, or owner of a broker or dealer, as well as any Director who has, or has had, a consulting or employment relationship with MIAX Exchange or any affiliate of MIAX Exchange within the prior three years. See MIAX Exchange By-Laws Article I(p). This definition is consistent with what the Commission has approved for other exchanges. See Securities Exchange Act Release No. 58375 (August 18, 2008), 73 FR 49498 (August 21, 2008) ("BATS Order"). See also Securities Exchange Act Release Nos. 66871 (April 27, 2012), 77 FR 26323 (May 3, 2012) ("BOX Order"); and 61698 (March 12, 2010), 75 FR 13151 (March 18, 2010) ("DirectEdge Exchanges Order").

<sup>19</sup> See MIAX Exchange By-Laws Article II, Section 2.2 (b)(i). "Member Representative Director" means a Director who has been appointed by Miami International Holdings, Inc. as an initial Director pursuant to Section 2.5 of the MIAX Exchange By-Laws to serve until the first annual meeting or who "has been elected by the LLC Member after having been nominated by the Member Nominating Committee or by an Exchange Member pursuant to [the] By-Laws and confirmed as the nominee of Exchange Members after majority vote of Exchange Members, if applicable. A Member Representative Director may, but is not required to be, an officer, director, employee, or agent of an Exchange Member." See MIAX Exchange By-Laws Article I(v). See also MIAX Exchange By-Laws Article II, Section 2.5.

<sup>20</sup> See MIAX Exchange By-Laws Article II, Section 2.2(b)(ii).

<sup>21</sup> See MIAX Exchange By-Laws Article II, Section 2.4. See also MIAX Exchange LLC Agreement Section 9(a).

<sup>22</sup> The Nominating Committee will be comprised of at least three directors, and the number of Non-Industry members on the Nominating Committee must equal or exceed the number of Industry members. See MIAX Exchange By-Laws Article V, Section 5.2. See also MIAX Exchange By-Laws Article IV, Section 4.2(a).

<sup>23</sup> The Member Nominating Committee will be comprised of at least three directors, and each member of the Member Nominating Committee

<sup>3</sup> See Letter from Michael J. Simon, Secretary, International Securities Exchange, LLC, to Elizabeth M. Murphy, Secretary, Commission, dated October 4, 2012 ("ISE Letter"); and Letter from Jeffrey S. Davis, Vice President and Deputy General Counsel, NASDAQ OMX Group, Inc., to Elizabeth M. Murphy, Secretary, Commission, dated October 4, 2012 ("NASDAQ Letter"). In its letter, the International Securities Exchange ("ISE"), requested that MIAX clarify what it considered to be potential "unique aspects" of the proposed MIAX rules and asked the Commission to discuss how such provisions are consistent with the Act. Similarly, the letter from NASDAQ OMX ("NASDAQ") requested that MIAX clarify certain of its proposed rules and provide greater explanation or detail as to how they would work. In Section IV, below, the Commission considers the issues raised by the comment letters, along with MIAX's response thereto, and considers whether MIAX sufficiently addressed those concerns. In summary, the Commission believes that MIAX has sufficiently addressed each of the commenters' concerns and has proposed reasonable changes to its rules to address those concerns. The changes also clarify the potential sources of ambiguity that commenters identified. The changes proposed in Amendment No. 1 are either not material, consistent with the existing rules of other registered national securities exchanges, or responsive to the concerns of the Commission and do not raise any new or novel regulatory issues.

<sup>4</sup> See Letter from Barbara Comly, Executive Vice President, General Counsel & Corporate Secretary, MIAX, to Elizabeth M. Murphy, Secretary, Commission, dated November 30, 2012 ("MIAX Response Letter").

<sup>5</sup> In Amendment No. 1, MIAX proposed changes to the Limited Liability Company Agreement and the By-Laws of Miami International Securities Exchange, LLC concerning the election of an interim board of directors, which is discussed below in Section IV. See Amendment No. 1. MIAX also proposed changes to its proposed rules in response to concerns raised by the two comment letters. See Amendment No. 1. The rule text changes are discussed below in Section III.

<sup>6</sup> 15 U.S.C. 78f(b) and 15 U.S.C. 78s(a), respectively.

<sup>7</sup> See 15 U.S.C. 78f(b)(3).

<sup>8</sup> See 15 U.S.C. 78f(b)(5).

<sup>9</sup> See *id.*

<sup>10</sup> See *id.*

<sup>11</sup> See 15 U.S.C. 78f(b)(8).

<sup>12</sup> See MIAX Exchange By-Laws Section 2.1. See also MIAX Exchange LLC Agreement Sections 7 and 8.

<sup>13</sup> The MIAX Exchange By-Laws are included in the Second Amended and Restated Limited Liability Company Agreement of MIAX Exchange ("MIAX Exchange LLC Agreement").

<sup>14</sup> See MIAX Exchange By-Laws Article II, Section 2.2(a).

<sup>15</sup> See MIAX Exchange By-Laws Article II, Section 2.2(b).

<sup>16</sup> "Non-Industry Director" means a Director who is an Independent Director or any other individual

committee's compositional requirements,<sup>24</sup> to nominate candidates for election to the Exchange Board. Each of the Nominating Committee and Member Nominating Committee, after completion of its respective duties for nominating directors for election to the Board for that year, shall nominate candidates to serve on the succeeding year's Nominating Committee or Member Nominating Committee, as applicable. Additional candidates for the Member Nominating Committee may be nominated and elected by MIA Exchange members pursuant to a petition process.<sup>25</sup>

The Nominating Committee will nominate candidates for each director position, and Miami Holdings, as the sole LLC Member, will elect those directors. For Member Representative Director positions, the Nominating Committee will nominate those candidates submitted to it, and approved, by the Member Nominating Committee.<sup>26</sup> Additional candidates, however, may be nominated for the Member Representative Director positions by MIA Exchange members pursuant to a petition process.<sup>27</sup> If no candidates are nominated pursuant to a petition process, then the initial nominees submitted by the Member Nominating Committee will be nominated as Member Representative Directors by the Nominating Committee. If a petition process produces additional candidates, then the candidates nominated pursuant to the petition process, together with those nominated by the Member Nominating Committee, will be presented to MIA Exchange members for a run-off election to determine the final slate of candidates for the vacant Member Representative

Director positions.<sup>28</sup> In the event of a contested run-off election, the candidates who receive the most votes will be nominated as the final slate of Member Representative Director candidates by the Nominating Committee.<sup>29</sup> Miami Holdings, as the sole LLC Member, is obligated to elect the final slate of the Member Representative Director candidates that are nominated by the Nominating Committee.<sup>30</sup>

The Commission believes that the requirement in the MIA Exchange By-Laws that 20% of the directors be Member Representative Directors and the means by which they will be chosen by MIA Exchange members provide for the fair representation of members in the selection of directors and the administration of MIA Exchange and therefore is consistent with Section 6(b)(3) of the Act.<sup>31</sup> As the Commission has previously noted, this requirement helps to ensure that members have a voice in the use of self-regulatory authority, and that an exchange is administered in a way that is equitable to all those who trade on its market or through its facilities.<sup>32</sup>

In addition, with respect to the requirement that the number of Non-Industry Directors, including at least one Independent Director, will equal or exceed the sum of the number of Industry Directors and Member Representative Directors, the Commission believes that the proposed composition of the MIA Exchange Board satisfies the requirements in Section 6(b)(3) of the Act,<sup>33</sup> which requires in part that one or more directors be representative of issuers and investors and not be associated with a member of the exchange, or with a broker or dealer. The Commission previously has stated that the inclusion of public, non-industry representatives on exchange oversight bodies is an

important mechanism to support an exchange's ability to protect the public interest.<sup>34</sup> Further, the presence of public, non-industry representatives can help to ensure that no single group of market participants has the ability to systematically disadvantage other market participants through the exchange governance process. The Commission believes that public, non-industry directors can provide unique, unbiased perspectives, which are designed to enhance the ability of the MIA Exchange Board to address issues in a non-discriminatory fashion and foster the integrity of MIA Exchange.<sup>35</sup>

*Interim Exchange Board.* Prior to commencing operations, Miami Holdings will appoint an interim Exchange board of directors ("Interim Exchange Board"), which will include interim Member Representative Directors. With respect to the selection of the interim Member Representative Directors for the Interim Exchange Board, prior to the commencement of operations as an exchange, MIA will submit the names of its nominees for the interim Member Representative Directors positions to persons that have begun the process of becoming members in the new MIA Exchange.<sup>36</sup> MIA represents that the persons and firms that have applied to become the initial members of MIA Exchange have already begun the process of completing the necessary applications, obtaining electronic connectivity, and testing their systems with MIA.<sup>37</sup> MIA additionally represents that the initial members of MIA will consist substantially of the current group of persons and firms that have begun the membership application process with MIA.<sup>38</sup>

Such persons will be allowed 14 days to submit the name of an alternative candidate and 5 days to vote for the final slate of candidates.<sup>39</sup> All other interim directors, except for the interim Member Representative Directors, will

shall be a Member Representative member. See MIA Exchange By-Laws Article V, Section 5.3. See also MIA Exchange By-Laws Article IV, Section 4.2(a). Pursuant to MIA Exchange By-Laws Article I(w), a "Member Representative member" is a member of any committee or hearing panel appointed by the Exchange Board who has been elected or appointed after having been nominated by the Member Nominating Committee pursuant to the by-laws and who is an officer, director, employee, or agent of an Exchange Member.

<sup>24</sup> See MIA Exchange By-Laws Article V, Section 5.1.

<sup>25</sup> See *id.*

<sup>26</sup> The Member Nominating Committee will solicit comments from MIA Exchange members for the purpose of approving and submitting names of candidates for election to the position of Member Representative Director. See MIA Exchange By-Laws Article II, Section 2.4(b).

<sup>27</sup> See MIA Exchange By-Laws Article II, Section 2.4(c). The petition must be signed by executive representatives of 10% or more of the MIA Exchange members. No MIA Exchange member, together with its affiliates, may account for more than 50% of the signatures endorsing a particular candidate. See *id.*

<sup>28</sup> See MIA Exchange By-Laws Article II, Section 2.4(e) and (f). Each MIA Exchange Member shall have the right to cast one vote for each available Member Representative Director nomination, provided that any such vote must be cast for a person on the List of Candidates and that no MIA Exchange member, together with its affiliates, may account for more than 20% of the votes cast for a candidate. See MIA Exchange By-Laws Article II, Section 2.4(f).

<sup>29</sup> See MIA Exchange By-Laws Article II, Section 2.4(f).

<sup>30</sup> See *id.*

<sup>31</sup> 15 U.S.C. 78f(b)(3).

<sup>32</sup> See, e.g., Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006) (granting the exchange registration of Nasdaq Stock Market, Inc.) ("Nasdaq Order"); and BATS Order, *supra* note 18. See also Securities Exchange Act Release No. 53382 (February 27, 2006), 71 FR 11251 (March 6, 2006) ("NYSE/Archipelago Merger Approval Order").

<sup>33</sup> 15 U.S.C. 78f(b)(3).

<sup>34</sup> See, e.g., Regulation of Exchanges and Alternative Trading Systems, Securities Exchange Act Release No. 40760 (December 8, 1998), 63 FR 70844 (December 22, 1998) ("Regulation ATS Release").

<sup>35</sup> See Nasdaq Order and NYSE/Archipelago Merger Approval Order, *supra* note 32, and BATS Order, *supra* note 18.

<sup>36</sup> See Amendment No. 1; see also MIA Exchange By-Laws Section 2.5(b). Specifically, MIA will submit the names of its nominees for the interim Member Representative Director positions to persons who have submitted initial documents for membership in the Exchange who would meet the qualifications for membership. See MIA Exchange By-Laws Section 2.5(b).

<sup>37</sup> See Amendment No. 1.

<sup>38</sup> See Amendment No. 1.

<sup>39</sup> See MIA Exchange By-Laws Sections 2.5(b) and (d).

be appointed and elected by Miami Holdings, and must meet the MIA Exchange board composition requirements as set forth in the MIA Exchange By-Laws. Once these interim Member Representative Directors are seated on the Interim Exchange Board, then the Interim Exchange Board will meet the board composition requirements set forth in the governing documents of MIA Exchange.

The Interim Exchange Board will serve until the first initial Exchange Board is elected pursuant to the full nomination, petition, and voting process set forth in the MIA Exchange By-Laws.<sup>40</sup> MIA Exchange will complete such process within 90 days after its application for registration as a national securities exchange is granted by the Commission.<sup>41</sup>

The Commission believes that the process for electing the Interim Exchange Board, as proposed, is consistent with the requirements of the Act, including that the rules of the exchange assure fair representation of the exchange's members in the selection of its directors and administration of its affairs.<sup>42</sup> As noted above, MIA Exchange represents that the initial members of MIA Exchange will consist substantially of the current group of persons and firms that have begun the membership application process with MIA Exchange. MIA Exchange will engage these persons and firms in the interim board election process by, prior to the commencement of operations as an exchange, providing each of them with the opportunity to participate in the selection of interim Member Representative Directors consistent with the MIA Exchange By-Laws. Further, MIA Exchange represents that it will complete the full nomination, petition, and voting process as set forth in the MIA Exchange By-Laws, which will provide persons that are approved as members after the effective date of this Order with the opportunity to participate in the selection of the Member Representative Directors, within 90 days of when MIA Exchange's application for registration

as a national securities exchange is granted.<sup>43</sup> The Commission therefore believes that MIA Exchange's initial interim board process is consistent with the Act, including Section 6(b)(3), in that it is designed to provide representation among the persons and firms likely to become members when MIA Exchange commences operations and is sufficient to allow MIA Exchange to commence operations for an interim period prior to going through the process to elect a new Exchange Board pursuant to the full nomination, petition, and voting process set forth in the MIA Exchange By-Laws.

## 2. Exchange Committees

In the MIA Exchange By-Laws, MIA Exchange has proposed to establish several standing committees, which will be divided into two categories: Committees of the Board (composed of MIA Exchange directors) and Committees of the MIA Exchange (composed of a mixture of MIA Exchange directors and persons that are not MIA Exchange directors).<sup>44</sup> The standing Committees of the Board will be the Audit, Compensation, Appeals, and Regulatory Oversight Committees.<sup>45</sup> In addition, the MIA Exchange Chairman, with approval of the Exchange Board, may appoint an Executive Committee and a Finance Committee, which also would be Committees of the Board.<sup>46</sup>

The Audit Committee will consist of three or more directors, a majority of which will be Non-Industry Directors.<sup>47</sup> Each of the Compensation and Regulatory Oversight Committees will consist of three or more directors, all of which will be required to be Non-Industry Directors.<sup>48</sup> The Appeals Committee will consist of one Independent Director, one Industry Director, and one Member Representative Director.<sup>49</sup> If established, the Finance Committee will consist of at least three persons (who may, but are not required to, be directors) a majority of whom will be Non-Industry Directors.<sup>50</sup> The Executive Committee, if

established, will consist of at least three directors. Because the Executive Committee will have the powers and authority of the Exchange Board in the management of the business and affairs of the MIA Exchange between meetings of the Exchange Board, its composition must reflect that of the Exchange Board. Accordingly, the number of Non-Industry Directors on the Executive Committee must equal or exceed the number of Industry Directors and the percentages of Independent Directors and Member Representative Directors must be at least as great as the corresponding percentages on the Exchange Board as a whole.<sup>51</sup>

With respect to Committees of MIA Exchange, MIA Exchange has proposed to establish a Nominating Committee<sup>52</sup> and a Member Nominating Committee.<sup>53</sup> As discussed above, these committees will have responsibility for, among other things, nominating candidates for election to the Exchange Board. On an annual basis, the members of these committees will nominate candidates for the succeeding year's respective committees to be elected by Miami Holdings, as the sole LLC Member.<sup>54</sup> In addition, MIA Exchange also has proposed to establish a Quality of Markets Committee,<sup>55</sup> which will provide advice and guidance to the Exchange Board on issues related to the fairness, integrity, efficiency and competitiveness of the information, order handling and execution mechanisms of the exchange from the perspective of individual and institutional investors, retail and market making firms, exchange listed companies, and other market participants. The Quality of Markets Committee will include a broad representation of participants in MIA Exchange. Additionally, at least 20% of the members of the committee will be Member Representative members, and the number of Non-Industry members must equal or exceed the total number of Industry and Member Representative members. MIA Exchange also has proposed to

<sup>40</sup> See Amendment No. 1; and MIA Exchange By-Laws Sections 2.2(e) and 2.5(a).

<sup>41</sup> See Amendment No. 1. The 90-day period is consistent with what the Commission recently approved for the BOX Exchange. See Securities Exchange Act Release No. 66871 (April 27, 2012), 77 FR 26323 (May 3, 2012) (allowing BOX Exchange to appoint an initial interim board to enable it to commence operations as a registered exchange). See also Securities Exchange Act Release No. 61152 (December 10, 2009), 74 FR 66699 (December 16, 2009) ("C2 Order") (allowing CBOE to appoint the initial board members and to issue a circular to trading permit holders identifying a slate of representative directors within 45 days from the date on which trading commenced on C2).

<sup>42</sup> See 15 U.S.C. 78f(b)(3).

<sup>43</sup> MIA Exchange's proposed timeline for the interim board process follows a process identical to what the Commission recently approved for the BOX Exchange.

<sup>44</sup> See MIA Exchange By-Laws Section 4.1.

<sup>45</sup> See MIA Exchange By-Laws Section 4.1(a).

<sup>46</sup> See MIA Exchange By-Laws Section 4.5(e) and (f), respectively.

<sup>47</sup> See MIA Exchange By-Laws Section 4.5(b). A Non-Industry Director shall serve as Chairman of the Committee. See *id.* See also MIA Exchange By-Laws Section 4.2(a) (requiring that each committee be comprised of at least three people).

<sup>48</sup> See MIA Exchange By-Laws Section 4.5(a) and 4.5(c).

<sup>49</sup> See MIA Exchange By-Laws Section 4.5(d).

<sup>50</sup> See MIA Exchange By-Laws Section 4.5(f). See also MIA Exchange By-Laws Section 4.2(a)

(providing that except as otherwise provided in the MIA Exchange By-Laws, committees may include persons who are not members of the Board).

<sup>51</sup> See MIA Exchange By-Laws Section 4.5(e).

<sup>52</sup> See MIA Exchange By-Laws Article V, Section 5.2, and *supra* note 22.

<sup>53</sup> See MIA Exchange By-Laws Article V, Section 5.3, and *supra* note 23.

<sup>54</sup> See MIA Exchange By-Laws Article V, Section 5.1, and *supra* note 25. Additional candidates for the Member Nominating Committee may be nominated and elected by MIA Exchange members pursuant to a petition process. See *supra* note 27 and accompanying text.

<sup>55</sup> See MIA Exchange By-Laws Article IV, Section 4.6.

establish a Business Conduct Committee as discussed further below.<sup>56</sup>

The Commission believes that MIAX Exchange's proposed committees, which are similar to the committees maintained by other exchanges,<sup>57</sup> are designed to help enable MIAX Exchange to carry out its responsibilities under the Act and are consistent with the Act, including Section 6(b)(1), which requires, in part, an exchange to be so organized and have the capacity to carry out the purposes of the Act.<sup>58</sup>

### B. Regulation of MIAX Exchange

When MIAX Exchange commences operations as a national securities exchange, MIAX Exchange will have all the attendant regulatory obligations under the Act. In particular, MIAX Exchange will be responsible for the operation and regulation of its trading system and the regulation of its members. Certain provisions in the MIAX Exchange and Miami Holdings governance documents are designed to facilitate the ability of MIAX Exchange and the Commission to fulfill their regulatory obligations. The discussion below summarizes some of these key provisions.

#### 1. Ownership Structure; Ownership and Voting Limitations

MIAX Exchange will be structured as a Delaware limited liability company ("LLC"), which will be wholly-owned by the sole member of the LLC, Miami International Holdings, Inc. ("Miami Holdings"). The Miami Holdings' proposed Amended and Restated Certificate of Incorporation ("Miami Holdings Certificate") includes restrictions on the ability to own and vote shares of capital stock of Miami Holdings.<sup>59</sup> These limitations are designed to prevent any Miami Holdings shareholder from exercising undue control over the operation of MIAX Exchange and to assure that the MIAX Exchange and the Commission

are able to carry out their regulatory obligations under the Act.

In particular, for so long as Miami Holdings (directly or indirectly) controls MIAX Exchange, no person, either alone or together with its related persons,<sup>60</sup> may beneficially own more than 40% of any class of capital stock of Miami Holdings.<sup>61</sup> MIAX proposed a more conservative restriction for MIAX Exchange members, wherein MIAX Exchange members, either alone or together with their related persons, are prohibited from beneficially owning more than 20% of shares of any class of capital stock of Miami Holdings.<sup>62</sup> If any stockholder violates these ownership limits, Miami Holdings would redeem the shares in excess of the applicable ownership limit at their par value.<sup>63</sup> In addition, no person, alone or together with its related persons, may vote or cause the voting of more than 20% of the voting power of the then issued and outstanding capital stock of Miami Holdings.<sup>64</sup> If any stockholder purports to vote, or cause the voting of, shares that would violate this voting limit, Miami Holdings would not honor such vote in excess of the voting limit.<sup>65</sup>

Any person that proposes to own shares of capital stock in excess of the 40% ownership limitation, or vote or grant proxies or consents with respect to shares of capital stock in excess of the 20% voting limitation, must deliver written notice to the Miami Holdings board to notify the Board of its intention.<sup>66</sup> The notice must be delivered to the Board not less than 45 days before the proposed ownership of such shares or proposed exercise of such voting rights or the granting of such proxies or consents.<sup>67</sup> The Miami Holdings board may waive the 40%

ownership limitation and the 20% voting limitation, pursuant to a resolution duly adopted by the Board of Directors, if it makes certain findings,<sup>68</sup> except that the Miami Holdings board cannot waive the voting and ownership limits above 20% for MIAX Exchange members and their related persons.<sup>69</sup> Any such waiver would not be effective unless and until approved by the Commission pursuant to Section 19 of the Act.<sup>70</sup>

The Miami Holdings Certificate also contains provisions that are designed to further safeguard the ownership and voting limitation described above, or are otherwise related to direct and indirect changes in control. Specifically, any person that, either alone or together with its related persons owns, directly or indirectly, of record or beneficially, 5% or more of the capital stock of Miami Holdings will be required to immediately notify Miami Holdings in writing upon acquiring knowledge of such ownership.<sup>71</sup> Thereafter, such persons will be required to update Miami Holdings of any increase or decrease of 1% or more in their previously reported ownership percentage.<sup>72</sup>

<sup>68</sup> See Miami Holdings Certificate NINTH (b)(ii)(B). The required determinations are that (A) such waiver will not impair the ability of MIAX Exchange to carry out its functions and responsibilities under the Act and the rules and regulations promulgated thereunder, (B) such waiver is otherwise in the best interests of MIAX Exchange and Miami Holdings, (C) such waiver will not impair the ability of the Commission to enforce the Act and (D) the transferee in such transfer and its related persons are not subject to any applicable "statutory disqualification" (within the meaning of Section 3(a)(39) of the Act). See Miami Holdings Certificate NINTH (b)(ii)(B) and (b)(iii). The Commission has previously approved the rules of other exchanges that provide for the ability of the exchange to waive the ownership and voting limitations discussed above for non-members of the exchange. See, e.g., DirectEdge Exchanges Order, *supra* note 18.

