

company (an “interval fund”) to make repurchase offers of between five and twenty-five percent of its outstanding shares at net asset value at periodic intervals pursuant to a fundamental policy of the interval fund. Rule 23c–3(b)(1) under the Act permits an interval fund to deduct from repurchase proceeds only a repurchase fee, not to exceed two percent of the proceeds, that is paid to the interval fund and is reasonably intended to compensate the fund for expenses directly related to the repurchase. A Fund will not impose a repurchase fee on investors who purchase and tender their shares.

3. Section 23(c)(3) provides that the Commission may issue an order that would permit a closed-end investment company to repurchase its shares in circumstances in which the repurchase is made in a manner or on a basis that does not unfairly discriminate against any holders of the class or classes of securities to be purchased.

4. Applicants request relief under section 6(c), discussed above, and section 23(c)(3) from rule 23c–3 to the extent necessary for the Funds to impose EWCs on shares of the Funds submitted for repurchase that have been held for less than a specified period.

5. Applicants state that the EWCs they intend to impose are functionally similar to CDSLs imposed by open-end investment companies under rule 6c–10 under the Act. Rule 6c–10 permits open-end investment companies to impose CDSLs, subject to certain conditions. Applicants note that rule 6c–10 is grounded in policy considerations supporting the employment of CDSLs where there are adequate safeguards for the investor and state that the same policy considerations support imposition of EWCs in the interval fund context. In addition, applicants state that EWCs may be necessary for the distributor to recover distribution costs. Applicants represent that any EWC imposed by the Funds will comply with rule 6c–10 under the Act as if the rule were applicable to closed-end investment companies. The Funds will disclose EWCs in accordance with the requirements of Form N–1A concerning CDSLs.

#### *Asset-Based Service and Distribution Fees*

1. Section 17(d) of the Act and rule 17d–1 under the Act prohibit an affiliated person of a registered investment company, or an affiliated person of such person, acting as principal, from participating in or effecting any transaction in connection with any joint enterprise or joint arrangement in which the investment

company participates unless the Commission issues an order permitting the transaction. In reviewing applications submitted under section 17(d) and rule 17d–1, the Commission considers whether the participation of the investment company in a joint enterprise or joint arrangement is consistent with the provisions, policies and purposes of the Act, and the extent to which the participation is on a basis different from or less advantageous than that of other participants.

2. Rule 17d–3 under the Act provides an exemption from section 17(d) and rule 17d–1 to permit open-end investment companies to enter into distribution arrangements pursuant to rule 12b–1 under the Act. Applicants request an order under section 17(d) and rule 17d–1 under the Act to the extent necessary to permit the Funds to impose asset-based service and distribution fees. Applicants have agreed to comply with rules 12b–1 and 17d–3 as if those rules applied to closed-end investment companies, which they believe will resolve any concerns that might arise in connection with a Fund financing the distribution of its shares through asset-based service and distribution fees.

3. For the reasons stated above, applicants submit that the exemptions requested under section 6(c) are necessary and appropriate in the public interest and are consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Act. Applicants further submit that the relief requested pursuant to section 23(c)(3) will be consistent with the protection of investors and will insure that applicants do not unfairly discriminate against any holders of the class of securities to be purchased. Finally, applicants state that the Funds’ imposition of asset-based service and distribution fees is consistent with the provisions, policies and purposes of the Act and does not involve participation on a basis different from or less advantageous than that of other participants.

#### **Applicants’ Condition**

Applicants agree that any order granting the requested relief will be subject to the following condition:

Each Fund relying on the order will comply with the provisions of rules 6c–10, 12b–1, 17d–3, 18f–3, 22d–1, and, where applicable, 11a–3 under the Act, as amended from time to time, as if those rules applied to closed-end management investment companies, and will comply with the Sales Charge Rule, as amended from time to time, as if that rule applied to all closed-end management investment companies.

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

**Eduardo A. Aleman,**  
*Assistant Secretary.*

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**BILLING CODE 8011–01–P**

## **SECURITIES AND EXCHANGE COMMISSION**

**[Release No. 34–81263; File No. SR–ISE–2017–32]**

### **Self-Regulatory Organizations; Nasdaq ISE, LLC; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, To Harmonize the Corporate Governance Framework of Nasdaq ISE, LLC With That of The NASDAQ Stock Market LLC, NASDAQ PHLX LLC, and NASDAQ BX, Inc.**

July 31, 2017.

#### **I. Introduction**

On April 11, 2017, Nasdaq ISE, LLC (“ISE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b–4 thereunder,<sup>2</sup> proposed rule changes to its corporate governance documents and trading rules to align its corporate governance framework to the structure of other exchanges owned by its ultimate parent company, Nasdaq, Inc. The proposed rule change was published for comment in the **Federal Register** on May 2, 2017.<sup>3</sup> The Commission received no comments on the proposal. On June 14, 2017, the Commission extended the time period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.<sup>4</sup> On July 6, 2017, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>5</sup> The

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

<sup>2</sup> 17 CFR 240.19b–4.

<sup>3</sup> See Securities Exchange Act Release No. 80530 (April 26, 2017), 82 FR 20508 (“Notice”).

<sup>4</sup> See Securities Exchange Act Release No. 80923, 82 FR 28102 (June 20, 2017).

<sup>5</sup> As discussed further herein, Amendment No. 1, which replaces the original filing in its entirety, includes, among other things: (1) Changes to the Exchange’s proposed Limited Liability Company Agreement (“New LLC Agreement”) and proposed By-Laws (“New By-Laws,” and together with the New LLC Agreement, the “New Governing Documents”) to better align these proposed documents with certain provisions in ISE’s existing governing documents and the governing documents

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Commission is publishing this notice to solicit comment on Amendment No. 1 from interested persons and is approving the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

## II. Background

On June 21, 2016, the Commission approved a proposed rule change relating to a corporate transaction in which Nasdaq, Inc. would become the ultimate parent of ISE (the “Nasdaq Acquisition”), Nasdaq GEMX, LLC (“GEMX”), and Nasdaq MRX, LLC (“MRX,” and together with ISE and GEMX, the “ISE Exchanges”).<sup>6</sup> On June 30, 2016, pursuant to this transaction, Nasdaq, Inc. acquired all of the capital stock of U.S. Exchange Holdings, Inc. (“Exchange Holdings”), and thereby became the indirect, ultimate parent of the ISE Exchanges.<sup>7</sup> Nasdaq, Inc. is also the ultimate parent of NASDAQ BX, Inc. (“BX”), The NASDAQ Stock Market LLC (“Nasdaq”), and NASDAQ PHLX LLC (“Phlx”) and, together with Nasdaq and BX, the “Nasdaq Exchanges”).<sup>8</sup> The

of other exchanges, including provisions concerning limitations on board committee powers, the confidentiality of books and records, the nomination of certain board directors by petition, and the confidentiality of board meetings pertaining to the Exchange’s self-regulatory functions; (2) revisions to the proposed amendments to ISE’s rules regarding ownership, voting, and transfer restrictions relating to certain market maker rights on the Exchange; (3) revisions to the related discussion of the purpose of the proposed changes; (4) clarification of certain aspects of the proposed rule changes (e.g., the nomination of Member Representative members to committees; and certain market maker rights and their related ownership, voting, and transfer restrictions); and (5) certain technical corrections (e.g., correcting incorrect cross references to Exhibits 5A, 5B, 5C, and 5D, updating the proposed implementation date and the description of the Exchange’s most recent annual election of its board, and amending the proposed New LLC Agreement to reflect the current address of the Exchange and its Sole LLC Member). When the Exchange filed Amendment No. 1 with the Commission, it also submitted Amendment No. 1 to the public comment file for SR-ISE-2017-32 (available at: <https://www.sec.gov/comments/sr-ise-2017-32/ise201732.htm>).

<sup>6</sup> See Securities Exchange Act Release No. 78119 (June 21, 2016), 81 FR 41611 (June 27, 2016) (SR-ISE-2016-11; SR-ISEGemini-2016-05; SR-ISEMercury-2016-10) (“Nasdaq Acquisition Order”) (order approving Nasdaq, Inc.’s acquisition of ISE, GEMX (f/k/a ISE Gemini, LLC), and MRX (f/k/a ISE Mercury, LLC)).