<sup>69</sup> See *id.* These provisions are generally consistent with waiver of ownership and voting limits approved by the Commission for other SROs. See e.g., BATS Exchange Registration Order; NSX Demutualization Order, *supra* note 59; CHX Demutualization Order, *supra* note 59; and Securities Exchange Act Release No. 49718 (May 17, 2004), 69 FR 29611 (May 24, 2004) (SR-PCX-2004-08).

<sup>70</sup> See Miami Holdings Certificate NINTH (b)(ii)(B).

<sup>71</sup> See Miami Holdings Certificate NINTH(c)(i). The notice will require the person's full legal name; the person's title or status; the person's approximate ownership interest in Miami Holdings; and whether the person has power, directly or indirectly, to direct the management or policies of Miami Holdings. See *id.*

<sup>72</sup> See Miami Holdings Certificate NINTH(c)(ii). Changes of less than 1% must also be reported to Miami Holdings if they result in such person crossing a 20% or 40% ownership threshold. See *id.* In addition, MIAX rules also impose limits on affiliation between the MIAX Exchange and a

<sup>56</sup> See *infra* note 381 and accompanying text.

<sup>57</sup> See, e.g., BATS Order, *supra* note 18, and Nasdaq Order, *supra* note 32.

<sup>58</sup> 15 U.S.C. 78f(b)(1).

<sup>59</sup> These provisions are consistent with ownership and voting limits approved by the Commission for other SROs. See e.g., Securities Exchange Act Release Nos. 62158 (May 24, 2010), 75 FR 30082 (May 28, 2010) (CBOE-2008-88) (CBOE Demutualization Approval Order); 58375 (August 18, 2008) 73 FR 49498 (August 21, 2008) (File No. 10-182) ("BATS Exchange Registration Order"); 53963 (June 8, 2006), 71 FR 34660 (June 15, 2006) (SR-NSX-2006-03) ("NSX Demutualization Order"); 51149 (February 8, 2005), 70 FR 7531 (February 14, 2005) (SR-CHX-2004-26) ("CHX Demutualization Order"); and 49098 (January 16, 2004), 69 FR 3974 (January 27, 2004) (SR-Phlx-2003-73) ("Phlx Demutualization Order").

<sup>60</sup> See Miami Holdings Certificate NINTH (a)(ii) (defining "related persons").

<sup>61</sup> See Miami Holdings Certificate NINTH (b)(i)(A).

<sup>62</sup> See Miami Holdings Certificate NINTH (b)(i)(B).

<sup>63</sup> See Miami Holdings Certificate NINTH (e). Any shares which have been called for redemption shall not be deemed outstanding shares for the purpose of voting or determining the total number of shares entitled to vote. Once redeemed by Miami Holdings, such shares shall become treasury shares and shall no longer be deemed to be outstanding. See *id.* Furthermore, if any redemption results in another stockholder owning shares in violation of the ownership limits described above, Miami Holdings shall redeem such shares. See *id.*

<sup>64</sup> See Miami Holdings Certificate NINTH (b)(i)(C).

<sup>65</sup> See Miami Holdings Certificate NINTH (d). The Miami Holdings Certificate also prohibits the payment of any stock dividends and conversions that would violate the ownership and voting limitations. See Miami Holdings Certificates FOURTH A.(b) and (e), and D.7.

<sup>66</sup> See Miami Holdings Certificate NINTH (b)(iv).

<sup>67</sup> See *id.*

The MIAX LLC Agreement does not include change of control provisions that are similar to those in the Miami Holdings Certificate; however the MIAX Exchange LLC Agreement explicitly provides that Miami Holdings is the sole LLC Member of MIAX Exchange.<sup>73</sup> Thus, if Miami Holdings ever proposes to no longer be the sole LLC Member of MIAX Exchange (and therefore no longer its sole owner), MIAX Exchange would be required to amend the MIAX Exchange LLC Agreement. Any changes to the MIAX Exchange LLC Agreement (which includes the MIAX Exchange By-Laws), including any change in the provisions that identify Miami Holdings as the sole owner of MIAX Exchange, must be filed with, or filed with and approved by, the Commission pursuant to Section 19 of the Act, as the case may be.<sup>74</sup> Further, pursuant to the MIAX Exchange By-Laws, Miami Holdings may not transfer or assign, in whole or in part, its ownership interest in MIAX Exchange, unless such transfer is filed with and approved by the Commission pursuant to Section 19 of the Act.<sup>75</sup>

Although Miami Holdings is not independently responsible for regulation, its activities with respect to the operation of MIAX Exchange must be consistent with, and must not interfere with, the self-regulatory obligations of MIAX Exchange. As described above, the provisions applicable to direct and indirect changes in control of Miami Holdings and MIAX Exchange, as well as the voting limitation imposed on owners of Miami Holdings who also are MIAX Exchange members, are designed to help prevent any owner of Miami Holdings from exercising undue influence or control over the operation of MIAX Exchange and to help assure that MIAX Exchange retains a sufficient degree of

independence to effectively carry out its regulatory obligations under the Act. In addition, these limitations are designed to address the conflicts of interests that might result from a member of a national securities exchange owning interests in the exchange. Members that trade on an exchange traditionally have had ownership interests in such exchange. As the Commission has noted in the past, however, a member's interest in an exchange, including an entity that controls an exchange, could become so large as to cast doubts on whether the exchange may fairly and objectively exercise its self-regulatory responsibilities with respect to such member.<sup>76</sup> A member that is a controlling shareholder of an exchange could seek to exercise that controlling influence by directing the exchange to refrain from, or the exchange may hesitate to, diligently monitor and conduct surveillance of the member's conduct or diligently enforce the exchange's rules and the federal securities laws with respect to conduct by the member that violates such provisions. As such, the Commission believes that these requirements are designed to minimize the potential that a person or entity can improperly interfere with or restrict the ability of MIAX Exchange to effectively carry out its regulatory oversight responsibilities under the Act.

The Commission believes that MIAX's and Miami Holding's proposed governance provisions are consistent with the Act, including Section 6(b)(1), which requires, in part, an exchange to be so organized and have the capacity to carry out the purposes of the Act.<sup>77</sup> In particular, these requirements are designed to minimize the potential that a person could improperly interfere with or restrict the ability of the Commission or MIAX Exchange to effectively carry out their regulatory oversight responsibilities under the Act.

## 2. Regulatory Independence and Oversight

Although Miami Holdings will not itself carry out regulatory functions, its activities with respect to the operation of MIAX Exchange must be consistent with, and must not interfere with, MIAX Exchange's self-regulatory obligations. In this regard, MIAX Exchange and Miami Holdings propose to adopt certain provisions in their respective governing documents that are designed to help maintain the independence of the regulatory functions of MIAX

Exchange. These proposed provisions are substantially similar to those included in the governing documents of other exchanges that recently have been granted registration.<sup>78</sup> Specifically:

- The directors, officers, employees, and agents of Miami Holdings must give due regard to the preservation of the independence of the self-regulatory function of MIAX Exchange and must not take actions that would interfere with the effectuation of decisions by the MIAX Exchange Board relating to its regulatory functions or that would interfere with MIAX Exchange's ability to carry out its responsibilities under the Act.<sup>79</sup>

- Miami Holdings must comply with federal securities laws and the rules and regulations promulgated thereunder, and agrees to cooperate with the Commission and MIAX Exchange pursuant to, and to the extent of, their respective regulatory authority. In addition, Miami Holdings' officers, directors, employees, and agents must comply with federal securities laws and the rules and regulations promulgated thereunder and agree to cooperate with the Commission and MIAX Exchange in respect of the Commission's oversight responsibilities regarding MIAX Exchange and the self-regulatory functions and responsibilities of MIAX Exchange.<sup>80</sup>

- Miami Holdings, and its officers, directors, employees, and agents submit to the jurisdiction of the U.S. federal courts, the Commission, and MIAX Exchange, for purposes of any action, suit, or proceeding pursuant to U.S. federal securities laws, and the rules

<sup>78</sup> See e.g., DirectEdge Exchanges Order and BATS Order, *supra* note 18, and C2 Order, *supra* note 41.

<sup>79</sup> See Amended and Restated By-Laws of Miami Holdings ("Miami Holdings By-Laws"), Article VII, Section 1.

Similarly, Article II, Section 2.1(d) of the MIAX Exchange By-Laws requires the MIAX Exchange Board to, when managing the business and affairs of MIAX Exchange and evaluating any proposal, consider the requirements of Section 6(b) of the Act. Section 2.1(e) also requires the MIAX Exchange Board, when evaluating any proposal to take into account (among other things and to the extent relevant), the potential impact on the integrity, continuity and stability of the national securities exchange operated by MIAX Exchange and the other operations of MIAX Exchange on the ability to prevent fraudulent and manipulative acts and practices and on investors and the public, and whether such would promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to and facilitating transactions in securities or assist in the removal of impediments to or perfection of the mechanisms for a free and open market and a national market system. See, e.g., Amended and Restated By-Laws of BATS, Article III, Section 1.

<sup>80</sup> See Miami Holdings By-Laws, Article VII, Section 4.

member of the MIAX Exchange. See MIAX Rule 201(g) ("Without prior Commission approval, the Exchange or any entity with which it is affiliated shall not directly or indirectly through one or more intermediaries acquire or maintain an ownership interest in an Exchange Member. In addition, without prior Commission approval, no Member shall be or become affiliated with (1) the Exchange; or (2) any affiliate of the Exchange. Nothing herein shall prohibit a Member from acquiring or holding an equity interest in (i) Miami International Holdings, Inc. that is permitted by the Certificate of Incorporation of Miami International Holdings, Inc. or (ii) Miami International Securities Exchange, LLC that is permitted by the Amended and Restated Limited Liability Company Agreement of Miami International Securities Exchange, LLC.").

<sup>73</sup> See MIAX Exchange LLC Agreement and MIAX Exchange By-Laws Article I(t) A (both of which define "LLC Member" to mean Miami Holdings, as the sole member of MIAX).

<sup>74</sup> See 15 U.S.C. 78s. See also MIAX Exchange LLC Agreement, Section 28(b).

<sup>75</sup> See MIAX Exchange By-Laws Article III, Section 3.4.

<sup>76</sup> See, e.g., DirectEdge Exchanges Order and BATS Order, *supra* note 18.

<sup>77</sup> 15 U.S.C. 78f(b)(1).

and regulations thereunder, arising out of, or relating to, MIAX Exchange activities.<sup>81</sup>

- All books and records of MIAX Exchange reflecting confidential information pertaining to the self-regulatory function of MIAX Exchange (including but not limited to disciplinary matters, trading data, trading practices, and audit information) shall be retained in confidence by MIAX Exchange and its personnel and will not be used by MIAX Exchange for any non-regulatory purpose and shall not be made available to persons (including, without limitation, any MIAX Exchange member) other than to personnel of the Commission, and those personnel of MIAX Exchange, members of committees of MIAX Exchange, members of the MIAX Exchange Board, or hearing officers and other agents of MIAX, to the extent necessary or appropriate to properly discharge the self-regulatory function of MIAX Exchange.<sup>82</sup>

- The books and records of MIAX Exchange and Miami Holdings must be maintained in the United States<sup>83</sup> and, to the extent they are related to the operation or administration of MIAX Exchange, Miami Holdings books and records will be subject at all times to inspection and copying by the Commission.<sup>84</sup>

- Furthermore, to the extent they relate to the activities of MIAX Exchange, the books, records, premises, officers, directors, employees, and agents of Miami Holdings will be deemed to be the books, records, premises, officers, directors, employees, and agents of MIAX Exchange, for purposes of, and subject to oversight pursuant to, the Act.<sup>85</sup>

- Miami Holdings will take necessary steps to cause its officers, directors, employees, and agents, prior to accepting a position as an officer,

director, employee or agent (as applicable) to consent in writing to the applicability of provisions regarding books and records, confidentiality, jurisdiction, and regulatory obligations, with respect to their activities related to MIAX Exchange.<sup>86</sup>

- Miami Holdings Certificate and By-Laws require that, so long as Miami Holdings controls MIAX Exchange, any changes to those documents be submitted to the MIAX Exchange Board, and, if such change is required to be filed with the Commission pursuant to Section 19(b) of the Act and the rules and regulations thereunder, such change shall not be effective until filed with, or filed with and approved by, the Commission.<sup>87</sup>

The Commission believes that the provisions discussed in this section, which are designed to help maintain the independence of MIAX Exchange's regulatory function and help facilitate the ability of MIAX Exchange to carry out its responsibility and operate in a manner consistent with the Act, are appropriate and consistent with the requirements of the Act, particularly with Section 6(b)(1), which requires, in part, an exchange to be so organized and have the capacity to carry out the purposes of the Act.<sup>88</sup> Whether MIAX Exchange operates in compliance with the Act, however, depends on how it and Miami Holdings in practice implement the governance and other provisions that are the subject of this Order.<sup>89</sup>

Further, Section 19(h)(1) of the Act<sup>90</sup> provides the Commission with the authority "to suspend for a period not exceeding twelve months or revoke the registration of [an SRO], or to censure or impose limitations upon the activities, functions, and operations of [an SRO], if [the Commission] finds, on the record after notice and opportunity for hearing, that [the SRO] has violated or is unable to comply with any provision of the Act, the rules or regulations thereunder, or

its own rules or without reasonable justification or excuse has failed to enforce compliance" with any such provision by its members (including associated persons thereof).<sup>91</sup> If Commission staff were to find, or become aware of, through staff review and inspection or otherwise, facts indicating any violations of the Act, including without limitation Sections 6(b)(1) and 19(g)(1), these matters could provide the basis for a disciplinary proceeding under Section 19(h)(1) of the Act.

The Commission also notes that, even in the absence of the governance provisions described above, under Section 20(a) of the Act any person with a controlling interest in MIAX Exchange would be jointly and severally liable with and to the same extent that MIAX Exchange is liable under any provision of the Act, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.<sup>92</sup> In addition, Section 20(e) of the Act creates aiding and abetting liability for any person who knowingly provides substantial assistance to another person in violation of any provision of the Act or rule thereunder.<sup>93</sup> Further, Section 21C of the Act authorizes the Commission to enter a cease-and-desist order against any person who has been "a cause of" a violation of any provision of the Act through an act or omission that the person knew or should have known would contribute to the violation.<sup>94</sup> These provisions are applicable to all entities' dealings with MIAX Exchange, including Miami Holdings.

### 3. Regulation of MIAX

As a prerequisite for the Commission's granting of an exchange's application for registration, an exchange must be organized and have the capacity to carry out the purposes of the Act.<sup>95</sup> Specifically, an exchange must be able to enforce compliance by its members, and persons associated with its members, with the federal securities laws and the rules of the exchange.<sup>96</sup> The discussion below summarizes how MIAX Exchange proposes to conduct and structure its regulatory operations.

<sup>81</sup> See Miami Holdings By-Laws, Article VII, Section 5.

<sup>82</sup> See MIAX Exchange By-Laws Article X, Section 10.4. The Commission notes that the Miami Holdings LLC Agreement also provides that all books and records of MIAX Exchange reflecting confidential information pertaining to the self-regulatory function of MIAX Exchange will be subject to confidentiality restrictions. See Miami Holdings By-Laws Article VII, Section 2. The requirement to keep such information confidential shall not limit the Commission's ability to access and examine such information or limit the ability of officers, directors, employees, or agent of Miami Holdings to disclose such information to the Commission. See *id.*

<sup>83</sup> See MIAX Exchange By-Laws Article X, Section 10.4; and Miami Holdings By-Laws Article VII, Section 3.

<sup>84</sup> See Miami Holdings By-Laws Article VII, Section 3.

<sup>85</sup> See Miami Holdings By-Laws Article VII, Section 3.

<sup>86</sup> See Miami Holdings By-Laws Article VII, Section 6.

<sup>87</sup> See Miami Holdings Certificate Article VII; and Miami Holdings By-Laws, Article XII, Section 1.

<sup>88</sup> 15 U.S.C. 78f(b)(1).

<sup>89</sup> The Commission notes that it is reviewing the various standards and processes it uses to facilitate the registration of national securities exchanges and other entities required to register with the Commission and plans to issue a concept release designed to collect information and evaluate different aspects of these registration standards and processes, including the policy objectives of registration, how best to achieve those policy objectives through registration and other means, and the relative benefits and costs of the various means available. See Securities Exchange Act Release No. 65543 (October 12, 2011), 76 FR 65784, 65786 fn. 13 (October 24, 2011).

<sup>90</sup> See 15 U.S.C. 78s(h)(1).

<sup>91</sup> See *id.*

<sup>92</sup> 15 U.S.C. 78t(a).

<sup>93</sup> 15 U.S.C. 78t(e).

<sup>94</sup> 15 U.S.C. 78u-3.

<sup>95</sup> See Section 6(b)(1) of the Act, 15 U.S.C. 78f(b)(1).

<sup>96</sup> See *id.* See also Section 19(g) of the Act, 15 U.S.C. 78s(g).



#### a. Regulatory Oversight Committee

The regulatory operations of MIAX Exchange will be monitored by the Regulatory Oversight Committee of the MIAX Exchange Board. The Regulatory Oversight Committee will consist of at least three directors, all of whom will be Non-Industry Directors. The Regulatory Oversight Committee will be responsible for overseeing the adequacy and effectiveness of MIAX Exchange's regulatory and SRO responsibilities, assessing MIAX Exchange's regulatory performance, and assisting the MIAX Exchange Board (and committees of the MIAX Exchange Board) in reviewing MIAX Exchange's regulatory plan and the overall effectiveness of MIAX Exchange's regulatory functions.<sup>97</sup>

Further, a Chief Regulatory Officer ("CRO") of MIAX Exchange will have general day-to-day supervision over MIAX Exchange's regulatory operations.<sup>98</sup> The Regulatory Oversight Committee also will be responsible for recommending compensation and personnel actions involving the CRO and senior regulatory personnel to the Compensation Committee of the MIAX Exchange for action.<sup>99</sup> The CRO will report to the Regulatory Oversight Committee.<sup>100</sup>

#### b. Regulatory Funding

To help assure the Commission that it has and will continue to have adequate funding to be able to meet its responsibilities under the Act, MIAX Exchange represented that, prior to commencing operations as a national securities exchange, Miami Holdings will provide sufficient funding to MIAX Exchange for the exchange to carry out its responsibilities under the Act.<sup>101</sup> Specifically, MIAX Exchange represents that prior to launching operations, Miami Holdings will allocate sufficient operational assets and make a capital contribution of not less than \$2,000,000 into MIAX Exchange's capital account, in addition to either directly making payments of, or contributing adequate funds from Miami Holdings to MIAX Exchange for payments by MIAX Exchange of: (i) Personnel costs (including regulatory department personnel), (ii) technology support for

regulatory oversight, (iii) infrastructure costs, and (iv) industry and regulatory memberships.<sup>102</sup>

MIAX Exchange also represents that such direct funding by Miami Holdings, as well as allocations and contributions by Miami Holdings to MIAX Exchange, will be adequate to operate MIAX Exchange, including the ongoing regulation of the exchange, and that Miami Holdings and MIAX Exchange have entered into a funding agreement that requires Miami Holdings to provide adequate funding for the exchange's initial and ongoing operations, including the regulation of MIAX Exchange.<sup>103</sup>

Further, any revenues received by MIAX Exchange from fees derived from its regulatory function or regulatory penalties will not be used for non-regulatory purposes.<sup>104</sup> Any excess funds, as determined by MIAX Exchange, may be remitted to Miami Holdings, however "Regulatory Funds" will not be remitted to Miami Holdings.<sup>105</sup>

#### c. Rule 17d-2 Agreements; Regulatory Contract With CBOE

Section 19(g)(1) of the Act,<sup>106</sup> among other things, requires every SRO registered as either a national securities exchange or national securities association to examine for, and enforce compliance by, its members and persons associated with its members with the Act, the rules and regulations thereunder, and the SRO's own rules, unless the SRO is relieved of this responsibility pursuant to Section 17(d) or Section 19(g)(2) of the Act.<sup>107</sup> Rule 17d-2 of the Act<sup>108</sup> permits SROs to

propose joint plans to allocate regulatory responsibilities amongst themselves for their common rules with respect to their common members.<sup>109</sup> These agreements, which must be filed with and declared effective by the Commission, generally cover areas where each SRO's rules substantively overlap, including such regulatory functions as personnel registration and sales practices. Without this relief, the statutory obligation of each individual SRO could result in a pattern of multiple examinations of broker-dealers that maintain memberships in more than one SRO. Such regulatory duplication would add unnecessary expenses for common members and their SROs.

A 17d-2 plan that is declared effective by the Commission relieves the specified SRO of those regulatory responsibilities allocated by the plan to another SRO.<sup>110</sup> Many SROs have entered into Rule 17d-2 agreements.<sup>111</sup> MIAX Exchange has represented to the Commission that it intends to become a party to the existing multiparty options Rule 17d-2 plans concerning sales practice regulation and market surveillance.<sup>112</sup> Under these agreements, the examining SROs will examine firms that are common

an SRO of its responsibilities to: (i) Receive regulatory reports from such members; (ii) examine such members for compliance with the Act and the rules and regulations thereunder, and the rules of the SRO; or (iii) carry out other specified regulatory responsibilities with respect to such members.