<sup>7</sup> See Notice, *supra* note 3, at 20508 n.3. Exchange Holdings is the sole owner of ISE Holdings, Inc. (“ISE Holdings,” and together with Exchange Holdings and Nasdaq, Inc., the “Upstream Owners”), which is the sole owner of 100% of the Exchange’s limited liability company interests. See Notice, *supra* note 3, at 20508–09; see also Nasdaq Acquisition Order, *supra* note 6, at 41611. ISE Holdings is also the sole direct owner of GEMX and MRX. See Nasdaq Acquisition Order, *supra* note 6, at 41611.

<sup>8</sup> See Notice, *supra* note 3, at 20508. See also Nasdaq Acquisition Order, *supra* note 6, at 41611. As a result of this transaction, the ISE Exchanges

Commission notes that the corporate governance documents of ISE, specifically its Third Amended and Restated Limited Liability Company Agreement (“Current LLC Agreement”) and its Second Amended and Restated Constitution (“Current Constitution”) and, together with the Current LLC Agreement, the “Current Governing Documents”) are rules of the Exchange,<sup>9</sup> as are the governing documents of ISE’s Upstream Owners,<sup>10</sup> which include certain provisions that are designed to maintain the independence of ISE’s self-regulatory functions (as well as the self-regulatory functions of the Upstream Owners’ other self-regulatory subsidiaries, *i.e.*, the Nasdaq Exchanges).<sup>11</sup>

The Exchange intends to effect a merger with a newly-formed Delaware limited liability company (“Merger”) under Nasdaq, Inc. that would result in ISE as the surviving entity with new corporate governance documents. In connection with that Merger, the Exchange proposes various changes to its corporate governance documents and rules (“Rules”).<sup>12</sup> Specifically, the Exchange proposes to: (1) Delete the Exchange’s Current LLC Agreement in its entirety and replace it with the New LLC Agreement, which is based on the limited liability company agreement of Nasdaq;<sup>13</sup> (2) delete the Exchange’s Current Constitution in its entirety and replace it with the New By-Laws, which are based on the by-laws of Nasdaq;<sup>14</sup> and (3) amend certain of its Rules to reflect the replacement of the Current Governing Documents with the New Governing Documents.<sup>15</sup>

The Exchange represents that the proposed changes are designed to align the Exchange’s corporate governance framework with the existing structure of the Nasdaq Exchanges, particularly as it relates to the board and committee

and the Nasdaq Exchanges became affiliates. See Nasdaq Acquisition Order, *supra* note 6, at 41611 n.8.

<sup>9</sup> See Securities Exchange Act Release No. 53705 (April 21, 2006), 71 FR 25260, 25262–63 (April 28, 2006) (“ISE HoldCo Order”) (order approving SR-ISE-2006-04).

<sup>10</sup> See Nasdaq Acquisition Order, *supra* note 6, at 41612; Securities Exchange Act Release No. 56955 (December 13, 2007), 72 FR 71979, 71981–82 (December 19, 2007) (order approving SR-ISE-2007-101); ISE HoldCo Order, *supra* note 9, at 25262.

<sup>11</sup> See, e.g., Nasdaq Acquisition Order, *supra* note 6, at 41612–13; ISE HoldCo Order, *supra* note 9, at 25264.

<sup>12</sup> The Rules as proposed to be amended pursuant to the proposed rule change are referred to herein as the “New Rules.”

<sup>13</sup> See Notice, *supra* note 3, at 20508 n.5.

<sup>14</sup> *Id.*

<sup>15</sup> The Exchange states that its affiliates, GEMX and MRX, will submit nearly identical proposed rule changes. See Notice, *supra* note 3, at 20508 n.4.

structure, nomination and election processes, and related governance practices.<sup>16</sup> The Exchange also represents that it is not proposing any amendments to its ownership structure. The Exchange does not propose any amendments to the governing documents of its Upstream Owners.<sup>17</sup> Thus, the provisions in the governing documents of these entities, which were designed to maintain the independence of ISE’s self-regulatory functions, would remain unchanged. The Exchange also represents that it is not proposing any amendments to its Rules at this time, other than to reflect the changes to its governing documents as described in more detail below.<sup>18</sup> The Exchange states that it intends to implement its proposed rule change no later than by the end of the third quarter of 2017.<sup>19</sup>

## III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>20</sup> Specifically, as discussed in more detail below, the Commission finds that the proposed rule change is consistent with Sections 6(b)(1) and 6(b)(3) of the Act,<sup>21</sup> which require, among other things, that a national securities exchange be so organized and have the capacity to carry out the purposes of the Act, and to comply and 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, and assure the fair representation of its members and persons associated with its members in the selection of its directors and administration of its affairs, and provide that one or more directors shall be representative of issuers and investors and not be associated with a member of the exchange, broker, or dealer. Further, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>22</sup> which requires,

<sup>16</sup> See *id.* at 20508.

<sup>17</sup> See generally *id.*; Amendment No. 1.

<sup>18</sup> See Notice, *supra* note 3, at 20509 and 20522. See also Amendment No. 1.

<sup>19</sup> See Amendment No. 1. The Exchange also states that it will alert its members in the form of a regulatory alert to provide notification of the implementation date. *Id.*

<sup>20</sup> In approving these proposed rule changes, the Commission has considered the proposed rules’ impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>21</sup> 15 U.S.C. 78f(b)(1) and (b)(3).

<sup>22</sup> 15 U.S.C. 78f(b)(5).

among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices; to promote just and equitable principles of trade; to foster cooperation and coordination with persons engaged in regulating, clearing, settling, and processing information with respect to, and facilitating 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.

#### A. Ownership of the Exchange

ISE is currently structured as a Delaware limited liability company ("Delaware LLC")<sup>23</sup> and, as discussed above, is a wholly-owned subsidiary of ISE Holdings. ISE Holdings, in turn is a wholly-owned subsidiary of Exchange Holdings, which is wholly-owned by Nasdaq, Inc. Pursuant to the Current LLC Agreement, ISE Holdings is defined as the Sole LLC Member.<sup>24</sup> As the Sole LLC Member, ISE Holdings may assign all (but not less than all) of its interest in the Exchange, subject to prior approval by the Commission pursuant to the rule filing procedures under Section 19 of the Act.<sup>25</sup>

Pursuant to the proposed rule change, ISE will be merged with a newly formed Delaware LLC, whereby ISE will be the surviving entity, governed by the New Governing Documents. ISE Holdings will continue to be the direct owner of ISE and will be defined as the "Company Member" or "Sole LLC Member" in the New LLC Agreement and New By-Laws.<sup>26</sup> Additionally, pursuant to the New LLC Agreement, ISE Holdings will not be permitted to assign, in whole or in part, its limited liability company interest in the Exchange, unless such transfer or assignment is filed with and approved by the Commission pursuant to the rule filing procedures under Section 19 of the Act.<sup>27</sup>

The Commission believes that the proposed restrictions on ISE Holdings'

assignment of its ownership interest in ISE, taken together with restrictions on voting and ownership limitations in the governing documents of ISE's Upstream Owners that were previously approved by the Commission,<sup>28</sup> are designed to minimize the potential that a person could improperly interfere with, or restrict the ability of, the Commission or ISE to effectively carry out its regulatory oversight responsibilities under the Act. The Commission also notes that the restrictions on transfer of ownership interest in the Exchange will be similar to those currently in place. In this regard, the Commission believes the proposed rule change is consistent with Section 6(b)(1) of the Act<sup>29</sup> in particular, which requires that an exchange be organized and have the capacity to be able to carry out the purposes of the Act and to comply, and 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 the exchange.

#### B. Governance of the Exchange

With the replacement of the Current Governing Documents with the New Governing Documents, the Exchange proposes to replace certain provisions pertaining to governance of the Exchange with related provisions that are based on provisions currently in the Nasdaq LLC Agreement and Nasdaq By-Laws.<sup>30</sup> These changes include, among others, provisions governing: the composition of the Exchange's board of directors ("Board" or "Board of Directors," and each member of the Board of Directors a "Director"); the process for nominating, electing, and removing Directors; the filling of vacancies on the Exchange's Board; its board committee structure; and regulatory independence of the

Exchange.<sup>31</sup> As noted above, the Exchange intends that the New Governing Documents would be implemented no later than by the end of the third quarter of 2017.<sup>32</sup>