<sup>109</sup> 17 CFR 240.17d-2. Section 19(g)(1) of the Act requires every SRO to examine its members and persons associated with its members and to enforce compliance with the federal securities laws and the SRO's own rules, unless the SRO is relieved of this responsibility pursuant to Section 17(d) of the Act. Section 17(d) was intended, in part, to eliminate unnecessary multiple examinations and regulatory duplication with respect to Common Members. See Securities Exchange Act Release No. 12935 (October 28, 1976), 41 FR 49091 (November 8, 1976) ("Rule 17d-2 Adopting Release").

<sup>110</sup> See *id.*

<sup>111</sup> See, e.g., Securities Exchange Act Release Nos. 59218 (January 8, 2009), 74 FR 2143 (January 14, 2009) (File No. 4-575) (FINRA/Boston Stock Exchange, Inc.); 58818 (October 20, 2008), 73 FR 63752 (October 27, 2008) (File No. 4-569) (FINRA/BATS Exchange, Inc.); 55755 (May 14, 2007), 72 FR 28057 (May 18, 2007) (File No. 4-536) (National Association of Securities Dealers, Inc. ("NASD") (n/k/a FINRA) and CBOE concerning the CBOE Stock Exchange); 55367 (February 27, 2007), 72 FR 9983 (March 6, 2007) (File No. 4-529) (NASD/ISE); and 54136 (July 12, 2006), 71 FR 40759 (July 18, 2006) (File No. 4-517) (NASD/Nasdaq).

<sup>112</sup> See MIAX Form 1 Application, Exhibit L. See also Securities Exchange Act Release Nos. 66974 (May 11, 2012), 77 FR 29705 (May 18, 2012) (File No. S7-966) (notice of filing and order approving and declaring effective an amendment to the multiparty 17d-2 plan concerning options-related sales practice matters); and 66975 (May 11, 2012), 77 FR 29712 (May 18, 2012) (File No. 4-551) (notice of filing and order approving and declaring effective an amendment to the multiparty 17d-2 plan concerning options-related market surveillance).

<sup>102</sup> See *id.*

<sup>103</sup> See *id.*

<sup>104</sup> See MIAX Exchange By-Laws Article IX, Section 9.4.

<sup>105</sup> See MIAX Form 1 Application, Exhibit I. See also MIAX Exchange LLC Agreement Section 16; and MIAX Exchange By-Laws Article IX, Section 9.4. MIAX Exchange By-Laws Article 1(ee) defines "Regulatory Funds" as "fees, fines, or penalties derived from the regulatory operations of the [MIAX Exchange]", but such term does not include "revenues derived from listing fees, market data revenues, transaction revenues, or any other aspect of the commercial operations of the [MIAX Exchange], even if such revenues are used to pay costs associated with the regulatory operations of the [MIAX Exchange]." This definition is consistent with the rules of other SROs. See e.g., By-Laws of NASDAQ OMX PHLX LLC, Article I(ii); and By-Laws of NASDAQ OMX BX, Inc., Article I(ii).

<sup>106</sup> 15 U.S.C. 78s(g)(1).

<sup>107</sup> 15 U.S.C. 78q(d) and 15 U.S.C. 78s(g)(2), respectively.

<sup>108</sup> See Section 17(d)(1) of the Act and Rule 17d-2 thereunder, 15 U.S.C. 78q(d)(1) and 17 CFR 240.17d-2. Section 17(d)(1) of the Act allows the Commission to relieve an SRO of certain responsibilities with respect to members of the SRO who are also members of another SRO. Specifically, Section 17(d)(1) allows the Commission to relieve

<sup>97</sup> See MIAX Exchange By-Laws Article IV Section 4.5(c). The Regulatory Oversight Committee is responsible for reviewing MIAX Exchange's regulatory budget, and also will meet regularly with the Chief Regulatory Officer. See *id.*

<sup>98</sup> See MIAX Exchange By-Laws Article VI, Section 6.10.

<sup>99</sup> See MIAX Exchange By-Laws Article IV, Section 4.5(c).

<sup>100</sup> See MIAX Exchange By-Law Article VI, Section 6.10.

<sup>101</sup> See MIAX Form 1 Application, Exhibit I.



members of MIAX Exchange and the particular examining SRO for compliance with certain provisions of the Act, certain rules and regulations adopted thereunder, and certain MIAX Exchange Rules.

In addition, MIAX Exchange has entered into a Regulatory Services Agreement ("RSA") with the Chicago Board Options Exchange, Incorporated ("CBOE"), under which CBOE will perform certain regulatory functions on behalf of MIAX Exchange.<sup>113</sup> Pursuant to the RSA, CBOE, in its capacity as service provider to MIAX Exchange, will perform various services on MIAX's behalf, including conducting certain market surveillances; assisting MIAX Exchange in conducting investigations of potential violations of MIAX Exchange rules and/or federal securities laws related to activity on the Exchange; conducting examinations related to Exchange members' conduct on MIAX Exchange; assisting MIAX Exchange with disciplinary proceedings pursuant to MIAX Exchange rules, including issuing charges and conducting hearings; and providing dispute resolution services to Exchange members on behalf of MIAX Exchange, including operation of the MIAX Exchange's arbitration program.<sup>114</sup> Notwithstanding the RSA, MIAX Exchange will retain ultimate legal responsibility for the regulation of its members and its market.

The Commission believes that it is consistent with the Act for MIAX Exchange to contract with another SRO to perform certain examination, enforcement, and disciplinary functions.<sup>115</sup> These functions are fundamental elements of a regulatory program, and constitute core self-regulatory functions. The Commission believes that CBOE, as an SRO that operates two options exchanges, should have the capacity to perform these functions for MIAX Exchange.<sup>116</sup> However, MIAX Exchange, unless relieved by the Commission of its

responsibility,<sup>117</sup> bears the ultimate responsibility for self-regulatory responsibilities and primary liability for self-regulatory failures, not the SRO retained to perform regulatory functions on MIAX Exchange's behalf. In performing these regulatory functions, however, the SRO retained to perform regulatory functions may nonetheless bear liability for causing or aiding and abetting the failure of MIAX Exchange to perform its regulatory functions.<sup>118</sup> Accordingly, although CBOE will not act on its own behalf under its SRO responsibilities in carrying out these regulatory services for MIAX Exchange, as the SRO retained to perform regulatory functions, CBOE may have secondary liability if, for example, the Commission finds that the contracted functions are being performed so inadequately as to cause a violation of the federal securities laws by MIAX Exchange.

### C. Trading System

#### 1. Access to MIAX

Access to MIAX will be granted to individuals or organizations who are approved to become members. Approved members will be issued Trading Permits that grant the member the ability to transact on MIAX Exchange through the exchange's electronic systems.<sup>119</sup> Trading Permits will not convey upon members any ownership interest in MIAX Exchange, and they will not be transferable except in cases where a member experiences a change in control or corporate reorganization.<sup>120</sup> Membership will be open to any broker-dealer that: (1) Is registered under Section 15 of the Act;<sup>121</sup> and (2) has and maintains membership in another registered options exchange or the Financial Industry Regulatory Authority ("FINRA").<sup>122</sup> There will be no limit to

the number of Trading Permits that MIAX Exchange can issue, although MIAX could determine in the future that a limit on or decrease to the number of Trading Permits issued is necessary.<sup>123</sup> Members of MIAX may be one of three classes of market maker,<sup>124</sup> or they may be non-market makers.

Those seeking to become members of MIAX will need to submit an application in accordance with procedures that MIAX will announce by Regulatory Circular.<sup>125</sup> Entities that become members, and their associated persons, will be required to meet and maintain certain qualification and registration criteria similar to what is required by other options exchanges.<sup>126</sup>

<sup>123</sup> See MIAX Rule 200(a). MIAX would announce in advance any limitation or decrease it plans to impose pursuant to Rule 200(a). See *id.* In the event that MIAX imposes a limitation or decrease, MIAX, in doing so, may not eliminate the ability of an existing member to trade on MIAX Exchange unless MIAX Exchange is permitted to do so pursuant to a rule filing submitted to the Commission under Section 19(b) of the Act. See *id.* In addition, MIAX's exercise of authority under proposed Rule 200 would be subject to the provisions of Section 6(c)(4) of the Act. See *id.* See also 15 U.S.C. 78f(c)(4) (providing that an exchange may limit: (1) The number of members of the exchange and (2) the number of members and designated representatives of members permitted to effect transactions on the floor of the exchange without the services of another person acting as broker, provided, however, that no exchange shall have the authority to decrease the number of memberships in such exchange, or the number of members and designated representatives of members permitted to effect transactions on the floor of such exchange without the services of another person acting as broker, below such number in effect on May 1, 1975, or the date such exchange was registered with the Commission, whichever is later. In addition, the Commission, in accordance with the provisions of section 19(c) of the Act, may amend the rules of any exchange to increase (but not to decrease) or to remove any limitation on the number of memberships in such exchange or the number of members or designated representatives of members permitted to effect transactions on the floor of the exchange without the services of another person acting as broker, if the Commission finds that such limitation imposes a burden on competition not necessary or appropriate in furtherance of the purposes of the Act.). See also CBOE Rule 3.1(a)(vi) (concerning limiting or reducing the number of types of trading permits). In addition, MIAX's exercise of authority under proposed Rule 200 would be subject to the provisions of Section 6(b)(2) of the Act, which requires the rules of an exchange to provide that any registered broker or dealer or any natural person associated with a registered broker or dealer may become a member of such exchange and any person may become associated with a member thereof. See 15 U.S.C. 78f(b)(2).

<sup>124</sup> See MIAX Rule 600. Market Maker registration is discussed in greater detail below, *infra* Section III(C)(3)(a).

<sup>125</sup> See MIAX Rule 200(c). Any proposed application fees contemplated by Rule 200(c) would need to be filed with the Commission pursuant to Section 19(b) of the Act and Rule 19b-4 thereunder. See 15 U.S.C. 78s(b) and 17 CFR 240.19b-4, respectively.

<sup>126</sup> See MIAX Rule 200 Series. Such criteria include, but are not limited to, capital maintenance

Continued

<sup>113</sup> See MIAX Form 1 Application, Exhibit L.

<sup>114</sup> See MIAX Form 1 Application, Exhibit L.

<sup>115</sup> See, e.g., Regulation ATS Release, *supra* note 34. See also Securities Exchange Act Release Nos. 50122 (July 29, 2004), 69 FR 47962 (August 6, 2004) (SR-Amex-2004-32) (order approving rule that allowed Amex to contract with another SRO for regulatory services) ("Amex Regulatory Services Approval Order"); 57478 (March 12, 2008), 73 FR 14521 (March 18, 2008) (SR-NASDAQ-2007-004) ("NOM Approval Order"); Nasdaq Order, *supra* note 32; and BATS Order, *supra* note 18.

<sup>116</sup> See, e.g., Amex Regulatory Services Approval Order, *supra* note 115; NOM Approval Order, *supra* note 115; and Nasdaq Order, *supra* note 32. The Commission notes that the RSA is not before the Commission and, therefore, the Commission is not acting on it.

<sup>117</sup> See *supra* note 108.

<sup>118</sup> For example, if failings by the SRO retained to perform regulatory functions have the effect of leaving an exchange in violation of any aspect of the exchange's self-regulatory obligations, the exchange will bear direct liability for the violation, while the SRO retained to perform regulatory functions may bear liability for causing or aiding and abetting the violation. See, e.g., Nasdaq Order, *supra* note 32; BATS Order, *supra* note 18; and Release No. 42455 (February 24, 2000), 65 FR 11388 (March 2, 2000) (File No. 10-127) (approval of registration of ISE as a national securities exchange).

<sup>119</sup> See MIAX Exchange Rule 200(a). MIAX intends to allow each member to determine the best method for accessing MIAX, whether by using customized front-end software or through third-party vendors who route orders to MIAX through front-end or service bureau configurations. See MIAX Form 1 Application, Exhibit E.

<sup>120</sup> See MIAX Rule 200(d).

<sup>121</sup> See MIAX Rule 200(b).

<sup>122</sup> See MIAX Rule 200(c)(7).

In addition, MIAX proposes further requirements on members that seek to do business with the public.<sup>127</sup> Applicants who are denied membership may appeal MIAX Exchange's decision pursuant to MIAX's rules governing Hearings, Review, and Arbitration.<sup>128</sup> Every member will be subject to MIAX's regulatory jurisdiction, including MIAX's disciplinary jurisdiction.<sup>129</sup>

Further, MIAX Rule 608 requires market makers to have a letter of guarantee. In its comment letter, NASDAQ argues that MIAX should broaden this rule to require all members to provide a letter of guarantee, not just market makers.<sup>130</sup> In response, MIAX explains that MIAX Rule 209 already requires a letter of guarantee for all MIAX members.<sup>131</sup>

In addition, in its comment letter, NASDAQ notes that MIAX Rule 507 requires a member who changes clearing information to contact the clearing member on the other side of a trade.<sup>132</sup> NASDAQ argues this approach is potentially burdensome for MIAX members since some MIAX members might not maintain contact information for all other MIAX members.<sup>133</sup> NASDAQ believes that a better approach, given that the Options Clearing Corporation serves as the central clearing party for listed options trades, would be for the member to notify MIAX.<sup>134</sup> In response, MIAX revised Rule 507 to accommodate this suggestion, which MIAX believes should be less burdensome for members.<sup>135</sup>

The Commission finds that MIAX's proposed membership rules are consistent with the Act, including Section 6(b)(2) of the Act, which requires the rules of an exchange to provide that any registered broker or dealer or natural person associated with a broker or dealer may become a member of such exchange or associated

with a member thereof.<sup>136</sup> MIAX's proposed rules with respect to exchange membership are substantively similar to the rules of other exchanges.

The Commission notes that pursuant to Section 6(c) of the Act,<sup>137</sup> an exchange must deny membership to any person, other than a natural person, that is not a registered broker or dealer, any natural person that is not, or is not associated with, a registered broker or dealer, and registered broker-dealers that do not satisfy certain standards, such as financial responsibility or operational capacity. As a registered exchange, MIAX must independently determine if an applicant satisfies the standards set forth in the Act, regardless of whether an applicant is a member of another SRO.<sup>138</sup>

In addition, members may enter into arrangements with other parties, including non-members and other members, to provide "Sponsored Access" to trading on MIAX.<sup>139</sup> Members who provide such Sponsored Access will be responsible for all trading conducted pursuant to the access agreement, and to the same extent as if the member were trading directly.<sup>140</sup> Accordingly, members that provide Sponsored Access must maintain and implement policies and procedures to supervise and monitor sponsored trading activity.<sup>141</sup> Additionally, non-members who seek to trade on MIAX through Sponsored Access agreements will need to agree to comply with all applicable federal securities laws and rules and MIAX Exchange rules.<sup>142</sup> MIAX's rules governing Sponsored Access arrangements are similar to the rules of other exchanges<sup>143</sup> and are consistent with Rule 15c3-5 under the Act.<sup>144</sup>

## 2. Linkage

MIAX intends to become a participant in the Plan Relating to Options Order Protection and Locked/Crossed Markets or any successor plan ("Linkage Plan").<sup>145</sup> If admitted as a participant to

the Plan, other plan participants would be able to send orders to MIAX in accordance with the terms of the plan as applied to MIAX Exchange.

MIAX Exchange rules include relevant definitions, establish the conditions pursuant to which members may enter orders in accordance with the Linkage Plan, impose obligations on MIAX Exchange regarding how it must process incoming orders, establish a general standard that members and MIAX Exchange should avoid trade-throughs, establish potential regulatory liability for members that engage in a pattern or practice of trading through other exchanges, and establish obligations with respect to locked and crossed markets.

The Commission believes that MIAX has proposed rules that are designed to comply with the requirements of the Linkage Plan.<sup>146</sup> Further, as provided below, before MIAX can commence operations as an exchange, it must become a participant in the Linkage Plan.

## 3. Market Makers

### a. Registration and Appointment

Members of MIAX may apply to become one of three types of market maker: Primary Lead Market Maker, Lead Market Maker, or Registered Market Maker (collectively, "Market Makers"). Market Makers are entitled to receive certain benefits and privileges in exchange for fulfilling certain affirmative and negative market-making obligations.<sup>147</sup> Each class of Market Maker will receive a specific level of benefits and privileges in exchange for a specific level of obligation that such Market Maker assumes to the MIAX market.

To begin the process of registering as a Registered Market Maker or Lead Market Maker, a member will be required to file a written application with MIAX.<sup>148</sup> In reviewing a member's application for membership, MIAX will consider, among other things, the applicant's market making ability.<sup>149</sup> Only approved Lead Market Makers

requirements. *See, e.g.*, C2 Rules 3.1 and 3.2 (containing similar criteria).

<sup>127</sup> *See* MIAX Rule 1300 Series. These Rules also are similar to the rules of other exchanges. *See, e.g.*, ISE Rules Chapter 6.

<sup>128</sup> *See* MAX Rule 1100 Series.

<sup>129</sup> *See* MIAX Rule 200(f). For MIAX's rules concerning discipline, *see* MIAX Rule 1000 Series.

<sup>130</sup> *See* NASDAQ Letter, *supra* note 3, at 4.

<sup>131</sup> *See* MIAX Response Letter, *supra* note 4, at 15-16. MIAX noted that MIAX Rule 608, which NASDAQ referenced, is a rule that relates specifically to market makers, and as such, it simply reiterates that Rule 209's general requirement concerning letters of guarantee applies specifically to market makers. *See id.*

<sup>132</sup> *See* NASDAQ Letter, *supra* note 3, at 4.

<sup>133</sup> *See id.*

<sup>134</sup> *See id.*

<sup>135</sup> *See* MIAX Response Letter, *supra* note 4, at 13. MIAX notes that its revised rule is similar to the operation of ISE Rule 707. *See id.*

<sup>136</sup> 15 U.S.C. 78f(b)(2).

<sup>137</sup> 15 U.S.C. 78f(c).

<sup>138</sup> *See, e.g.*, BOX Order, *supra* note 18 at 26337; BATS Order, *supra* note 18, at 73 FR 49502; and Nasdaq Order, *supra* note 32, at 71 FR 3555.

<sup>139</sup> *See* MIAX Rule 210.

<sup>140</sup> *See* MIAX Rule 210(a).

<sup>141</sup> *See id.*

<sup>142</sup> *See* MIAX Rule 210(d)(1)(i). *See also, e.g.*, 17 CFR 240.15c3-5.

<sup>143</sup> *See, e.g.*, Nasdaq Rule 4611(d).

<sup>144</sup> 17 CFR 240.15c3-5.

<sup>145</sup> *See* MIAX Form 1 Application, Exhibit E. *See also* Securities Exchange Act Release No. 60405 (July 30, 2009), 74 FR 39362 (August 6, 2009) (File No. 4-546) (order approving the national market system Plan Relating to Options Order Protection and Locked/Crossed Markets Submitted by the

Chicago Board Options Exchange, Incorporated, ISE, The NASDAQ Stock Market LLC, NASDAQ OMX BX, Inc., NASDAQ OMX PHLX, Inc., NYSE Amex LLC, and NYSE Arca, Inc.).

<sup>146</sup> *See* MIAX Rule 1400 Series.

<sup>147</sup> Market Makers' benefits and obligations are discussed in greater detail in the following section.

<sup>148</sup> *See* MIAX Rule 600(b).

<sup>149</sup> *See id.* The provision permitting MIAX to consider "such other factors as [it] deems appropriate" must be applied in a manner that is consistent with the Act, including provisions that prohibit an exchange from acting in an unfairly discriminatory manner. *See* 15 U.S.C. 78f(b)(5); *see also* C2 Order, *supra* note 41, at n. 80, 76 FR at 66704.

may apply to be considered for appointment as a Primary Lead Market Maker in one or more option classes traded on MIAAX.<sup>150</sup> All members who are approved to become Market Makers will be designated as specialists on MIAAX for all purposes under the Act and rules thereunder.<sup>151</sup>

Once approved, a Market Maker would seek appointment to make markets in options classes.<sup>152</sup> Either the Exchange Board or a committee thereof<sup>153</sup> would evaluate an application for Market Maker status based on: (1) The financial resources available to the Market Maker; (2) the Market Maker's experience and expertise in market making or options trading; (3) the preferences of the Market Maker to receive appointment(s) in specific option class(es); and (4) the maintenance and enhancement of competition among Market Makers in each option class.<sup>154</sup> MIAAX will allow one Primary Lead Market Maker appointment per class, and will have a maximum class quoting limit of fifty Market Makers per class.<sup>155</sup> Once appointed, MIAAX will surveil a Market Maker's activity for continued compliance with all applicable rules and requirements, which are discussed in more detail below.

The Commission finds that MIAAX's rules for the registration and appointment of Market Makers are consistent with the Act. In particular, MIAAX's rules provide an objective process by which a member could become a Market Maker on MIAAX and provide for oversight by MIAAX Exchange to monitor for continued compliance by Market Makers with the terms of their application for such status. The Commission notes that MIAAX's proposed Market Maker registration and appointment requirements are similar to those of other options exchanges.<sup>156</sup>

#### b. Market Maker Obligations

Pursuant to MIAAX rules, all Market Makers will be subject to a number of

general obligations. In particular, the transactions of a Market Maker must constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market.<sup>157</sup> Among other things, a Market Maker must: (1) Engage in dealings for its own account when there is a lack of price continuity, a temporary disparity between the supply of and demand for a particular option contract, or a temporary distortion of the price relationships between options contracts of the same class; (2) compete with other market makers; (3) make markets that will be honored for the number of contracts entered; (4) update quotations in response to changed market conditions; and (5) price option contracts fairly by, among other things, meeting the bid/ask differential requirements prescribed.<sup>158</sup> In addition, Market Makers must maintain minimum net capital in accordance with MIAAX rules and the federal securities laws.<sup>159</sup> Market Makers also must maintain information barriers between market making activities and any other business activities that are reasonably designed to prevent the misuse of material, non-public information.<sup>160</sup>

MIAAX's rules governing Market Maker quoting obligations are tailored to the specific class of Market Maker.<sup>161</sup> Specifically, a Primary Lead Market Maker will be subject to the highest standard applicable on MIAAX, as they will be required to provide continuous two-sided Standard quotes and/or Day eQuotes<sup>162</sup> throughout the trading day 99% of the time in the lesser of 99% of the series, or 100% of the series minus one put-call pair, in each appointed class.<sup>163</sup> Primary Lead Market Makers also are required to participate in the

opening rotation.<sup>164</sup> Lead Market Makers must provide continuous two-sided quotes (consisting of Standard quotes and/or Day eQuotes) throughout the trading day 90% of the time in 90% of the series in each of their appointed classes.<sup>165</sup> Lead Market Makers also must participate in the opening rotation.<sup>166</sup> Lastly, Registered Market Makers must provide continuous two-sided quotes (consisting of Standard quotes and/or Day eQuotes) 90% of the time in 60% of the series in each of its appointed classes.<sup>167</sup> Further, Registered Market Makers may be called upon by a MIAAX Exchange official to submit a single quote or maintain continuous quotes in one or more series of its appointed classes whenever, in the judgment of such official, it is necessary to do so in the interest of fair and orderly markets.<sup>168</sup> For purposes of meeting the continuous quoting obligations discussed herein, a Market Maker's quote must meet the bid/ask differential requirements of MIAAX Rule 603(b)(4).<sup>169</sup>

In options classes other than to which they are appointed, a Market Maker is prohibited from engaging in transactions in an account in which it has an interest that are disproportionate to, or in derogation of, the performance of its market making obligations as set forth in the MIAAX rules.<sup>170</sup> Further, the total number of contracts executed during a quarter by a Registered Market Maker in options classes to which it is not appointed may not exceed 25% of the total number of contracts traded by such Registered Market Maker in classes to which it is appointed.<sup>171</sup> Similarly, the total number of contracts executed during a quarter by a Lead Market Maker (including a Primary Lead Market Maker) in options classes to which it is not appointed may not exceed 10% of

<sup>157</sup> See MIAAX Rule 603(a).

<sup>158</sup> See MIAAX Rule 603(b)(4). Specifically, as set forth in note 285, *infra*, following the opening rotation, Market Makers must create differences of no more than \$5 between the bid and offer. Prior to the opening rotation, bid/ask differentials shall be no more than \$.25 between the bid and offer for each option contract for which the bid is less than \$2, no more than \$.40 where the bid is at least \$2 but does not exceed \$5, no more than \$.50 where the bid is more than \$5 but does not exceed \$10, no more than \$.80 where the bid is more than \$10 but does not exceed \$20, and no more than \$1 where the bid is more than \$20, provided that the Exchange may establish differences other than the above for one or more option.

<sup>159</sup> See MIAAX Rule 609.

<sup>160</sup> See MIAAX Rule 610.

<sup>161</sup> See MIAAX Rule 604.

<sup>162</sup> See *infra* Section III(C)(5) (discussing the various types of quotes that may be submitted by Market Makers on MIAAX).

<sup>163</sup> See MIAAX Rule 604(e)(1). See also Amendment No. 1 (revising MIAAX Rule 604(e)(1) to provide that these obligations will be applied on a class-by-class basis).

<sup>164</sup> See MIAAX Rule 604(e)(1)(i).

<sup>165</sup> See MIAAX Rule 604(e)(1). See also Amendment No. 1 (revising MIAAX Rule 604(e)(2) to provide that these obligations will be applied on a class-by-class basis).

<sup>166</sup> See MIAAX Rule 604(e)(2).

<sup>167</sup> See MIAAX Rule 604(e)(3). See also Amendment No. 1 (revising MIAAX Rule 604(e)(3) to provide that these obligations will be applied on a class-by-class basis).

<sup>168</sup> See MIAAX Rule 604(e)(3)(iii).

<sup>169</sup> See MIAAX Rule 604(e)(1)–(3) (for Primary Lead Market Makers, Lead Market Makers, and Registered Market Makers, respectively).

<sup>170</sup> See MIAAX Rule 603(d). Among other things, a Market Maker should not effect purchases or sales except in an orderly manner. See *id.* See also ISE Rule 803(d) (containing an identical provision).

<sup>171</sup> See MIAAX Rule 605(b)(2). See also ISE Rule 805(b)(2) (limiting the total number of contracts a Competitive Market Maker registered on that Exchange may execute per quarter in classes to which it is not appointed to 25% or less of the total contracts traded by that Market Maker in classes to which it is appointed).

<sup>150</sup> See *id.*

<sup>151</sup> See MIAAX Rule 600(a).

<sup>152</sup> See MIAAX Rule 602.

<sup>153</sup> See MIAAX Rule 602(a). MIAAX Rule 1100 Series provides the process for hearings, review, and arbitration of claims by persons economically aggrieved by MIAAX Exchange action, which would include denial of registration as a Market Maker.

<sup>154</sup> See *id.*

<sup>155</sup> See Amendment No. 1 (in which MIAAX revised its Rule 602(c) to increase the proposed class quoting limit from 10 to 50). See also, e.g., C2 Rule 8.11(a) (imposing a class quoting limit of 50) and CBOE Rule 8.3A, Interpretations and Policies .01 (imposing a class quoting limit of 50).

<sup>156</sup> See, e.g., ISE Rules 800 and 801, and C2 Rule 8.1 (registration); ISE Rule 802 and C2 Rule 8.11 (appointment).

the total number of contracts traded by such Lead Market Maker in classes to which it is appointed.<sup>172</sup> Executions resulting from orders in a Registered Market Maker's and Lead Market Maker's appointed classes are included in these 25% and 10% limitations, respectively.<sup>173</sup>

If MIAx finds any failure by a Market Maker to meet minimum performance standards or properly perform as a Market Maker, such Market Maker may be subject to suspension, termination, or restriction of registration in one or more of the securities in which the Market Maker is registered.<sup>174</sup>

Market Makers will receive certain benefits in return for satisfying their responsibilities.<sup>175</sup> For example, a broker-dealer or other lender may extend "good faith" credit to a member of a national securities exchange or registered broker-dealer to finance its activities as a market maker or specialist.<sup>176</sup> In addition, market makers are excepted from the prohibition in Section 11(a) of the Act.<sup>177</sup> The Commission believes that a market maker must be subject to sufficient and commensurate affirmative obligations, including the obligation to hold itself out as willing to buy and sell options for its own account on a regular or continuous basis, to justify favorable treatment.<sup>178</sup> The Commission further believes that the rules of all U.S. options

markets need not provide the same standards for market maker participation, so long as they impose affirmative obligations that are consistent with the Act.<sup>179</sup>

The Commission believes that MIAx's Market Maker participation requirements impose appropriate affirmative obligations on MIAx Exchange's Market Makers that are commensurate with the benefits afforded to such participants and, accordingly, are consistent with the Act.

Specifically, with regard to MIAx's proposed continuous quoting obligations, only those quotes that are liquidity providing—Standard quotes and Day eQuotes—will be counted towards a Market Maker's quoting obligations, rather than all types of eQuotes that a Market Maker will be permitted to utilize.<sup>180</sup> The Commission believes that this treatment is appropriate under the Act and consistent with a Market Maker's obligation to contribute to the maintenance of a fair and orderly market. Further, the Commission believes that the specific levels of benefits conferred on the different classes of Market Makers are appropriately balanced by the obligations imposed by MIAx's rules. For example, as discussed below, Primary Lead Market Makers and Lead Market Makers are entitled to certain participation entitlements,<sup>181</sup> and at the same time, are subject to heightened continuous quoting obligations to justify these special benefits.<sup>182</sup>

Finally, the Commission believes that the Act does not mandate a particular market model for exchanges, and while Market Makers may become an important source of liquidity on MIAx, they will likely not be the only source as MIAx is designed to match buying and selling interest of all MIAx participants.

#### 4. Order Display, Execution, and Priority

MIAx will operate a fully automated electronic options marketplace. Liquidity will be derived from orders to buy and orders to sell, as well as market maker quotations, submitted to MIAx electronically by its members from

remote locations. There will be no physical trading floor. Options traded on the Exchange will be subject to Minimum Price Variations that will begin at \$0.05 for option contracts trading at less than \$3.00 per option, and \$.10 for option contracts trading at \$3.00 per option or higher.<sup>183</sup> In addition, MIAx will participate in the penny pilot program pursuant to which it will permit certain options with premiums under \$3 (as well as heavily traded options on certain indices) to be quoted and traded in increments as low as \$.01.<sup>184</sup>

All orders and quotes submitted to MIAx will be displayed unless: (i) The order is a contingent order (such as immediate or cancel orders); or (ii) the quote is a certain type of eQuote<sup>185</sup> (such as an Auction or Cancel eQuote). Displayed orders and quotes will be displayed on an anonymous basis (except for attributable orders,<sup>186</sup> which will allow voluntary disclosure of firm identification information) at a specified price. Non-displayed orders will not be displayed to any participant.

In certain cases, orders and quotes may be displayed at a price different from the price specified by the submitting member.<sup>187</sup> One such case is

<sup>183</sup> See MIAx Rule 510(a).

<sup>184</sup> NASDAQ points out that MIAx's rule concerning the "penny pilot" did not contain a date for the end of the penny pilot. See NASDAQ Letter, *supra* note 3, at 3. In response, MIAx amended its Rule 510 to insert the industry-wide date for the schedule expiration the penny pilot (*i.e.*, December 31, 2012), and MIAx noted that at the time it filed its Form 1 application, the scheduled expiration of the penny pilot was June 30, 2012 (which the Commission notes preceded publication of the notice of MIAx's Form 1 application in the **Federal Register**). See MIAx Response Letter, *supra* note 4, at 13. MIAx notes that the December 31, 2012 expiration date conforms to other exchange rules, including CBOE Rule 6.42 and ISE Rule 710. See *id.*

<sup>185</sup> See *infra* Section III(C)(5) (discussing eQuotes). The Commission notes that MIAx has not proposed orders with reserve size at this time.

<sup>186</sup> An Attributable Order is a market or limit order which displays the user firm's ID for purposes of trading on MIAx. Use of Attributable Orders will be voluntary. This order type is consistent with similar order types on other exchanges. See, *e.g.*, CBOE Rule 6.53(o) (attributable order type).

<sup>187</sup> In its comment letter, ISE disagreed with the broad statement in Exhibit E of MIAx's Form 1 application that says that orders and quotes will be displayed at the price specified by the submitting member. ISE points out that there are two additional instances, beyond what MIAx described in its Exhibit E, where an order or quote will not be displayed at the submitted price: (1) Customer interest (either Professional or Priority customers) that is marked Do Not Route that would lock or cross the NBBO; and (2) market maker quotes and orders that would trade through the ABBO. See ISE Letter, *supra* note 3, at 1–2. In each case, the orders will be displayed one minimum price variation away from the opposite side NBBO, but will remain available for execution on MIAx at the price that locks the NBBO. See ISE Letter, *supra* note 3, at 1–2. In response, MIAx revised Exhibit E to note all

<sup>172</sup> See MIAx Rule 605(b)(3); see also ISE Rule 805(b)(3) (limiting the total number of contracts a Primary Market Maker registered on that Exchange may execute per quarter in classes to which it is not appointed to 10% or less of the total contracts traded by that Market Maker in classes to which it is appointed).

<sup>173</sup> See MIAx Rule 605(b)(2)–(3). MIAx's inclusion of executions resulting from orders is more restrictive than similar rules of other exchanges, which do not include orders executed in appointed classes towards Market Makers' 25% and 10% limitations, respectively. See, *e.g.*, ISE Rule 805(b)(2)–(3).

See also Amendment No. 1 (where MIAx revised Rule 605 to remove consideration of non-priority quotes from the 25% and 10% limitations). MIAx's proposal not to count non-priority quotes in the 25% or 10% buckets does not raise any new or novel issue because even a non-priority quote still would be required to meet the maximum differential provision contained in MIAx Rule 603(b)(4). Accordingly, such a valid width quote, even if it may not comply with a potentially narrower "priority quote width standard" under MIAx Rule 517(b)(ii), would still represent a valid width quote that can be counted towards a Market Maker's quoting obligation, consistent with the practice on other exchanges.

<sup>174</sup> See MIAx Rules 600 and 602(f).

<sup>175</sup> See, *e.g.*, NOM Approval Order, *supra* note 115, at 73 FR 14526 (discussing the benefits and obligations of market makers).

<sup>176</sup> See 12 CFR 221.5 and 12 CFR 220.7; see also 17 CFR 240.15c3–1(a)(6) (capital requirements for market makers).

<sup>177</sup> 15 U.S.C. 78k(a).

<sup>178</sup> See NOM Approval Order, *supra* note 115, at 73 FR 14526.

<sup>179</sup> See *id.*

<sup>180</sup> See *infra* Section III(C)(5) (discussing the various quote types that Market Makers can utilize).

<sup>181</sup> See *infra* notes 225–240 and accompanying text (describing the Primary Lead Market Maker and Directed Lead Market Maker participation entitlements). See also *infra* Section III(C)(5) (discussing the benefit Market Makers receive from the MIAx priority quote rule).

<sup>182</sup> See *supra* Section III(C)(3)(b) (describing Primary Lead Market Maker and Lead Market Maker quoting obligations).

non-displayed penny orders. Specifically, MIAX proposes to allow a member to enter an order or quote (as applicable) priced in a penny increment for series that are subject to a minimum price variation other than a penny (e.g., 5 cents or 10 cents). The order would be displayed at the applicable minimum increment (rounded as appropriate), not the narrower penny price, but would be available for execution at the non-displayed penny price (i.e., a “non-displayed penny order”).<sup>188</sup> With respect to MIAX’s proposed use of non-displayed penny orders, the ISE Letter appears to assert that MIAX has proposed to permit non-displayed prices to be entered in regular trading increments in all classes, which (if true) ISE would oppose to the extent it could decrease transparency and further internalization of order flow.<sup>189</sup> ISE believes that MIAX’s proposal on this point could be much broader than what has been previously approved by the Commission.<sup>190</sup> In response, MIAX notes that, pursuant to MIAX Rule 516(b)(3), non-displayed penny orders will only be accepted in designated classes, which must have a minimum price variation larger than one penny.<sup>191</sup> MIAX notes that such orders, which are limit orders priced in a one-cent increment, are executable at their stated penny limit price, but are displayed at the closest minimum price variation that does not violate the limit price.<sup>192</sup> MIAX reiterated that it does not propose to handle orders and quotes in a manner that will permit non-displayed prices in the regular trading increments in all options classes, and that its proposed rule is not intended to be broader than what has previously been approved by the Commission.<sup>193</sup> To clarify this point, MIAX revised Rule 516(b)(3) to state that non-displayed penny orders would only be accepted in designated classes and must have a minimum pricing variation larger than one penny.<sup>194</sup>

In its comment letter, NASDAQ notes that proposed MIAX Rule 516(b)(4) is silent on what would happen if a member attempted to submit a non-displayed penny order in an option that

is not eligible for such orders.<sup>195</sup> In response, MIAX amended proposed MIAX Rule 516(b)(3) to state that such order would be rejected.<sup>196</sup>

Members may submit the following types of orders: Market; Limit (including Marketable Limit, Fill-or-Kill, Immediate-or-Cancel, Non-Displayed Penny,<sup>197</sup> and Auction or Cancel (“AOC”)); WAIT;<sup>198</sup> Attributable; Intermarket Sweep (“ISO”); Do Not Route;<sup>199</sup> Opening; Customer Cross; Qualified Contingent Cross; Day Limit; and Good ‘Til Cancelled.<sup>200</sup> With the

<sup>195</sup> See NASDAQ Letter, *supra* note 3, at 3.

<sup>196</sup> See MIAX Response Letter, *supra* note 4, at 9.

<sup>197</sup> See *supra* note 188.

<sup>198</sup> “WAIT” orders are orders that, upon entry into the MIAX system, are held for one second without processing for potential display and/or execution. After one second, the order is processed for potential display and/or execution in accordance with all order entry instructions as determined by the entering party. See MIAX Rule 516(c). See also NYSE Arca Rule 6.62(w) (containing an identical type of WAIT Order).

<sup>199</sup> In its comment letter, ISE notes that MIAX Rule 520 does not address how hidden prices that may result from the display of Do Not Route orders are treated for the requirement to expose orders before attempting to trade against them. See ISE Letter, *supra* note 3, at n. 6. MIAX clarified this point by revising Rule 520 (Limitation on Orders) to add new Interpretation .04 stating that Market Maker orders and quotes displayed at a price other than their limit price or quote price as described in Rule 515(d), and orders subject to the managed interest process—which includes all Do Not Route orders that could not be executed in full and are not cancelled—are not deemed to be “exposed” for purposes of Rule 520. See MIAX Response Letter, *supra* note 4, at 8–9.

In addition, NASDAQ requests clarification on MIAX Rule 516(f) regarding Do Not Route orders and how they operate when the NBBO locks contemporaneously. See NASDAQ Letter, *supra* note 3, at 4. In response, MIAX revised MIAX Rule 516(g) (previously 516(f)) to clarify that a Do Not Route order may execute at a price equal to or better than, but not inferior to, the best away market price, and if, after exhausting interest on MIAX, the best away market remains and the Do Not Route order has not been fully executed, the order will be handled in accordance with MIAX’s managed interest process. See MIAX Response Letter, *supra* note 4, at 7–8. MIAX further notes that in case of contemporaneous locks, Do Not Route orders will be handled as set forth in MIAX Rules 515 and 516. See MIAX Response Letter, *supra* note 4, at 8. Further, ISE requests a technical clarification about the use of the term “away best bid/offer” in MIAX Rule 516(f), and whether it is intended to be different from the term “ABBO.” See ISE Letter, *supra* note 3, at n. 3. In response, MIAX eliminated this term in Rule 516 and instead notes that the specifics for handling a Do Not Route Order are set forth in Rule 515(c)(2), which explains such orders’ handling without using the term “away best bid/offer.” See MIAX Response Letter, *supra* note 4, at 7.

<sup>200</sup> See MIAX Rule 516 for a description of each of the order types. MIAX notes that not all of these order types will be available upon initiation of operations. Rather, MIAX Exchange will update members through Regulatory Circulars as to the order types that will be available initially. See also *infra* Section III(C)(5) (discussing various quote types that market makers may submit). NASDAQ argues that MIAX should be compelled to define which order types will be available and file changes

exception of the AOC Order, which is unique to MIAX, all of these order types are based on similar order types available on other options exchanges.<sup>201</sup> MIAX’s AOC Order is a limit order which is used to provide liquidity during a specific MIAX Exchange mechanism (e.g., the opening imbalance mechanism in MIAX Rule 503) with a time in force that corresponds to the duration of that event.<sup>202</sup> In other words, such an order would automatically expire at the end of the auction or event. AOC Orders are not displayed to any market participant, are not included in the MIAX best bid or offer, are not eligible for trading outside of the event, and may not be routed. The Commission believes that this order type, while not specifically based on an order type on another exchange, is substantially similar to order types approved by the Commission on other exchanges for use in various auction mechanisms, which are similarly not displayed to any participant and have a limited time in force related to the auction, and thus raises no new regulatory issues.<sup>203</sup>

Trades will execute on MIAX when orders or quotes on the MIAX order book match one another.<sup>204</sup> The MIAX system will continuously and automatically match orders pursuant to

when new order types are introduced. See NASDAQ Letter, *supra* note 3, at 3. In response, MIAX represents that it plans to use each of the order types listed in Rule 516 in the foreseeable future and states that it believes that its rule provides adequate detail about each order type. See MIAX Response Letter, *supra* note 4, at 14. In addition, MIAX represents that it will file a proposed rule change whenever it seeks to introduce a new order type. See MIAX Response Letter, *supra* note 4, at 14–15. The Commission agrees that MIAX has appropriately set forth in its rules the order types that it plans to introduce, has represented that it intends to utilize all of the proposed order types contained in its current proposed rules, and has acknowledged that it will need to file a proposed rule change if it ever seeks to introduce additional new order types.

<sup>201</sup> See, e.g., NOM Chapter VI, Section 1(g)(5) (WAIT Order); ISE rule 715(h) (Attributable Order); NOM Chapter VI, Section 1(e)(8) (Intermarket Sweep Order); Phlx Rule 1080(m)(iv)(A) (Do Not Route Order); ISE Rule 714(i) (Customer Cross Order); ISE Rule 715(j) (Qualified Contingent Cross Order); NYSE MKT Rule 131 (Day Order and Good ‘Til Cancelled Order).

<sup>202</sup> See MIAX Rule 517(a)(2)(ii).

<sup>203</sup> See, e.g., CBOE Rule 6.13A, Simple Auction Liaison (“SAL”). See also Securities Exchange Act Release No. 54229 (July 27, 2006), 71 FR 44058 (August 3, 2006) (CBOE–2005–90) (order approving a proposal to adopt a Simple Auction Liaison system to auction qualifying inbound orders for potential price improvement).

<sup>204</sup> NASDAQ points out that MIAX Rules 511 (Acceptance of Quotes and Orders) and 512 (Contract Made on Acceptance of Bid or Offer) appear to be duplicative. See NASDAQ Letter, *supra* note 3, at 4. In response, MIAX has deleted MIAX Rule 512 as duplicative. See MIAX Response Letter, *supra* note 4, at 13.

instances of when orders and quotes will not be displayed or will be displayed at one price and executable at a different price. See MIAX Response Letter, *supra* note 4, at 3–4.

<sup>188</sup> See MIAX Rule 516(b)(4) (Non-displayed Penny Order). This functionality is based on similar rules of other exchanges. See, e.g., CBOE Rule 6.13B (Penny Price Improvement).

<sup>189</sup> See ISE Letter, *supra* note 3, at 2.

<sup>190</sup> See *id.*

<sup>191</sup> See MIAX Response Letter, *supra* note 4, at 9.

<sup>192</sup> See *id.*

<sup>193</sup> See *id.*

<sup>194</sup> See *id.*

either price/time priority or pro-rata priority, as determined by MIAX on a class-by-class basis.<sup>205</sup>

MIAX also will offer additional priority overlays at its discretion on a class-by-class basis, which include “Priority Customer” and “Market Turner” overlays. Priority overlays would only be applicable for pro rata priority.<sup>206</sup> Under the “Priority Customer” overlay, the highest bid and lowest offer will have priority except that Priority Customer orders<sup>207</sup> will have priority over “professional interest”<sup>208</sup> and all Market Maker interest at the same price.<sup>209</sup> If there were two or more Priority Customer orders for the same options series at the same price, priority would be afforded based on the sequence in which such orders were received. This priority overlay is the same as public customer priority overlays that have been approved by the Commission on other exchanges.<sup>210</sup>

Under the “Market Turner” priority overlay, the “Market Turner” refers to the participant that was the first to enter an order or quote at a better price than the previous best disseminated MIAX price, where such order or quote is continuously in the market until the order or quote trades. When this priority overlay is in effect, the Market Turner would have priority at the highest bid or lowest offer that he or she established.<sup>211</sup> The Commission notes that an identical Market Turner priority overlay has been approved for use on another exchange.<sup>212</sup>

In its comment letter, ISE asks for clarification on the proposed execution priority provisions, including priority overlays. Specifically, ISE believes that it is difficult to understand how the different combinations or allocation methodologies, priority overlays, and

entitlements will work.<sup>213</sup> ISE noted that the Form 1, by design, does not require a level of detail and discussion, as well as statutory analysis, which is required in SRO proposed rule changes filed on Form 19b-4.<sup>214</sup> For example, ISE presents an example of an allocation methodology that consists of pro rata with a Priority Customer and Market Turner overlays and asks how the overlays would interact with each other on MIAX.<sup>215</sup> NASDAQ also asks whether the priority provisions contained in MIAX Rule 514, when read in conjunction with the execution processes in MIAX Rule 515, might result in the ability for directing or internalizing orders in a new way.<sup>216</sup> In particular, NASDAQ asks about the interplay between the market turner overlay, non-displayed penny orders, and the liquidity refresh pause.<sup>217</sup>

In response, MIAX amended proposed MIAX Rules 514 and 515 to clarify the operation of two different trade allocation methodologies (*i.e.*, price-time and pro rata) with the possible priority overlays, which includes clarification of the different priority overlays that are applicable to a pro rata allocation methodology.<sup>218</sup> Specifically, MIAX revised proposed Rule 514 to clarify that the Market Turner overlay will never be in effect in conjunction with any other priority overlays, and that the priority overlays are only applicable to the pro rata allocation methodology (*i.e.*, the priority overlays cannot be used in conjunction with the price time methodology).<sup>219</sup> MIAX also clarified in Rule 514(d) that market maker priority quotes have precedence over other professional interest under the pro rata methodology only (*i.e.*, priority quotes would not have precedence under the price time methodology).<sup>220</sup>

In addition, MIAX expanded the discussion in Exhibit E to its Form 1 application to provide a detailed description of how the different trade allocation and priority overlays would operate.<sup>221</sup> MIAX also provided a series of examples to illustrate the proposed operation of its execution rule.<sup>222</sup> MIAX states that the clarifications to the rule text make clear that it has no intention

to allow for the ability for directing or internalizing orders in a way not previously approved by the Commission.<sup>223</sup> Further, in response to NASDAQ, MIAX stated that it does not believe that there is any unique aspect to the operation of the market turner priority overlay, the liquidity refresh pause, or the rules related to non-displayed penny orders on MIAX or the overall functionality of these features when used in combination on the Exchange.<sup>224</sup>

In addition, proposed MIAX rules provide that it may grant Primary Lead Market Makers and Lead Market Makers certain participation entitlements. For example, Primary Lead Market Makers<sup>225</sup> may be entitled to a participation entitlement with respect to each incoming order if they have a priority quote<sup>226</sup> at the National Best Bid and Offer (“NBBO”).<sup>227</sup> The Primary Lead Market Maker participation entitlements will only be in effect if the Priority Customer overlay also is in effect and will apply only to any remaining balance after any Priority Customer orders have first been satisfied.<sup>228</sup> Further, neither a Primary Lead Market Maker nor a Lead Market Maker could be allocated a total quantity greater than the quantity they are quoting at the execution price, and they will not receive any further allocation of an order if they receive a participation entitlement.<sup>229</sup>

Another such entitlement provides that small size orders (*i.e.*, five or fewer contracts) will be allocated in full to the Primary Lead Market Maker if it has a priority quote at the NBBO.<sup>230</sup> In its comment letter, NASDAQ commented that MIAX Rule 514(g)(2), which provides this small order preference to Primary Lead Market Makers, states that small size is “initially” defined as 5 or fewer contracts.<sup>231</sup> NASDAQ argues that

<sup>205</sup> See MIAX Rule 514.

<sup>206</sup> See Amendment No. 1. See also *infra* notes 218 to 224 and accompanying text (describing more completely the revisions MIAX made to the priority rules in response to comments).

<sup>207</sup> MIAX rules define “priority customer” as a person or entity that (i) is not a broker or dealer in securities, and (ii) does not place more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s). See MIAX Rule 100. See also ISE Rule 100(a)(37A) (containing an identical definition of “priority customer”).

<sup>208</sup> Pursuant to MIAX Rule 100, “professional interest” includes: (i) An order that is for the account of a person or entity that is not a Priority Customer, and (ii) an order or non-priority quote for the account of a Market Maker. See also *infra* notes 284–290 for a discussion of “priority” and “non-priority” quotes.

<sup>209</sup> See MIAX Rule 514(d)(1).

<sup>210</sup> See, e.g., CBOE Rule 6.45A(a)(ii)(1).

<sup>211</sup> See MIAX Rule 514(d)(2).

<sup>212</sup> See CBOE Rule 6.45A(a)(iii)(2).

<sup>213</sup> See ISE Letter, *supra* note 3, at 3.

<sup>214</sup> See *id.*

<sup>215</sup> See *id.*

<sup>216</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>217</sup> See *id.*

<sup>218</sup> See MIAX Response Letter, *supra* note 4, at 10–11.

<sup>219</sup> See *id.*

<sup>220</sup> See *id.* See also *infra* Section III(C)(5) for a more detailed discussion of priority quotes.

<sup>221</sup> See MIAX Response Letter, *supra* note 4, at 10.

<sup>222</sup> See Amendment No. 1.

<sup>223</sup> See MIAX Response Letter, *supra* note 4, at 2.

<sup>224</sup> See *id.*

<sup>225</sup> See *supra* Section III(C)(3) (discussing the various categories of Market Makers, including Primary Lead Market Makers).

<sup>226</sup> See *infra* Section III(C)(5) (discussing priority quotes).

<sup>227</sup> See MIAX Rule 514(g). Specifically, the Primary Lead Market Maker’s participation entitlement will be equal to the greater of: (i) The proportion of the total size at the best price represented by the size of its quote, or (ii) 60% of the contracts to be allocated if there is only one other Market Maker quotation at the NBBO or 40% if there are two or more other Market Maker quotes at the NBBO. See MIAX Rule 514(g)(1).

<sup>228</sup> See MIAX Rule 514(g).

<sup>229</sup> See MIAX Rule 514(i)(4).

<sup>230</sup> See MIAX Rule 514(g)(2). The rule provides that MIAX Exchange will review the functioning of this provision quarterly to make sure that small size orders do not account for more than 40% of the volume executed on MIAX.

<sup>231</sup> See NASDAQ Letter, *supra* note 3, at 3.



MIAX should not be allowed to have the discretion to change that number without filing a proposed rule change, and worries that MIAX might seek to unilaterally define such orders as “10 or 50 contracts” without first submitting a rule filing.<sup>232</sup> In response, MIAX amended Rule 514(g)(2) to avoid any doubt by stating that “small size orders are defined as five (5) or fewer contracts.”<sup>233</sup> MIAX further represents that any changes to the small size order rule would be made pursuant to a subsequent proposed rule change filing with the Commission.<sup>234</sup>

MIAX also permits Electronic Exchange Members<sup>235</sup> to utilize Directed Orders.<sup>236</sup> A “Directed Order” refers to an order that an Electronic Exchange Member enters into the MIAX system and directs to a particular Lead Market Maker, including a Primary Lead Market Maker<sup>237</sup> (“Directed Lead Market Maker”). The Lead Market Maker must have an appointment in the relevant options class to receive a Directed Order in that class. A Directed Lead Market Maker may be granted a participation entitlement if he or she has a priority quote at the NBBO.<sup>238</sup> The Directed Lead Market Maker participation entitlement will only be in effect if the Priority Customer overlay also is in effect and will apply only to any remaining balance after Priority Customer orders have first been satisfied. The Commission believes that these participation entitlements for Primary Lead Market Makers and Directed Lead Market Makers are consistent with those that the Commission has approved for other exchanges.<sup>239</sup> Further, the Commission believes that these entitlements are appropriately balanced by the obligations imposed on these classes of market makers, as discussed in detail above.<sup>240</sup> In particular, the Commission notes that Primary Lead Market Makers

and Lead Market Makers are subject to higher quoting obligations than other Registered Market Makers who are not eligible to receive the aforementioned participation entitlements.<sup>241</sup> Therefore, the Commission believes that the proposed rules regarding participation entitlements are consistent with the Act.

In its comment letter, ISE identifies several proposed MIAX rules that ISE believes would benefit from increased detail or description. For example, ISE opines that certain aspects of Rule 514 (regarding quote priority) and Rule 515 (regarding processing of orders and quotes) may be novel.<sup>242</sup> In response, MIAX states that it does not believe that any aspects of MIAX Rules 514 or 515 raise new issues not previously addressed by the Commission; nevertheless MIAX made revisions to those rules to clarify their operation.<sup>243</sup>

In its comment letter, NASDAQ expresses concern over a few MIAX rules that used terms such as “from time to time” or “may.”<sup>244</sup> For example, NASDAQ notes MIAX Rule 514(j) that says MIAX may, from time to time, make available to members the quantity of Priority Customer contracts included in its best bid and offer.<sup>245</sup> NASDAQ questions when MIAX might do this and asks whether this would be a market data feed.<sup>246</sup> NASDAQ asks for a more detailed description of this provision, and recommends that it not be adopted at this time if MIAX is not prepared to roll it out at its commencement of operations.<sup>247</sup> In response, MIAX revised several of its proposed rules to add further detail including changing the terms “from time to time” or “may” to a more definitive “will” or a more specific time frame.<sup>248</sup> For example, MIAX revised MIAX Rule 503(b) concerning openings to clarify that the procedure described in that rule “will” be used to reopen a class after a trading halt.<sup>249</sup> In addition, MIAX amended MIAX Rule 514(h) to provide that

eligible order types for Directed Lead Market Makers will only be set forth in the MIAX Rules and not by regulatory circular.<sup>250</sup> Further, MIAX deleted MIAX Rule 514(j) and instead has included text in MIAX Rule 506 to clarify that it “will” make available to subscribers of its data feeds and to all market participants through the public data feed an indication when there is Public Customer interest included in the MBBO.<sup>251</sup>

In addition, NASDAQ recommends that MIAX Rule 503(h) and (i), which use the term “may,” should be clarified to specify how a closing procedure would be employed after the close of the market.<sup>252</sup> In response, as noted above, MIAX revised MIAX Rule 503 to replace the word “may” with the word “will” to clarify that the procedure described in that rule “will” be used to reopen a class after a trading halt.<sup>253</sup> Further, MIAX deleted MIAX Rule 503(i) concerning rotations in the event of a trading halt in a proprietary product because MIAX does not have any proprietary products at the time and that provision would be inapplicable currently.<sup>254</sup>

NASDAQ also requests clarification on MIAX Rule 503(e)(1) concerning the opening process, and in particular, whether MIAX would consider off-exchange trades or trades on markets other than the primary market when it decides whether to open an option class for trading.<sup>255</sup> In response, MIAX revised MIAX Rule 503(e)(1) to clarify that the opening process will begin following the dissemination of a quote or trade in the “market for the underlying security,” which MIAX previously defined in MIAX Rule 503(d) as either the primary listing market, the primary volume market, or the first market to open the underlying security, as determined on a class-by-class basis and announced to members in advance.<sup>256</sup>

Further, NASDAQ recommends that MIAX Rule 503(g) be clarified to be more specific about when the Help Desk may deviate from the standard manner of the opening procedure.<sup>257</sup> In response, MIAX revised Rule 503 to note that the Help Desk may delay (rather than “deviate”) the opening procedure when necessary in the interests of maintaining a fair and

<sup>232</sup> See *id.*

<sup>233</sup> See MIAX Response Letter, *supra* note 4, at 13.

<sup>234</sup> See *id.*

<sup>235</sup> An Electronic Exchange Member is the holder of a trading permit who is not a Market Maker. See MIAX Rule 100.

<sup>236</sup> See MIAX Rule 514(h).

<sup>237</sup> See *supra* Section III(C)(3) (discussing the various categories of market makers, including Lead Market Makers).

<sup>238</sup> See MIAX Rule 514(h). Specifically, the Directed Lead Market Maker's participation entitlement will be equal to the greater of: (i) The proportion of the total size at the best price represented by the size of its quote; or (ii) 60% of the contracts to be allocated if there is only one other Market Maker quotation at the NBBO or 40% if there are two or more other Market Maker quotes at the NBBO.

<sup>239</sup> See, e.g., ISE Rule 713, Supp. 01 and .03.

<sup>240</sup> See *supra* Section III(C)(3)(b) (discussing market maker obligations).

<sup>241</sup> As discussed above, *supra* Section III(C)(3)(b), Primary Lead Market Makers must provide continuous two-sided quotes 99% of the time in: (i) The lesser of 99% of the series, or 100% of the series minus one put-call pair, in each appointed class that is traded on at least one other exchange; and (ii) 100% of the series in each appointed class that is singly listed on MIAX. See MIAX Rule 604(e)(1). Lead Market Makers must provide continuous two-sided quotes 90% of the time in 90% of the series in each of its appointed classes. See MIAX Rule 604(e)(2).

<sup>242</sup> See ISE Letter, *supra* note 3, at 1.

<sup>243</sup> See MIAX Response Letter, *supra* note 4, at 2.

<sup>244</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>245</sup> See *id.*

<sup>246</sup> See *id.*

<sup>247</sup> See *id.*

<sup>248</sup> See MIAX Response Letter, *supra* note 4, at 12–13.

<sup>249</sup> See *id.*

<sup>250</sup> See *id.* at 13.

<sup>251</sup> See *id.* at 12.

<sup>252</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>253</sup> See MIAX Response Letter, *supra* note 4, at 13.

<sup>254</sup> See *id.* at 12.

<sup>255</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>256</sup> See MIAX Response Letter, *supra* note 4, at 13.

<sup>257</sup> See NASDAQ Letter, *supra* note 3, at 2.



orderly market.<sup>258</sup> MIAX notes that Phlx Rule 1047(c) similarly allows an exchange official to delay the opening procedure, and that the Phlx rule provides the same level of detail as the revised MIAX rule.<sup>259</sup>

NASDAQ believes that MIAX's proposed rule text provides MIAX with too much discretion concerning the order types that initially will be available for use on MIAX, and argues that MIAX should be compelled to define which order types will be available when and file new rule changes when new order types are introduced or when order types are processed differently.<sup>260</sup>

For example, NASDAQ notes MIAX Rule 516 states that "not all order types listed and described in this rule will be initially available for use on the Exchange."<sup>261</sup> NASDAQ argues that, if the functionality related to certain order and quote types is not available on MIAX, then MIAX should specify in its rules what is available and file proposed rule changes when it introduces additional order or quote types and related functionality.<sup>262</sup> In response, MIAX believes it is permissible and appropriate to list in its rules all order and quote types that it intends to use soon after it commences operations, provided that the applicable rules contain a sufficient level of detail about each order and quote type.<sup>263</sup> MIAX believes that MIAX Rules 516 and 517 provide adequate detail on each of the order and quote types listed therein.<sup>264</sup> MIAX further believes that it is appropriate to use a regulatory circular to specify which order and quote types have been activated from among those specified in its rules.<sup>265</sup> MIAX represents that it intends to activate in the foreseeable future each of the

proposed order and quote types contained in its proposed rules.<sup>266</sup>

In addition, NASDAQ notes that MIAX Rule 514(g)(2) states that MIAX will advise membership through a Regulatory Circular when additional order types are eligible to be directed.<sup>267</sup> NASDAQ believes this flexibility may be problematic, and notes that directed orders can warrant additional regulatory scrutiny in light of the issues surrounding participation guarantees that usually accompany directed orders.<sup>268</sup> In response, MIAX amended MIAX Rule 514(h)(2) to remove its ability to specify this information in a regulatory circular and instead represents that it will submit a rule filing with the Commission when it proposes to extend directed order functionality to additional order types.<sup>269</sup> MIAX further represents that any order types eligible to be directed will be set forth in the MIAX rules.<sup>270</sup>

The Commission believes that MIAX Exchange's proposed display, execution, and priority rules discussed above in this section are consistent with the Act. In particular, the Commission finds that the proposed rules are consistent with Section 6(b)(5) of the Act,<sup>271</sup> which, among other things, requires that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating transactions in securities, 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, and to not permit unfair discrimination between customers, issuers, or dealers. The Commission also finds that the proposed rules are consistent with Section 6(b)(8) of the Act,<sup>272</sup> which requires that the rules of an exchange not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The trading rules of MIAX are substantially similar to the current trading rules of other exchanges, as noted above, which were filed with and approved by the Commission (or otherwise became effective) pursuant to Section 19(b) of the Act. Therefore, the Commission believes that these rules raise no new regulatory issues and are consistent with the Act. However,

certain MIAX trading rules are, in fact, novel in some respect or unique to MIAX and may not be similarly based on the existing rules of other exchanges. The trading rules that are novel or unique to MIAX, including the use of eQuotes, priority quotes, and exposure mechanisms, are discussed separately in detail below.

##### 5. eQuotes and Priority Quotes

The MIAX rules provide that Market Makers will be permitted to submit bids and offers to MIAX as orders, Standard quotes, or "eQuotes."<sup>273</sup> Standard quotes refer to the traditional type of quotes that exist on other markets, and submission of a Standard quote by a Market Maker will cancel and replace any previously submitted Standard quote by the Market Maker.<sup>274</sup> In contrast, eQuotes will be quotes with a specific time in force, and Market Makers will be permitted to submit multiple eQuotes to MIAX Exchange (in addition to their single Standard quote).<sup>275</sup> In other words, the submission of an eQuote will not replace an existing Standard quote or eQuote. Thus, while Market Makers could only have one Standard quote active at any one time, they will be permitted to have multiple types of eQuotes active in a single series. The types of eQuotes available on MIAX will include Day eQuotes, Auction or Cancel ("AOC") eQuotes, Opening Only ("OPG") eQuotes, Immediate or Cancel ("IOC") eQuotes, Fill or Kill eQuotes ("FOK"), and Intermarket Sweep eQuotes.<sup>276</sup> MIAX's proposed eQuote types are analogous to order types, often of the same name, that could be used by members and Market Makers on MIAX, as discussed above, except that the eQuotes would be submitted by Market Makers through their quote handling

<sup>258</sup> See MIAX Response Letter, *supra* note 4, at 12.

<sup>259</sup> See *id.* at 14.

<sup>260</sup> See NASDAQ Letter, *supra* note 3, at 2–3.

NASDAQ notes that existing exchanges are required to file detailed rule changes that describe how a proposed rule would work. See *id.* NASDAQ notes that the details and specific functionality are important to users, who need to understand how their orders will be handled in various situations. See *id.* at 3.

<sup>261</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>262</sup> See *id.* at 3. For example, NASDAQ notes that MIAX Rule 516(d) says that Attributable Orders may not be available for all MIAX systems and MIAX would issue a Regulatory Circular specifying which systems and class of securities will have Attributable Orders. See *id.* In response, MIAX has revised Rule 516(e) (previously Rule 516(d)) to clarify that Attributable Orders will be available in the MIAX system on initial launch. See MIAX Response Letter, *supra* note 4, at 8.

<sup>263</sup> See MIAX Response Letter, *supra* note 4, at 14–15.

<sup>264</sup> See *id.* MIAX notes that other exchanges have similar rules, for example C2 Options Exchange.

<sup>265</sup> See *id.*

<sup>266</sup> See *id.* at 14.

<sup>267</sup> See NASDAQ Letter, *supra* note 3, at 3.

<sup>268</sup> See *id.*

<sup>269</sup> See MIAX Response Letter, *supra* note 4, at 13.

<sup>270</sup> See *id.*

<sup>271</sup> 15 U.S.C. 78f(b)(5).

<sup>272</sup> 15 U.S.C. 78f(b)(8).

<sup>273</sup> See MIAX Rule 517.

<sup>274</sup> See MIAX 517(a)(1).

<sup>275</sup> While Market Makers would be permitted to layer the book with multiple types of quotes, MIAX Rule 517(a)(2)(i) provides that one type of eQuote, the Day eQuote, will have limitations as to the number of such quotes that a single Market Maker could place on the same side of an individual option. This limitation is no more than 10 Day eQuotes on the same side of an individual option (as that term is defined in MIAX Rule 100), and the specific limit within this range would be sent to members through a Regulatory Circular. The same limit will apply to all types of Market Makers. MIAX has stated in its Form 1 that it does not intend to allow to the use of Day eQuotes upon initiation of its operations. See Exhibit E of MIAX's Form 1 Application.

<sup>276</sup> See MIAX Rule 517(a)(2) for a description of each of the e-Quote types. MIAX notes that not all of these order types will be available upon initiation of operations. Rather, MIAX will update members through Regulatory Circulars as to the order types that initially will be available and as additional order types become available.

terminal and may receive priority over other orders and quotes, as discussed below.<sup>277</sup>

The Commission believes that the proposed eQuotes provisions are consistent with the Act. The Commission acknowledges that, while Market Maker “quotes” traditionally provide liquidity to the market, MIAX’s proposed eQuotes will allow Market Makers to utilize various types of “quotes” that may instead remove liquidity from the market. However, under MIAX’s proposed rules, only certain types of quotes that provide liquidity (*i.e.*, only Standard quotes and Day eQuotes) will be permitted to count toward a Market Maker’s continuous quoting obligations.<sup>278</sup> In other words, Market Makers on MIAX will still be required to post traditional, continuous two-sided quotes that provide liquidity to the market.

Further, as noted above, the proposed eQuote types are largely analogous to orders, and other markets allow Market Makers to submit similar types of orders that also are not permitted to count towards a Market Maker’s quoting obligations.<sup>279</sup>

The Commission notes that all quote types that may be submitted by Market Makers, whether Standard quotes or eQuotes, must be firm in accordance with the Market Maker’s obligations under the MIAX rules<sup>280</sup> and Rule 602 of Regulation NMS.<sup>281</sup> However, the MIAX rules provide that bids and offers in certain of the eQuote types will not be disseminated to quotation vendors, including AOC eQuotes, OPG eQuotes, IOC eQuotes, FOK eQuotes, and Immediate or Cancel Intermarket Sweep Quotes. The Commission believes that this is consistent with the Act and Rule 602 of Regulation NMS due to the limited time in force or other contingencies associated with these

particular eQuote types. Rule 602 of Regulation NMS generally requires exchanges to make their best bids and offers in U.S.-listed securities available in the consolidated quotation data that is widely disseminated to the public.<sup>282</sup> Paragraph (a)(1)(i)(A) of Rule 602, however, excludes bids and offers communicated on an exchange that either are executed immediately after communication or cancelled or withdrawn if not executed immediately after communication. The Commission believes that IOC eQuotes, FOK eQuotes, and Immediate or Cancel Intermarket Sweep Quotes fall within this exclusion under paragraph (a)(1)(i)(A) of Rule 602 and thus are consistent with the Act. Further, paragraph (a)(1)(i)(B) of Rule 602 excludes any bid or offer communicated prior to the commencement of trading in a security. Accordingly, the Commission notes that OPG eQuotes, which are quotes that can be submitted by a Market Maker only during the opening and will expire at the end of the opening process, are excluded from the dissemination requirements of Rule 602. Finally, as noted above with respect to AOC orders, the Commission has previously approved similar order types as consistent with the Act that are used in various auction mechanisms on other exchanges that are not displayed to any market participants.<sup>283</sup> The Commission believes that AOC eQuotes are analogous to these types of orders, and as such, the Commission believes that MIAX’s proposal to not disseminate AOC eQuotes is consistent with the Act.

On MIAX, all Market Maker quotes will be designated as either “priority quotes” or “non-priority quotes.”<sup>284</sup> As clarified by MIAX in Amendment No. 1, to be considered a *priority quote*, the following standards must be met at the time of execution:

1. The Market Maker must have a two-sided quote pair that is valid width (*i.e.*, it must meet the bid/ask differential requirements in MIAX Rule 603(b)(4)<sup>285</sup> (*i.e.*, a “valid width quote”));

2. The initial size of both of the Market Maker’s bid and offer must meet the minimum quote size requirements of MIAX Rule 604(b)(2);

3. The bid/ask differential of the Market Maker’s two-sided quote pair must meet the priority width requirements specified by MIAX for each option;<sup>286</sup> and

4. Either of the following are true: (i) At the time a locking or crossing quote or order enters the MIAX system, the Market Maker’s two-sided quote pair is a valid width quote resting on the Book; or (ii) immediately prior to the time the Market Maker enters a new quote that locks or crosses the MBBO, the Market Maker must have had a valid width quote already existing (*i.e.*, exclusive of the Market Maker’s new marketable quote or update) among his two-sided quotes.<sup>287</sup>

When determining whether a Market Maker has a valid width quote, MIAX will consider only Standard quotes and Day eQuotes.<sup>288</sup> In the event that a Market Maker has a priority quote on MIAX Exchange, all of that Market Maker’s quotes (including all Standard quotes and eQuotes) would be entitled to have precedence over all other “Professional Interest”<sup>289</sup> (*i.e.*, non-Priority Customer orders, Market Maker orders, and non-priority quotes) at the same price in accordance with MIAX Rule 514(e).<sup>290</sup>

In its comment letter, ISE asks about MIAX Rule 514(e) and whether a Market Maker priority quote has precedence over other professional interest under both pro rata priority and price time priority, as well as when executing against an Intermarket Sweep Order.<sup>291</sup> In response, MIAX revised MIAX Rule 514(e) to clarify that Market Maker priority quotes will have precedence over other professional interest under the pro rata allocation methodology but not under the price time methodology.<sup>292</sup>

Further, ISE commented on MIAX Rule 603 and the priority quote provision. ISE believes that quote width

<sup>277</sup> NASDAQ pointed out an inconsistency between MIAX’s proposed Rule 612(a) and MIAX’s technical system specifications, as the technical specifications say that eQuotes are not considered for purposes of the MIAX Aggregate Risk Manager. See NASDAQ Letter, *supra* note 3, at 3. NASDAQ recommended that MIAX clarify this point in its rule text. See *id.* In response, MIAX states that it believes the rule and the technical specifications are both correct as written. See MIAX Response Letter, *supra* note 4, at 15. Specifically, MIAX notes that it does not plan to support Day eQuotes at its initial launch. See *id.* Accordingly, the technical specifications are accurate in that Day eQuotes would not be considered at this time for purposes of the Aggregate Risk Manager. See *id.* The subsequent introduction by MIAX of Day eQuotes would require corresponding amendments to the technical specifications. See *id.*

<sup>278</sup> See MIAX Rule 604(e); see also *supra* Section III(C)(3)(b) (discussing Market Maker obligations).

<sup>279</sup> See, e.g., ISE Rule 805.

<sup>280</sup> See MIAX Rules 604(d) and 517.

<sup>281</sup> 17 CFR 242.602.

<sup>282</sup> See *id.*

<sup>283</sup> See *supra* note 203 and accompanying text.

<sup>284</sup> See MIAX Rule 517(b).

<sup>285</sup> MIAX Rule 603(b)(4) provides that, following the opening rotation, Market Makers must create differences of no more than \$5 between the bid and offer. Prior to the opening rotation, bid/ask differentials shall be no more than \$25 between the bid and offer for each option contract for which the bid is less than \$2, no more than \$40 where the bid is at least \$2 but does not exceed \$5, no more than \$50 where the bid is more than \$5 but does not exceed \$10, no more than \$80 where the bid is more than \$10 but does not exceed \$20, and no more than \$1 where the bid is more than \$20, provided that MIAX may establish differences other than the above for one or more option.

<sup>286</sup> MIAX added text to MIAX Rule 517(b)(1)(ii) to clarify that MIAX will establish priority quote widths through a proposed rule change filed with the Commission, and the width could be as narrow as one MVP or as wide as, but not wider than, the bid/ask differentials in MIAX Rule 603(b)(4). See Amendment No. 1.

<sup>287</sup> See MIAX Rule 517(b)(1)(i).

<sup>288</sup> See MIAX Rule 517(b)(2).

<sup>289</sup> See MIAX Rule 100 and *supra* note 208.

<sup>290</sup> See MIAX Rules 517(b)(1) and 514(e).

<sup>291</sup> See ISE Letter, *supra* note 3, at 4.

<sup>292</sup> See Amendment No. 1 and MIAX Response Letter, *supra* note 4, at 10. MIAX also clarified that a Market Maker will have precedence over other professional interest when MIAX receives an Intermarket Sweep Order at a price inferior to the NBBO. See *id.*

violations would not be “against the rules” on MIAX, and also questions whether the priority quote provision is an appropriate “heightened” quotation requirement for a Market Maker to obtain a “priority quote”.<sup>293</sup> While stating that it would not object to this approach, ISE requests that the Commission, if it approves MIAX’s registration, to set forth the statutory basis for allowing a Market Maker to obtain a priority over other professional interests via a priority quote.<sup>294</sup> In response, MIAX added text to MIAX Rule 517(b) to clarify that MIAX would establish the priority quote width requirement through a proposed rule change filed with the Commission, and the requirement can have bid/ask differentials as narrow as one minimum price variation or as wide as, but never wider than, the minimum bid/ask differentials contained in MIAX Rule 603.<sup>295</sup> MIAX represented that the priority quote width standards “will be in addition to and generally more stringent than the regulatory requirements applied to Market Makers,” and that “the categorization of Market Maker quotes as priority and non-priority allows the Exchange to provide incentives to its Market Makers to provide tighter markets.”<sup>296</sup> Until MIAX establishes narrower priority quote width requirements, however, the priority quote width will be the standard bid/ask differentials contained in MIAX Rule 603.<sup>297</sup> In addition, MIAX clarified that the initial size of the bid and the offer for a priority quote must meet the minimum size requirement of MIAX Rule 604(b)(2).<sup>298</sup> Further, MIAX affirms that there is, despite ISE’s assumption to the contrary, a maximum market quotation spread requirement during regular market hours.<sup>299</sup> Thus, a violation of the quote width requirements contained in MIAX Rule 603, which is a free-standing rule, would constitute a rule violation separate and apart from the priority quote provisions and would subject a market maker to disciplinary action.<sup>300</sup>

The Commission believes that it is appropriate and consistent with the Act

for MIAX to provide its Market Makers that are meeting their priority quote width obligations with precedence over other Professional interest in the manner that MIAX has proposed. MIAX’s proposed priority quote rule and the precedence afforded to Market Makers that maintain a priority quote provides Market Makers with a benefit in return for the obligations to the market that they have assumed (*e.g.*, the obligation to supply a continuous quote), while Market Makers will have precedence at the same price over other Professional participants that either do not have any obligations (*i.e.*, non-Market Maker Professional interest) or participants that are not quoting valid width markets (*i.e.*, other Market Makers).<sup>301</sup> As discussed in further detail above, the Commission previously has recognized that, due to the obligations imposed on market makers, it is appropriate and consistent with the Act to confer certain corresponding benefits on them.<sup>302</sup> In the event a professional participant wanted to receive the benefits of becoming a market maker, it could apply to register as a market maker, subject to the Exchange’s registration requirements and the participant’s willingness to undertake the applicable obligations.<sup>303</sup> Further, at least one other exchange affords market makers precedence over other professional interest in a manner similar to the MIAX rules.<sup>304</sup>

<sup>301</sup> See Phlx Rule 1000(b)(14) (defining a “professional” to mean any person or entity that (i) is not a broker or dealer in securities, and (ii) places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s), and providing that, subject to limited exceptions, “[a] professional will be treated in the same manner as an off-floor broker-dealer for purposes of Rules 1014(g) \* \* \*”).

<sup>302</sup> See *infra* Section III(C)(3)(b) (discussing Market Maker obligations and benefits).

<sup>303</sup> In Amendment No. 1, MIAX revised the maximum number of Market Makers allowed to quote per class up to 50 from 10. See Amendment 1 (revising rule 602(c)(2) to increase the Class Quoting Limit to 50 from 10). MIAX notes that a class quoting limit of 50 Market Makers is consistent with the practice at other exchanges (*see, e.g.*, CBOE Rule 8.3A and C2 Rule 8.11). See MIAX Response Letter, *supra* note 4, at 12. In addition, the higher limit will provide additional opportunity for interested participants to become Market Makers on MIAX and avail themselves of the benefits afforded to Market Makers on MIAX in return for undertaking the applicable obligations to the MIAX market. See *id.*

<sup>304</sup> See Phlx Rule 1014(g)(vii). Unlike MIAX’s proposed rule, the Phlx rule provides that, for automatically executed trades, all market makers have precedence over other market participants, irrespective of whether such market makers are meeting their bid-ask differential requirements. In addition, NASDAQ BX has filed a proposed rule change to provide similar precedence for its market makers. See Securities Exchange Act Release No. 68041 (October 11, 2012), 77 FR 63903 (October 17, 2012) (BX-2012-065).

## 6. Section 11(a) of the Act

Section 11(a)(1) of the Act<sup>305</sup> prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises discretion (collectively, “covered accounts”), unless an exception applies.

Rule 11a2–2(T) under the Act,<sup>306</sup> known as the “effect versus execute” rule, provides exchange members with an exemption from the Section 11(a)(1) prohibition. Rule 11a2–2(T) permits an exchange member, subject to certain conditions, to effect transactions for covered accounts by arranging for an unaffiliated member to execute the transactions on the exchange. To comply with Rule 11a2–2(T)’s conditions, a member: (1) Must transmit the order from off the exchange floor; (2) may not participate in the execution of the transaction once it has been transmitted to the member performing the execution;<sup>307</sup> (3) may not be affiliated with the executing member; and (4) with respect to an account over which the member has investment discretion, neither the member nor its associated person may retain any compensation in connection with effecting the transaction except as provided in the Rule.

In addition, MIAX’s priority quote proposal establishes a framework that could readily take into account future efforts by MIAX, which would be submitted pursuant to a proposed rule change submitted in accordance with Section 19 of the Act, to reduce and further narrow the maximum permitted width from the standard maximum \$5 width, which is the current standard among U.S. options exchanges. If it does so, MIAX’s system would provide an additional incentive for Market Makers to provide these narrower valid width quotes at all times through affording them precedence in return for their increased obligations.

At the same time, the Commission acknowledges that MIAX’s current proposed bid/ask differential requirement (*i.e.*, \$5 following the opening) is in line with the current industry standard among the options exchanges. Thus, MIAX will provide precedence to Market Makers based on a proposed quote width standard that is, at present, no more strict than other markets. However, as noted above, even if MIAX does not ultimately impose a narrower valid priority quote width, MIAX’s proposal is consistent with the rules of two other exchanges, which provide such precedence to market makers without regard to whether they are meeting their bid-ask differential requirements.

<sup>305</sup> 15 U.S.C. 78k(a)(1).

<sup>306</sup> 17 CFR 240.11a2–2(T).

<sup>307</sup> The member may, however, participate in clearing and settling the transaction. See Securities Exchange Act Release No. 14563 (March 14, 1978), 43 FR 11542 (March 17, 1978) (regarding the NYSE’s Designated Order Turnaround System (“1978 Release”)).

<sup>293</sup> See ISE Letter, *supra* note 3, at 4. MIAX responded that ISE’s assumption was incorrect, and MIAX affirmed that market makers may be subject to disciplinary action if their quotation spread exceeds \$5. See MIAX Response Letter, *supra* note 4, at 11.

<sup>294</sup> See ISE Letter, *supra* note 3, at 5.

<sup>295</sup> See Amendment No. 1 and MIAX Response Letter, *supra* note 4, at 11–12.

<sup>296</sup> See MIAX Response Letter, *supra* note 4, at 11.

<sup>297</sup> See Amendment 1 (revising MIAX Rule 517(b)(ii)).

<sup>298</sup> See MIAX Response Letter, *supra* note 4, at 11.

<sup>299</sup> See *id.*

<sup>300</sup> See *id.*

In a letter to the Commission,<sup>308</sup> MIAX requested that the Commission concur with its conclusion that MIAX members that enter orders into the MIAX trading system satisfy the requirements of Rule 11a2-2(T). For the reasons set forth below, the Commission believes that MIAX members entering orders into the MIAX trading system will satisfy the conditions of Rule 11a2-2(T).

First, Rule 11a2-2(T) requires that orders for covered accounts be transmitted from off the exchange floor. MIAX will not have a physical trading floor, and the MIAX trading system will receive orders from members electronically through remote terminals or computer-to-computer interfaces. In the context of other automated trading systems, the Commission has found that the off-floor transmission requirement is met if a covered account order is transmitted from a remote location directly to an exchange's floor by electronic means.<sup>309</sup> Since the MIAX trading system receives all orders electronically through remote terminals or computer-to-computer interfaces, the Commission believes that the trading system satisfies the off-floor transmission requirement.

Second, Rule 11a2-2(T) requires that the member not participate in the execution of its order once it has been transmitted to the member performing the execution. MIAX has represented that the MIAX trading system will at no time following the submission of an order allow a member or an associated person of such member to acquire control or influence over the result or timing of an order's execution.<sup>310</sup>

According to MIAX, the execution of a member's order is determined solely by what orders, bids, or offers are present in the MIAX trading system at the time the member submits the order and the order priority based on MIAX rules.<sup>311</sup> Accordingly, the Commission believes that a MIAX member will not participate in the execution of its order submitted into the trading system.

Rule 11a2-2(T)'s third condition is that the order be executed by an exchange member who is unaffiliated with the member initiating the order. The Commission has stated that the requirement is satisfied when automated exchange facilities, such as the MIAX trading system, are used, as long as the design of these systems ensures that members do not possess any special or unique trading advantages over non-members in handling their orders after transmitting them to MIAX Exchange.<sup>312</sup> MIAX has represented that the design of its trading system ensures that no member has any special or unique trading advantage over non-members in the handling of its orders after transmitting its orders to MIAX.<sup>313</sup> Based on MIAX's representation, the Commission believes that the MIAX trading system satisfies this requirement.

Fourth, in the case of a transaction effected for an account with respect to which the initiating member or an associated person thereof exercises investment discretion, neither the initiating member nor any associated person thereof may retain any compensation in connection with effecting the transaction, unless the

quote at any time before the order is executed on the Exchange. See MIAX Form 1 Application, Exhibit E. The Commission has stated that the non-participation requirement is satisfied under such circumstances, so long as such modifications or cancellations are also transmitted from off the floor. See 1978 Release, *supra* note 307 (stating that the "non-participation requirement does not prevent initiating members from canceling or modifying orders (or the instructions pursuant to which the initiating member wishes orders to be executed) after the orders have been transmitted to the executing member, provided that any such instructions are also transmitted from off the floor").

<sup>311</sup> See MIAX11(a) Request Letter, *supra* note 308.

<sup>312</sup> In considering the operation of automated execution systems operated by an exchange, the Commission noted that while there is no independent executing exchange member, the execution of an order is automatic once it has been transmitted into each system. Because the design of these systems ensures that members do not possess any special or unique trading advantages in handling their orders after transmitting them to the exchange, the Commission has stated that executions obtained through these systems satisfy the independent execution requirement of Rule 11a2-2(T). See 1979 Release.

<sup>313</sup> See MIAX 11(a) Request Letter, *supra* note 308.

person authorized to transact business for the account has expressly provided otherwise by written contract referring to Section 11(a) of the Act and Rule 11a2-2(T).<sup>314</sup> MIAX members trading for covered accounts over which they exercise investment discretion must comply with this condition in order to rely on the rule's exemption.<sup>315</sup>

## 7. Exposure Mechanisms and Routing

MIAX's system is designed to automatically execute incoming orders or quotes against orders and quotes in its system, provided that such incoming orders and quotes will not be executed at prices inferior to the NBBO.<sup>316</sup> In the event that an incoming order could not be fully executed on MIAX because it would trade through the NBBO (see "Route Timer," below) or, in certain cases, because there is insufficient size on MIAX to execute an incoming order in full when that order exhausts a Market Maker quote (see "Liquidity Refresh Pause," below), its proposed execution rules provide for the use of exposure mechanisms in certain instances.

**Liquidity Refresh Pause.** First, MIAX proposes to implement a "Liquidity Refresh Pause" to allow additional orders or quotes to be received where an incoming order ("initiating order") exhausts a Market Maker's quote that was all or part of the MIAX BBO ("MBBO") and there are unexecuted contracts remaining from the initiating order.<sup>317</sup> Specifically, the Liquidity Refresh Pause would be utilized in instances where MIAX is the only market at the NBBO, and an incoming initiating order is a limit order that crosses the NBBO upon receipt or is a market order and, in either case, could only be partially executed on MIAX where it exhausted a Market Maker quote at the MBBO. In such cases, rather than immediately executing at the next available price, the MIAX system would

<sup>314</sup> 17 CFR 240.11a2-2(T)(a)(2)(iv). In addition, Rule 11a2-2(T)(d) requires a member or associated person authorized by written contract to retain compensation, in connection with effecting transactions for covered accounts over which such member or associated person thereof exercises investment discretion, to furnish at least annually to the person authorized to transact business for the account a statement setting forth the total amount of compensation retained by the member in connection with effecting transactions for the account during the period covered by the statement. See 17 CFR 240.11a2-2(T)(d). See also 1978 Release, *supra* note 307 (stating "[t]he contractual and disclosure requirements are designed to assure that accounts electing to permit transaction-related compensation do so only after deciding that such arrangements are suitable to their interests").

<sup>315</sup> See MIAX 11(a) Request Letter, *supra* note 308.

<sup>316</sup> See MIAX Rule 515.

<sup>317</sup> See MIAX Rule 515(c)(1)(iii).

<sup>308</sup> See Letter from Barbara J. Comly, General Counsel and Corporate Secretary, Miami Holdings, to Richard R. Holley, III, Assistant Director, Division of Trading and Markets, Commission, dated November 30, 2012 ("MIAX 11(a) Request Letter").

<sup>309</sup> See, e.g., Securities Exchange Act Release Nos. 59154 (December 23, 2008) 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48) (order approving proposed rules of BX); 49068, (January 13, 2004), 69 FR 2775 (January 20, 2004) (establishing, among other things, BOX as an options trading facility of BSE); 44983, (October 25, 2001), 66 FR 55225 (November 1, 2001) (approving the PCX's use of the Archipelago Exchange as its equity trading facility); 29237 (May 24, 1991), 56 FR 24853 (May 31, 1991) (regarding NYSE's Off-Hours Trading Facility). See 1978 Release, *supra* note 307. See also Securities Exchange Act Release No. 15533 (January 29, 1979), 44 FR 6084 (January 31, 1979) (regarding the American Stock Exchange ("Amex") Post Execution Reporting System, the Amex Switching System, the Intermarket Trading System, the Multiple Dealer Trading Facility of the Cincinnati Stock Exchange, the PCX Communications and Execution System, and the Philadelphia Stock Exchange ("Phlx") Automated Communications and Execution System) ("1979 Release").

<sup>310</sup> See MIAX 11(a) Request Letter, *supra* note 308. Members may change or cancel an order or

pause the market for a period of time not to exceed one second to allow additional Market Maker orders and quotes and other market participant orders to be submitted.

At the start of the Liquidity Refresh Pause, the MIAX system will broadcast a message to subscribers of MIAX's data feeds, providing a description of the option and the size and side of the order or quote.<sup>318</sup> During the pause, the system will display the remainder of the initiating order at the original NBBO price and, on the opposite side of the market, it will display MIAX's next bid or offer as non-firm.<sup>319</sup>

All market participants may respond to the broadcast message during the Liquidity Refresh Pause.<sup>320</sup> During the Liquidity Refresh Pause, if MIAX receives a new order or quote on the opposite of the market from the initiating order's remaining contracts that locks or crosses the original NBBO, MIAX will immediately execute the remaining contracts at the original NBBO price, provided it would not trade through the current NBBO.<sup>321</sup> If MIAX receives a new order or quote on the same side of the market as the initiating order's remaining contracts that locks or crosses the original NBBO, MIAX will add the new order or quote to the MBBO size and disseminate the updated MBBO.<sup>322</sup> The initiating order and any new orders or quotes on the same side of the market received during the Liquidity Refresh Pause will be processed in the order in which they were received.<sup>323</sup>

<sup>318</sup> See MIAX Rule 515(c)(1)(iii)(A).

<sup>319</sup> See *id.* See also Phlx Rule 1082a(ii)(B)(3) (dissemination of non-firm quotes on opposite side of initiating order during Quote Exhaust timer); Securities Exchange Act Release No. 66315 (February 3, 2012), 77 FR 6828 (February 9, 2012) (Phlx-2012-12) (immediately effective filing to display non-firm quotes in conjunction with Quote Exhaust process).

<sup>320</sup> See MIAX Rule 515(c)(1)(iii)(A)(1)(a).

<sup>321</sup> See MIAX Rule 515(c)(1)(iii)(A)(1)(b).

<sup>322</sup> See MIAX Rule 515(c)(1)(iii)(A)(1)(c). If MIAX receives an IOC or a FOK order on the same side of the market as the initiating order's remaining contracts, the MIAX system will immediately cancel the IOC and FOK orders. If MIAX receives an AOC order on the same side of the market as the initiating order's remaining contracts, the MIAX system will immediately reject the AOC order. If MIAX receives an ISO on the same side of the market as the initiating order's remaining contracts, the Liquidity Refresh Pause will be terminated early and the initiating order and any new orders received during the pause will be processed in the order in which they were received. See MIAX Rule 515(c)(1)(iii)(A)(1)(e)-(g).

<sup>323</sup> See MIAX Rule 515(c)(1)(iii)(A)(1)(c). If all of the remaining contracts in the initiating order and any new orders or quotes on the same side of the market received during the Liquidity Refresh Pause are traded or cancelled during the Liquidity Refresh Pause, the Liquidity Refresh Pause will be terminated early and normal trading will resume. See MIAX Rule 515(c)(1)(iii)(A)(1)(d).

At the end of the Liquidity Refresh Pause, if there are still unexecuted contracts remaining in the initiating order or any new interest on the same side of the market, the MIAX system will execute the remaining contracts in accordance with MIAX's "price protection" process, which ensures that the execution of remaining contracts is limited to only one minimum price variation ("MPV") inferior to the original NBBO price, provided it does not trade through the current NBBO.<sup>324</sup> Specifically, if the next MIAX bid or offer is only one MPV inferior to the original NBBO, the initiating order's remaining contracts will be immediately executed at the next MIAX bid or offer up to the remaining contracts or the size of the MIAX bid or offer, whichever is less, provided the execution does not trade at a price inferior to the current NBBO.<sup>325</sup> If the next MIAX bid or offer is more than one MPV inferior to the original NBBO, then the initiating order will be handled depending on whether the limit price of the initiating order crosses the original NBBO by one or more MPVs. In particular, if the initiating order is a limit order whose limit price crosses the original NBBO by more than one MPV or if it is a market order, the remaining unexecuted portion of the initiating order will be cancelled.<sup>326</sup> If the initiating order is a limit order whose limit price crosses the original NBBO by one MPV, the MIAX system will display and book the initiating order at its limit price. If the limit price would lock or cross the NBBO, then the MIAX system will handle the order in accordance with MIAX's "managed interest process."<sup>327</sup>

Under the "managed interest process," the initiating order will be displayed one MPV away from the current opposite-side NBBO if displaying the order at its limit price

<sup>324</sup> See MIAX Rule 515(c)(1)(iii)(A)(2) and MIAX Form 1 Application, Exhibit E.

<sup>325</sup> If there are still contracts remaining from the initiating order, then the order will be handled pursuant to subparagraphs (1) or (2) of MIAX Rule 515(c)(1)(iii)(A)(2)(a), depending on whether the limit price of the initiating order crosses the original NBBO by one MPV or more.

<sup>326</sup> See MIAX Rule 515(c)(1)(iii)(A)(2)(b)(2).

<sup>327</sup> See MIAX Rule 515(c)(1)(iii)(A)(2)(b)(1). The "managed interest process" is set forth in MIAX Rule 515(c)(2). In addition to its potential use at the end of the Liquidity Refresh Pause, the "managed interest process" would be used more broadly for orders, such as Do Not Route orders, that could not be executed or could not be executed in full and could not be displayed at their limit price because that limit price would lock or cross the NBBO. See MIAX Rule 515(c)(2) (noting specifically that the "managed interest process" could apply pursuant to Rule 515 subparagraphs (c)(1)(i)(A), (c)(1)(ii)(A), (c)(1)(ii)(B)1.a, (c)(1)(ii)(B)2.a, c(1)(iii)(A)2.a.1, (c)(1)(iii)(A)2.b.1, (c)(1)(iii)(B)1.a., and (c)(1)(iii)(B)2.a.).

would lock or cross the NBBO.<sup>328</sup> Should the NBBO price change to an inferior price level, the initiating order's displayed price will continue to re-price so that it is displayed one MPV away from the new NBBO until the order reaches its original limit price, is fully executed, or is cancelled.<sup>329</sup> However, while displaying the initiating order one MPV away from the opposite-side NBBO, the initiating order will be placed on the MIAX book at a price that locks the current opposite-side NBBO.<sup>330</sup> If MIAX receives a new order or quote on the opposite side of the market from the initiating order that could be executed, the MIAX system will immediately execute the remaining contracts to the extent possible at the initiating order's current booked bid or offer price, provided that it does not trade through the current NBBO.<sup>331</sup>

In its comment letter, ISE requests that MIAX clarify the operation of MIAX Rule 515, with reference to the execution price of a resting order that has a non-displayed execution price, including confirmation that the order would not be executed at a price that would trade through the NBBO.<sup>332</sup> ISE further requests clarification as to how certain orders are re-priced, including pursuant to MIAX Rule 515(c)(2) and (d) and whether those rules contemplate that an order will be continuously re-priced, or only re-priced once.<sup>333</sup> NASDAQ asked a question similar to ISE concerning whether the managed interest process would result in a resting order being re-priced only once or

<sup>328</sup> See MIAX Rule 515(c)(2).

<sup>329</sup> See *id.* See also Phlx Rule 1080(m)(iv)(A) (providing a functionally similar process of handling Do Not Route orders, displaying the order one MPV away from the current NBBO, booking the order internally on the Phlx book at a price that would lock the current NBBO, and re-pricing the order until it reaches its limit price in the event the NBBO moves to an inferior level).

<sup>330</sup> See *id.*

<sup>331</sup> See Phlx Rule 1080(m)(iv)(A) (providing that Do Not Route orders that are re-priced to one MPV away from the current NBBO will interact with incoming contra-side orders at the best away market price); see also, e.g. Phlx Rule 1082(a)(ii)(B)(3)(d) (providing that if Phlx receives an order or quote on the opposite side of the market from the initiating quote or order during the Quote Exhaust Timer that locks or crosses the reference price at any time during the Quote Exhaust Timer, it will execute immediately against the initiating quote or order at the reference price, which is price at which the initiating order was initially partially executed).

<sup>332</sup> See ISE Letter, *supra* note 3, at n. 3. MIAX added the phrase "provided that the execution price does not violate the current NBBO" to the place in MIAX Rule 516(f) (which was renumbered to 516(g)) where ISE noted it was missing. See MIAX Response Letter, *supra* note 4, at 6.

<sup>333</sup> See ISE Letter, *supra* note 3, at n. 3. ISE also asks for clarification as to whether Do Not Route orders will be continuously re-priced, or only re-priced once. See *id.* at n. 2.

dynamically as the away markets move.<sup>334</sup>

In response, MIAX revised several provisions in MIAX Rule 515 to clarify the execution price for a resting non-displayed order and to clarify the circumstances under which such orders are re-priced and the circumstances in which the booked price would differ from the NBBO.<sup>335</sup> For example, MIAX amended MIAX Rule 515(c)(2) to clarify that orders in the managed interest process are continuously re-priced.<sup>336</sup> MIAX also clarified in additional spots in MIAX Rules 515, 516, and 529 that such orders will not be executed at a price that would trade through the NBBO.<sup>337</sup>

In addition, NASDAQ notes that MIAX Rule 515 contains a number of situations where the rule provides that a posted order will immediately execute any remaining contracts when an inbound order comes into the MIAX system; however, MIAX's rule does not address what happens if the inbound order does not contain sufficient size to fully execute against the resting order.<sup>338</sup> In response, MIAX revised Rules 515(c) and 515(d) as well as 529(b)(2) to clarify what happens in such situations if an inbound order comes into the MIAX system where such inbound order contains less than the size of the posted order.<sup>339</sup> Specifically, MIAX will disseminate a revised MBBO that reflects the incoming order's remaining size and price.<sup>340</sup> For example, when MIAX is alone at the NBBO and utilizes the Liquidity Refresh Pause, if unexecuted contracts remain from an initiating order, MIAX would revise its MBBO to reflect the balance of the unexecuted order.<sup>341</sup>

**Route Timer.** MIAX also has proposed to subject Public Customer<sup>342</sup> orders to a "Route Timer" when it receives a route-eligible Public Customer order that cannot be filled on MIAX.<sup>343</sup> Specifically, if MIAX receives a Public

Customer order ("initiating order") that is marketable against the NBBO on an away market ("ABBO") and MIAX is not at the NBBO, or MIAX's disseminated market is equal to the ABBO but MIAX has insufficient size to satisfy the initiating order,<sup>344</sup> the order may be subject to a Route Timer not to exceed one second.<sup>345</sup> During the Route Timer, Market Makers and other market participants may interact with the initiating order before MIAX routes the order to an away market or otherwise handles the order in accordance with MIAX Rule 515 or 529, as discussed below.

Like the Liquidity Refresh Pause discussed above, when the Route Timer is activated, MIAX will broadcast a notification ("Route Notification") to subscribers of MIAX's data feeds, providing the size and side of the option.<sup>346</sup> During the timer, the MIAX system will display and book the initiating order at its limit price. However, if the limit price locks or crosses the current opposite side NBBO, the system will display the initiating order one MPV away from the current opposite side NBBO and book the initiating order at price that will internally lock the current opposite side NBBO.<sup>347</sup> The initiating order will remain available for execution up to its original bid or down to its original offer.<sup>348</sup> MIAX will display its next bid or offer on the opposite side of the market from the initiating order as non-firm.<sup>349</sup>

During the Route Timer, if MIAX receives a new order or quote on the opposite side of the market from the initiating order that can be executed, the MIAX system will immediately execute the remaining contracts at the initiating order's current booked bid or offer

price,<sup>350</sup> provided that the execution price does not trade through the current NBBO.<sup>351</sup> If MIAX receives orders or quotes on the same side of the market as the initiating order, such new orders or quotes will join the initiating order in the Route Timer, and the MIAX system will disseminate an updated MBBO that includes the new order or quote's size.<sup>352</sup> If there is a change in the ABBO during the Route Timer that would allow the initiating order to trade on MIAX at the revised NBBO, the Route Timer will be cancelled and regular trading will resume.<sup>353</sup>

At the end of the Route Timer, if necessary, the MIAX system will route ISO orders to away markets disseminating the NBBO.<sup>354</sup> If, after routing to away markets, additional contracts remain to be executed from the initiating order, the MIAX system will handle the remaining interest in accordance with MIAX Rule 515.<sup>355</sup>

**Immediate Routing.** In addition, in limited circumstances where a number of criteria are met, certain Public Customer orders that are eligible for routing could be routed immediately without being subject to the Route Timer ("Immediate Routing").<sup>356</sup> These criteria generally require that a Public Customer order be significantly greater in size than the size of the NBBO posted at away markets and must be received by MIAX at a time when MIAX has significant interest posted at one MPV inferior to the NBBO at away markets. Specifically, an incoming Public Customer order ("initiating order") will be eligible for Immediate Routing if: (i) The initiating order's limit price crosses the opposite side NBBO; (ii) the MBBO is inferior to the NBBO on the opposite

<sup>350</sup> See *supra* note 331.

<sup>351</sup> See *id.*

<sup>352</sup> See MIAX Rule 529(b)(2)(ii).

<sup>353</sup> See MIAX Rule 529(b)(2)(ii). In addition, if, during the Route Timer, the initiating order and all interest on the same side of the market is traded in full or cancelled, the Route Timer will be terminated.

<sup>354</sup> See MIAX Rule 529(b)(2)(iii). At the end of the Route Timer, same side orders or quotes will be handled in the order in which they were received by MIAX. See MIAX Rule 529(b)(2)(ii).

<sup>355</sup> See MIAX Rule 529(b)(2)(iii). MIAX Rule 515 is the general rule governing execution of orders and quotes. It provides a number of different provisions describing how the MIAX system will handle orders that cannot be executed in part or in full. In accordance with Rule 515, depending on a variety of factors, orders may be cancelled, handled in accordance with the "managed interest process," or subject to the Liquidity Refresh Pause, among others. See generally MIAX Rule 515.

<sup>356</sup> See MIAX Rule 529(b)(1). See also *infra* notes 359–363 and accompanying text (concerning ISE's comment regarding the proposed rule's limited applicability to Priority Customers) and Amendment No. 1 (in which MIAX revised the rule to apply to the broader category of Public Customers).

<sup>334</sup> See NASDAQ Letter, *supra* note 3, at 2.

<sup>335</sup> See MIAX Response Letter, *supra* note 4, at 5–6.

<sup>336</sup> See *id.*

<sup>337</sup> See *id.*

<sup>338</sup> See NASDAQ Letter, *supra* note 3, at 4.

<sup>339</sup> See MIAX Response Letter, *supra* note 4, at 6–7.

<sup>340</sup> See MIAX Rules 515(d), 515(c)(1)(iii)(A)(1)(b), and 529(b)(2)(i).

<sup>341</sup> See MIAX Rule 515(c)(1)(iii)(A)(1)(b).

<sup>342</sup> See *supra* note 207.

<sup>343</sup> Orders with certain contingencies, such as IOC orders, and orders marked with a "do not route" qualifier are not eligible for routing. See also *infra* notes 359–363 and accompanying text (concerning ISE's comment regarding the proposed rule's limited applicability to Priority Customers) and Amendment No. 1 (in which MIAX revised the rule to apply to the broader category of Public Customers).

<sup>344</sup> The Route Timer will be utilized when MIAX is not at the NBBO, or is at the NBBO along with other markets but does not have sufficient size to execute a routable Public Customer initiating order in full. In contrast, the Liquidity Refresh Pause, discussed above, will be used when MIAX is the only market at the NBBO. See MIAX Rule 515(c)(1)(iii). The Route Timer is applicable only for Public Customer orders that are routable but do not meet the criteria for immediate routing discussed below. See MIAX Rule 529(b)(2)(i).

<sup>345</sup> See MIAX Rule 529(b)(2). Orders that meet certain criteria may be eligible for immediate routing rather than the one second Route Timer, as discussed further below. See *infra* notes 356–357 and accompanying text.

<sup>346</sup> See MIAX Rule 529(b)(2)(i). See also Amendment No. 1 (in which MIAX removed rule text from Rule 529(b)(2)(i) that also would have provided the NBBO price on the opposite side of the market from the order in the Route Notification).

<sup>347</sup> The internally locked price will not be visible to any participant.

<sup>348</sup> See MIAX Rule 529(b)(2)(i).

<sup>349</sup> See *id.* See also *supra* note 319.

side of the market by one MPV; (iii) the displayed NBBO is not crossed; (iv) the initiating order size is equal to or greater than three times the total size of the away markets represented in the opposite side ABBO; (v) the size of the quotes and orders at the MBBO combined with the total size of the ABBO on the opposite side of the market are equal to or greater than one half the size of the initiating order; (vi) MIAX's disseminated market includes a bid of greater than zero with a size of greater than zero if the order is a sell order; and (vii) the size of MIAX's disseminated market is equal to or greater than three times the total size of the away markets represented in the opposite side ABBO.<sup>357</sup> If a Public Customer order meets the aforementioned criteria, the MIAX system will immediately route ISO orders priced at the ABBO to the away markets disseminating prices better than the MBBO.<sup>358</sup>

In its comment letter, ISE discusses MIAX Rules 515(c) and 529 and notes that MIAX would only route Priority Customer Orders but not other types of public customer orders, like Professional orders.<sup>359</sup> ISE questions whether this distinction is consistent with the Intermarket Linkage Plan and the Act.<sup>360</sup> In addition, ISE requests clarification on the use of the terms "NBBO" and "ABBO" in MIAX Rules 515 and 529, respectively.<sup>361</sup> In response, MIAX revised its Route Timer provisions in MIAX Rules 529 (Order Routing to Other Exchanges) and 503 (Openings on the Exchange) to change all references from "Priority Customer Order" to "Public Customer Order."<sup>362</sup> The term "Public Customer" is defined in MIAX Rule 100 to mean a person that is not a broker or dealer in securities.<sup>363</sup> Accordingly, MIAX has addressed ISE's comment by broadening the types of interest that it will route, as ISE suggested, to include all Public Customer interest, which term includes Professional Customers, in a manner

that is consistent with the Intermarket Linkage Plan and the Act.

The Commission believes that MIAX's proposed exposure and routing mechanisms, including the Liquidity Refresh Pause, Route Timer, and Immediate Routing criteria, are consistent with the Act. Several exchanges have adopted rules that provide for substantially similar exposure functionalities<sup>364</sup> that afford an opportunity for members to electronically "step up" and match a better-priced bid or offer available on another exchange, rather than immediately sending orders to other exchanges for execution.<sup>365</sup>

The Commission believes that MIAX's proposed Liquidity Refresh Pause is consistent with the Act. The rules governing MIAX's Liquidity Refresh Pause are substantially similar to those that the Commission approved for Phlx's "Quote Exhaust" process.<sup>366</sup> However, unlike MIAX, Phlx does not broadcast a message during its Quote Exhaust Timer. The Commission has, however, approved other similar broadcast messages for dissemination during order exposure or flash-type processes on other exchanges.<sup>367</sup> Further, MIAX's Liquidity Refresh Pause will limit the incoming order's execution price to one MPV inferior to the original NBBO price.<sup>368</sup> The Commission believes that this "price protection" functionality of MIAX's Liquidity Refresh Pause can benefit investors by ensuring that, should the NBBO price move to an inferior price during the one second (or less) pause, a limit will be imposed on how far away from the original NBBO price the initiating order may be executed; specifically, it may only be executed

one MPV from the original NBBO price. In addition, an incoming order will not receive an execution pursuant to the Liquidity Refresh Pause process if such order would trade through the then-current NBBO. Further, market participants may utilize an IOC or FOK order to avoid having MIAX potentially subject their order to the Liquidity Refresh Pause process.<sup>369</sup>

Pursuant to MIAX's Immediate Routing process, orders will have to meet a number of criteria to be eligible for immediate routing, as described above. As such, many, if not most, orders likely will be subject to the one second Route Timer, rather than immediately routing to an away exchange displaying the NBBO. MIAX, however, is not required to route orders to away exchanges. Further, market participants may avoid the Route Timer by utilizing an IOC or FOK Order.

In addition, broker-dealers have a duty of best execution.<sup>370</sup> A broker-dealer must carry out a regular and rigorous review of the quality of the options markets to evaluate its best execution policies, including the determination as to which options market it routes customer order flow.<sup>371</sup>

<sup>369</sup> See MIAX Rules 515(c)(1), 515(e), and 515(f).

<sup>370</sup> A broker-dealer has a legal duty to seek to obtain best execution of customer orders. See, e.g., *Newton v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 135 F.3d 266, 269–70, 274 (3d Cir.), cert. denied, 525 U.S. 811 (1998); *Certain Market Making Activities on Nasdaq*, Securities Exchange Act Release No. 40900 (Jan. 11, 1999) (settled case) (citing *Sinclair v. SEC*, 444 F.2d 399 (2d Cir. 1971); *Arleen Hughes*, 27 SEC 629, 636 (1948), aff'd sub nom. *Hughes v. SEC*, 174 F.2d 969 (DC Cir. 1949)). See also *Order Execution Obligations*, Securities Exchange Act Release No. 37619A (Sept. 6, 1996), 61 FR 48290 (Sept. 12, 1996) ("Order Handling Rules Release"). A broker-dealer's duty of best execution derives from common law agency principles and fiduciary obligations, and is incorporated in SRO rules and, through judicial and Commission decisions, the antifraud provisions of the federal securities laws. See *Order Handling Rules Release*, 61 FR at 48322. See also *Newton*, 135 F.3d at 270. The duty of best execution requires broker-dealers to execute customers' trades at the most favorable terms reasonably available under the circumstances, i.e., at the best reasonably available price. *Newton*, 135 F.3d at 270. *Newton* also noted certain factors relevant to best execution—order size, trading characteristics of the security, speed of execution, clearing costs, and the cost and difficulty of executing an order in a particular market. See *id.* at 270 n.2 (citing *Payment for Order Flow*, Exchange Act Release No. 33026 (Oct. 6, 1993), 58 FR 52934, 52937–38 (Oct. 13, 1993) (Proposed Rules)). See *In re E.F. Hutton & Co.*, Securities Exchange Act Release No. 25887 (July 6, 1988). See also *Securities Exchange Act Release No. 34902* (October 27, 1994), 59 FR 55006, 55008–55009 (November 2, 1994) ("Approval of Payment for Order Flow Final Rules"). See also *Securities Exchange Act Release No. 51808* (June 9, 2005), 70 FR 37496 (June 29, 2005) ("NMS Adopting Release"), at 37537 (discussing the duty of best execution).

<sup>371</sup> See NMS Adopting Release, *supra* note 370, at 37538. See also *Securities Exchange Act Release*

<sup>357</sup> See MIAX Rule 529(b)(1).

<sup>358</sup> See *id.* If there are still contracts remaining to be executed from the initiating order after routing, the remaining interest will be handled in accordance with MIAX Rule 515.

<sup>359</sup> See ISE Letter, *supra* note 3, at 3.

<sup>360</sup> See *id.*

<sup>361</sup> See *id.* at n. 7. MIAX notes that the NBBO is the combined best bid and best offer from both the ABBO (all markets excluding MIAX) and the MBBO (MIAX's best bid and best offer). See MIAX Response Letter, *supra* note 4, at 8–9. MIAX believes that the terms are used correctly in MIAX Rules 515 and 529. See MIAX Response Letter, *supra* note 4, at 7.

<sup>362</sup> See MIAX Response Letter, *supra* note 4, at n. 35.

<sup>363</sup> See MIAX Rule 100.

<sup>364</sup> See, e.g., ISE Rule 803, Supplementary Material .02 and Securities Exchange Act Release Nos. 57812 (May 12, 2008), 73 FR 28846 (May 19, 2008) (SR–ISE–2008–28) and 58038 (June 26, 2008), 73 FR 38261 (July 3, 2008) (SR–ISE–2008–50); and CBOE Rule 6.14A(b), HAL.

<sup>365</sup> The Commission notes that it has proposed changes to Rule 602 of Regulation NMS that may affect these electronic "flash" mechanisms, if adopted. See *Securities Exchange Act Release No. 60684* (September 18, 2009), 74 FR 48632, 48633 (September 23, 2009) (File No. S7–21–09).

<sup>366</sup> See Phlx Rule 1082(a)(ii)(B)(3). See also *Securities Exchange Act Release No. 59995* (May 28, 2009), 74 FR 26750 (June 3, 2009) (SR–Phlx–2009–32) (approving Quote Exhaust process) and *supra* note 319.

<sup>367</sup> See, e.g., CBOE Rule 6.14A, Hybrid Agency Liaison ("HAL"). CBOE sends out an "exposure message" for orders received by its HAL system to electronically expose the order at the NBBO price.

<sup>368</sup> Phlx's rule does not include a similar provision. Phlx Rule 1082(a)(ii)(B)(3)(f) provides that the system will conduct an "Acceptable Price Range" test to determine whether there is a valid next available price at which the system may execute the remaining unexecuted contracts. See Phlx Rule 1082(a)(ii)(B)(3)(f).



The protection against trade-throughs supports the broker-dealer's duty of best execution by helping ensure that customer orders are not executed at prices inferior to the best quotations, but it does not supplant or diminish the broker-dealer's responsibility for achieving best execution, including its duty to evaluate the execution quality of markets to which it routes customer orders.<sup>372</sup> Thus, to meet their best execution obligations, broker-dealers will need to consider and evaluate the functioning of the MIAX routing mechanisms and the quality of any resulting executions in making their determination of whether to route customer orders to MIAX.

#### D. Discipline and Oversight of Members

As noted above, one prerequisite for the Commission's grant of an exchange's application for registration is that a proposed exchange must be so organized and have the capacity to be able to carry out the purposes of the Act.<sup>373</sup> Specifically, an exchange must be able to enforce compliance by its members and persons associated with its members with federal securities laws and the rules of the exchange.<sup>374</sup>

MIAX rules codify MIAX's disciplinary jurisdiction over its members, thereby facilitating its ability to enforce its members' compliance with its rules and the federal securities laws.<sup>375</sup> MIAX's rules permit it to sanction members for violations of its rules and violations of the federal securities laws by, among other things, expelling or suspending members; limiting members' activities, functions, or operations; fining or censuring members; suspending or barring a person from being associated with a member; or any other fitting sanction in accordance with MIAX rules.<sup>376</sup>

MIAX's disciplinary and oversight functions will be administered in accordance with Chapter X of the MIAX rules, which governs disciplinary actions. Unless delegated to another SRO pursuant to the terms of an effective 17d-2 plan,<sup>377</sup> MIAX regulatory staff (including regulatory staff of another SRO that may be acting on MIAX Exchange's behalf pursuant to a regulatory services agreement) will,

among other things, investigate potential securities laws violations and initiate charges pursuant to MIAX rules.<sup>378</sup>

Upon a finding of probable cause of a violation within the disciplinary jurisdiction of MIAX Exchange and where further proceedings are warranted,<sup>379</sup> MIAX will conduct a hearing on disciplinary matters before a professional hearing officer<sup>380</sup> and two members of the Business Conduct Committee<sup>381</sup> (the "Panel").<sup>382</sup> The

<sup>378</sup> See MIAX Rules 1002 and 1004. As noted above, MIAX has entered into a RSA with CBOE under which CBOE will perform certain regulatory functions on behalf of MIAX. MIAX may perform some or all of the functions specified in the Chapter X of the MIAX Rules. See also MIAX Rule 1015. CBOE will: assist MIAX in conducting market surveillance and investigations of potential violations of MIAX rules and/or federal securities laws related to activity on MIAX; conduct examinations related to MIAX members' conduct on MIAX; assist MIAX with disciplinary proceedings pursuant to MIAX rules, including issuing charges and conducting hearings; and provide dispute resolution services to MIAX members on behalf of MIAX, including operation of MIAX's arbitration program. See *supra* notes 113–114 and accompanying text.

<sup>379</sup> See MIAX Rule 1004. If there is probable cause for finding a violation, MIAX Exchange regulatory staff will prepare a statement of charges including the allegations and specifying the provisions of the Act and/or MIAX Exchange rules, regulations or policies thereunder alleged to have been violated by the MIAX member or associated person. The CRO must approve the statement of charges.

<sup>380</sup> See MIAX Rule 1015, Interpretation and Policy .01. As noted above, MIAX has entered into a RSA with CBOE to provide certain regulatory functions, including providing professional hearing officers. Under MIAX Rule 1006(a), the professional hearing officer is designated as the Chairman of the Panel. Under MIAX Rule 1006(e), the Panel Chairman has the sole responsibility to determine the time and place of all meetings of the Panel, and make all determinations with regard to procedural or evidentiary matters, as well as prescribe the time within which all documents, exhibits, briefs, stipulations, notices or other written materials must be filed where such is not specified in MIAX rules.

<sup>381</sup> In Amendment No. 1, MIAX proposed new By-Law 4.7 to include additional specifics of the Business Conduct Committee, which shall be appointed by the Chairman of the Exchange Board. Specifically, the Committee, which will not be a Board Committee, will have a minimum of three members and will be composed of a number of individuals as determined by the MIAX Chairman, none of whom shall be Directors of MIAX. In addition, at least one member of the Business Conduct Committee and any panel thereof must be an officer, director or employee of a MIAX member. See Amendment No. 1; see also MIAX Exchange By-Laws Sections 4.1 and 4.7. See also BOX Bylaw 6.08(a) (containing an identical composition for the BOX Hearing Committee).

<sup>382</sup> See MIAX Rule 1006. A Panel may make a determination without a hearing and may impose a penalty as to violations that the Member or associated person has admitted or has failed to answer or that otherwise do not appear to be in dispute. See MIAX Rule 1008. A Member or associated person alleged to have committed a disciplinary violation may submit a written offer of settlement to the Panel, or CRO if a Panel is not yet been appointed, which the Panel or CRO may accept or reject. If the second offer of settlement is rejected (such decision is not subject to review), a

MIAX member (or their associated person) or the MIAX Exchange regulatory staff may petition for review of the decision of the Panel by the MIAX Exchange Board.<sup>383</sup> Any review would be conducted by the MIAX Exchange Board or a committee thereof composed of at least three Directors of the MIAX Exchange Board<sup>384</sup> (whose decision must be ratified by a majority of the MIAX Exchange Board) and such decision will be final.<sup>385</sup> In addition, the MIAX Exchange Board on its own motion may order review of a disciplinary decision.<sup>386</sup>

Appeals from any determination that impacts access to MIAX, such as termination or suspension of membership, will be instituted under, and governed by, the provisions in the Chapter XI of the MIAX Rules. MIAX's Chapter XI applies to persons economically aggrieved by any of the following actions of MIAX including, but not limited to: (a) Denial of an application to become a Member; (b) barring a person from becoming associated with a Member; (c) limiting or prohibiting services provided by the MIAX or services of any exchange member.<sup>387</sup>

Any person aggrieved by an action of MIAX within the scope of the Chapter XI may file a written application to be heard within thirty days<sup>388</sup> after such

hearing will proceed in accordance with MIAX Rule 1006. See MIAX Rule 1009.

<sup>383</sup> See MIAX Rule 1010.

<sup>384</sup> Specifically, the Chairman of the MIAX Board, with the approval of the Board, shall appoint an Appeals Committee to preside over all appeals related to disciplinary and adverse action determinations. See note 49 and accompanying text (detailing the composition of the Appeals Committee). If the Independent Director serving on the Appeals Committee recuses himself or herself from an appeal, due to conflict of interest or otherwise, the Independent Director may be replaced by a Non-Industry Director for purposes of the applicable appeal if there is no other Independent Director able to serve as the replacement. See MIAX Exchange By-Laws Section 4.5(d). See also Amended and Restated By-Laws of BATS Exchange, Inc., Section V, Article 6 (specifying a similar Appeals Committee).

<sup>385</sup> See MIAX Rule 1010.

<sup>386</sup> See *id.*

<sup>387</sup> See MIAX Rule 1100. As noted above, MIAX has entered into a RSA with CBOE under which CBOE will perform certain regulatory functions on behalf of MIAX. CBOE may perform some or all of the functions specified in the Chapter XI of the MIAX Rules. See *supra* note 114. See also MIAX Rule 1106.

<sup>388</sup> An applicant may file for an extension of time as allowed by the Chairman of the Business Conduct Committee within thirty days of the MIAX Exchange's action. An application for an extension will be ruled upon by the Chairman of the Business Conduct Committee, and his ruling will be given in writing. Rulings on applications for extensions of time are not subject to appeal. See MIAX Rule 1101.

No. 49175 (February 3, 2004), 69 FR 6124, 6128 (February 9, 2004) ("Options Concept Release").

<sup>372</sup> See NMS Adopting Release, *supra* note 370, at 37538.

<sup>373</sup> See 15 U.S.C. 78f(b)(1).

<sup>374</sup> See *id.*

<sup>375</sup> See MIAX Rule 1000.

<sup>376</sup> See *id.* See also CBOE Rule 17.1(a) and ISE Rule 1600(a) (containing identical provisions).

<sup>377</sup> See *supra* note 112 (concerning the 17d-2 plans to which MIAX has committed to join).

action has been taken.<sup>389</sup> Applications for hearing and review will be referred to the Business Conduct Committee, which will appoint a hearing panel of no less than three members of such Committee.<sup>390</sup> The decision of the hearing panel made pursuant to Chapter XI of the MIAX rules is subject to review by the MIAX Exchange Board, either on its own motion within 30 days after issuance of the decision, or upon written request submitted by the applicant or the President of MIAX Exchange within 15 days after issuance of the decision.<sup>391</sup> The review would be conducted by the MIAX Exchange Board or a committee of the MIAX Exchange Board composed of at least three directors.<sup>392</sup>

The Commission finds that MIAX's proposed disciplinary and oversight rules and structure, as well as its proposed process for persons economically aggrieved by certain MIAX actions, are consistent with the requirements of Sections 6(b)(6) and 6(b)(7) of the Act<sup>393</sup> in that they provide fair procedures for the disciplining of members and persons associated with members. The Commission further finds that the proposed MIAX rules are designed to provide MIAX Exchange with the ability to comply, and with the authority to enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulations thereunder, and the rules of MIAX.<sup>394</sup>

#### E. Listing

MIAX does not intend to offer original listings when it commences operations. Instead, MIAX will list and trade only equity options that are listed on other national securities exchanges and cleared by the Options Clearing

Corporation. MIAX's listing rules, including the criteria for the underlying securities of the options to be traded, are substantially similar to the rules of other exchanges.<sup>395</sup> The Commission finds that MIAX's proposed initial and continued listing rules are consistent with the Act, including Section 6(b)(5), in that they are designed to protect investors and the public interest and to promote just and equitable principles of trade. Before beginning operation, MIAX will need to become a participant in the Plan for the Purpose of Developing and Implementing Procedures Designed to Facilitate the Listing and Trading of Standardized Options Submitted Pursuant to Section 11A(a)(3)(B) of the Act ("OLPP"). In addition, before beginning operation, MIAX will need to become a participant in the Options Clearing Corporation.

#### IV. Exemption From Section 19(b) of the Act With Regard to CBOE and NYSE Rules Incorporated by Reference

MIAX proposes to incorporate by reference certain CBOE rules concerning arbitration. Thus, MIAX arbitration proceedings will be governed by the applicable CBOE arbitration rules. Specifically, as referenced in MIAX Rule 1107 (Arbitration), MIAX proposes to incorporate by reference Chapter XVIII of CBOE's rulebook (CBOE Arbitration Rules).<sup>396</sup> MIAX also proposes in Rule 1502 to incorporate by reference the CBOE or NYSE rules concerning initial and maintenance margin requirements.

In connection with the proposal to incorporate the CBOE and NYSE rules by reference, MIAX requested, pursuant to Rule 240.0-12 under the Act,<sup>397</sup> an exemption under Section 36 of the Act from the rule filing requirements of Section 19(b) of the Act for changes to the MIAX rules that are effected solely by virtue of a change to a cross-referenced CBOE or NYSE rules.<sup>398</sup> MIAX proposes to incorporate by reference categories of rules, rather than individual rules within a category, that are not trading rules. In addition, MIAX agrees to provide written notice to its members whenever CBOE or NYSE proposes a change to a rule within a cross-referenced category of rules.<sup>399</sup>

<sup>395</sup> See, e.g., ISE Rule 502 (Criteria for Underlying Securities).

<sup>396</sup> In addition, with respect to pre-dispute arbitration agreements, MIAX Rule 1107(c) provides that CBOE Rule 18.35 would apply to disputes between MIAX members and their customers.

<sup>397</sup> 17 CFR 240.0-12.

<sup>398</sup> See Letter from Barbara Comly, General Counsel, MIAX, to Elizabeth M. Murphy, Secretary, Commission, dated November 30, 2012 ("Section 19(b) Exemption Request").

<sup>399</sup> See *id.*

and whenever any such proposed changes are approved by the Commission or otherwise become effective.<sup>400</sup>

Using the authority under Section 36 of the Act,<sup>401</sup> the Commission previously exempted certain SROs from the requirement to file proposed rule changes under Section 19(b) of the Act.<sup>402</sup> The Commission is hereby granting MIAX's request for exemption, pursuant to Section 36 of the Act, from the rule filing requirements of Section 19(b) of the Act with respect to the rules that MIAX proposes to incorporate by reference. The exemption is conditioned upon MIAX providing written notice to MIAX members whenever CBOE or NYSE proposes to change an incorporated by reference rule. The Commission believes that the exemption is appropriate in the public interest and consistent with the protection of investors because it will promote more efficient use of Commission and SROs resources by avoiding duplicative rule filings based on simultaneous changes to identical rule text sought by more than one SRO.

#### V. Conclusion

It is ordered that the application of MIAX Exchange for registration as a national securities exchange be, and it hereby is, granted.

It is further ordered that operation of MIAX Exchange is conditioned on the satisfaction of the requirements below:

A. *Participation in National Market System Plans Relating to Options Trading.* MIAX Exchange must join: (1) The Plan for the Reporting of Consolidated Options Last Sale Reports and Quotation Information (Options Price Reporting Authority); (2) the OLPP; (3) the Linkage Plan; and (4) the Plan of the Options Regulatory Surveillance Authority.

B. *Participation in Multiparty Rule 17d-2 Plans.* MIAX Exchange must become a party to the multiparty Rule 17d-2 agreements concerning options sales practice regulation and market surveillance.

C. *Participation in the Options Clearing Corporation.* MIAX Exchange

<sup>400</sup> MIAX will provide such notice through a posting on the same Web site location where MIAX posts its own rule filings pursuant to Rule 19b-4 under the Act, within the required time frame. The Web site posting will include a link to the location on the FINRA or CBOE Web site where FINRA's or CBOE's proposed rule change is posted. See *id.*

<sup>401</sup> 15 U.S.C. 78mm.

<sup>402</sup> See, e.g., DirectEdge Exchanges Order, BATS Order, and BOX Order, *supra* note 18, and C2 Order, *supra* note 41. In particular, the BOX Order granted relief for BOX's arbitration rule (which is substantively similar to MIAX's proposed rule), which also incorporates the same FINRA rules that MIAX proposes to incorporate.

<sup>389</sup> The application must include: (1) The action for which review is sought; (2) the specific reasons for the applicant's exception to such action; (3) the relief sought; and (4) whether the applicant intends to submit any documents, statements, arguments or other material in support of the application, with a description of any such materials. See MIAX Rule 1101(a).

<sup>390</sup> See MIAX Rule 1102. The decision of the hearing panel will be made in writing and sent to the parties to the proceedings. See MIAX Rule 1103.

<sup>391</sup> See MIAX Rule 1104. The MIAX Exchange Board, or a committee of the MIAX Exchange Board, will have sole discretion to grant or deny either request. See *id.*

<sup>392</sup> See MIAX Rule 1104(b). The MIAX Exchange Board or its designated committee may affirm, reverse, or modify in whole or in part, the decision of the hearing panel. The decision of the MIAX Exchange Board or its designated committee would be final, and must be in writing and would be sent to the parties to the proceeding. See MIAX Rule 1104(c).

<sup>393</sup> 15 U.S.C. 78f(b)(6) and (b)(7), respectively.

<sup>394</sup> See Section 6(b)(1) of the Act, 15 U.S.C. 78f(b)(1).

must become an Options Clearing Corporation participant exchange.

D. *Participation in the Intermarket Surveillance Group.* MIAX Exchange must join the Intermarket Surveillance Group.

E. *Effective Regulation.* MIAX Exchange must have, and represent in a letter to the staff in the Commission's Office of Compliance Inspections and Examinations that it has, adequate procedures and programs in place to effectively regulate MIAX.

F. *Trade Processing and Exchange Systems.* MIAX Exchange must have, and represent in a letter to the staff in the Commission's Division of Trading and Markets that it has, adequate procedures and programs in place, as detailed in Commission Automation Policy Review guidelines, to effectively process trades and maintain the confidentiality, integrity, and availability of MIAX's systems.<sup>403</sup>

It is further ordered, pursuant to Section 36 of the Act,<sup>404</sup> that MIAX shall be exempted from the rule filing requirements of Section 19(b) of the Act with respect to the FINRA and CBOE rules that MIAX proposes to incorporate by reference, subject to the conditions specified in this Order.

By the Commission.

Kevin M. O'Neill,  
Deputy Secretary.

[FR Doc. 2012-29568 Filed 12-6-12; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 30286; 812-13959]

### Cambria Investment Management, L.P. and Cambria ETF Trust; Notice of Application

November 30, 2012.

**AGENCY:** Securities and Exchange Commission ("Commission").

**ACTION:** Notice of an application for an order under section 6(c) of the Investment Company Act of 1940 ("Act") for an exemption from sections 2(a)(32), 5(a)(1), 22(d) and 22(e) of the

Act and rule 22c-1 under the Act, under sections 6(c) and 17(b) of the Act for an exemption from sections 17(a)(1) and 17(a)(2) of the Act, and under section 12(d)(1)(J) of the Act for an exemption from sections 12(d)(1)(A) and (B) of the Act.

**APPLICANTS:** Cambria Investment Management, L.P. ("Cambria") and Cambria ETF Trust (the "Trust").

**SUMMARY:** *Summary of Application:*

Applicants request an order that permits: (a) Actively-managed series of certain open-end management investment companies to issue shares ("Shares") redeemable in large aggregations only ("Creation Units"); (b) secondary market transactions in Shares to occur at negotiated market prices; (c) certain series to pay redemption proceeds, under certain circumstances, more than seven days from the tender of Shares for redemption; (d) certain affiliated persons of the series to deposit securities into, and receive securities from, the series in connection with the purchase and redemption of Creation Units; and (e) certain registered management investment companies and unit investment trusts outside of the same group of investment companies as the series to acquire Shares.

**DATES:** *Filing Dates:* The application was filed on September 12, 2011, and amended on February 29, 2012, July 9, 2012, and November 13, 2012.

**HEARING OR NOTIFICATION OF HEARING:** An order granting the requested relief will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on December 26, 2012, and should be accompanied by proof of service on applicants, in the form of an affidavit or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

**ADDRESSES:** Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090. Applicants: 2321 Rosecrans Avenue, Suite 3225, El Segundo, CA 92045.

**FOR FURTHER INFORMATION CONTACT:** Barbara T. Heussler, Senior Counsel, at (202) 551-6990 or Jennifer L. Sawin, Branch Chief, at (202) 551-6821 (Division of Investment Management,

Office of Investment Company Regulation).

**SUPPLEMENTARY INFORMATION:** The following is a summary of the application. The complete application may be obtained via the Commission's Web site by searching for the file number, or an applicant using the Company name box, at <http://www.sec.gov/search/search.htm> or by calling (202) 551-8090.

### Applicants' Representations

1. The Trust is registered as an open-end management investment company under the Act and is a statutory trust organized under the laws of Delaware. The Trust will initially offer an actively-managed series, Cambria Shareholder Yield ETF (the "Initial Fund"). The investment objective of the Initial Fund will be to seek to preserve and grow capital by investing in domestic equity securities and in particular in companies that will generate investment returns through the payment of dividends and through the appreciation of their share price.

2. Cambria, a California limited partnership, will be the investment adviser to the Initial Fund. Cambria is and any other Adviser (as defined below) is or will be registered as an "investment adviser" under section 203 of the Investment Advisers Act of 1940 ("Advisers Act"). The Adviser may enter into sub-advisory agreements with investment advisers to act as sub-advisers with respect to the Funds (each, a "Subadviser"). Any Subadviser will be registered under the Advisers Act or not subject to such registration. A registered broker-dealer under the Securities Exchange Act of 1934 ("Exchange Act"), which may be an affiliate of the Adviser, will act as the distributor and principal underwriter of the Funds ("Distributor").

3. Applicants request that the order apply to the Initial Fund and any future series of the Trust or of other existing or future open-end management investment companies that may utilize active management investment strategies ("Future Funds"). Any Future Fund will (a) be advised by Cambria or an entity controlling, controlled by, or under common control with Cambria (each such entity and any successor thereto included in the term "Adviser"),<sup>1</sup> and (b) comply with the terms and conditions of the application.<sup>2</sup> The

<sup>1</sup> For purposes of the requested order, a "successor" is limited to an entity that results from a reorganization into another jurisdiction or a change in the type of business organization.

<sup>2</sup> All entities that currently intend to rely on the order are named as applicants. Any entity that

Continued

<sup>403</sup> On November 16, 1989, the Commission published its first Automation Review Policy ("ARP I"), in which the Commission created a voluntary framework for SROs to establish comprehensive planning and assessment programs to determine systems capacity and vulnerability. On May 9, 1991, the Commission published its second Automation Review Policy ("ARP II") to clarify the types of review and reports expected from SROs. See Securities Exchange Act Release Nos. 27445 (November 16, 1989), 54 FR 48703 (November 24, 1989) and 29185 (May 9, 1991), 56 FR 22490 (May 15, 1991).

<sup>404</sup> 15 U.S.C. 78mm.