#### 1. Board of Directors: Powers and Composition

Under the New Governing Documents and consistent with the Current LLC Agreement,<sup>33</sup> the business and affairs of the Exchange will be managed under the discretion of its Board, which will be vested with the power to do any and all acts necessary or for the furtherance of the purposes described in the New LLC Agreement, including fulfilling the Exchange's self-regulatory responsibilities as set forth in the Act.<sup>34</sup> The new Board will also have the power to bind the Exchange and delegate powers,<sup>35</sup> as it does today.<sup>36</sup>

ISE Holdings, as the Sole LLC Member, may determine at any time, in its sole and absolute discretion, the number of Directors to constitute the Board of Directors.<sup>37</sup> At least 20% of the Directors shall be "Member Representative Directors."<sup>38</sup> Additionally, the Board of Directors must include a number of "Non-Industry Directors," including at least one "Public Director" and at least one "issuer representative" (or if the Board consists of ten or more Directors, at least two issuer representatives), that equals or exceeds the sum of the number of Industry Directors and Member Representative Directors.<sup>39</sup>

<sup>31</sup> See Notice, *supra* note 3, at 20514–17; and Amendment No. 1.

<sup>32</sup> See *supra* note 19 and accompanying text.

<sup>33</sup> See Current LLC Agreement, Article II, Section 2.2 and Article V, Sections 5.1 and 5.7; and Current Constitution, Article III, Section 3.1.

<sup>34</sup> See New LLC Agreement, Sections 7, 8, and 9(a).

<sup>35</sup> See New LLC Agreement, Section 9(b).

<sup>36</sup> See Current LLC Agreement, Article II, Section 2.2; and Current Constitution, Article V, Section 5.1.

<sup>37</sup> See New LLC Agreement, Section 9(a).

<sup>38</sup> See *id.* A "Member Representative Director" will be defined as a Director who has been elected or appointed after having been nominated by the Member Nominating Committee or by an Exchange Member pursuant to the New By-Laws and may be, but is not required to be, an officer, director, employee, or agent of an Exchange Member. See New By-Laws, Article I(r).

<sup>39</sup> See New By-Laws, Article III, Section 2(a). A "Non-Industry Director" will be defined as a Director (excluding an officer of the Exchange serving as a Director ("Staff Director")) who is (i) a Public Director; (ii) an officer, director, or employee of an issuer of securities listed on the Exchange; or (iii) any other individual who would not be an Industry Director. See New By-Laws, Article I(w). A "Public Director" will be defined as a Director who has no material business relationship with a broker or dealer, the Exchange or its affiliates, or FINRA. See New By-Laws, Article I(z). An "Industry Director" will be defined as a

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<sup>23</sup> See Current LLC Agreement.

<sup>24</sup> See *id.* The Current Constitution also defines ISE Holdings as the Sole LLC Member of the Exchange and permits assignment of its LLC interest as provided in the Current LLC Agreement. See Current Constitution, Section 1.1.

<sup>25</sup> See Current LLC Agreement, Section 7.1.

<sup>26</sup> See New LLC Agreement, Schedule A; and New By-Laws, Article I(f).

<sup>27</sup> See New LLC Agreement, Section 20. Pursuant to Section 7.1 of the Current LLC Agreement, ISE Holdings may only assign all (but not less than all) of its ownership interest, and any assignment of ISE Holdings' interest in ISE would similarly be subject to approval by the Commission pursuant to the rule filing procedures under Section 19 of the Act.

<sup>28</sup> See Nasdaq Acquisition Order, *supra* note 6, at 41612–17 (discussing provisions, including voting and ownership limitations, in the governing documents of Nasdaq, Inc. and other Upstream Owners that are designed to maintain the independence of their self-regulatory subsidiaries); ISE HoldCo Order, *supra* note 9, at 25262–63 (discussing voting and ownership limitations in the governing documents of ISE Holdings); see also Securities Exchange Act Release No. 76998 (January 29, 2016), 81 FR 6066, 6067, 6069, 6071–73 (February 4, 2016) ("Mercury Exchange Approval") (approving the registration of ISE Mercury, LLC as a national securities exchange and discussing the provisions in the governing documents of ISE Holdings and other Upstream Owners that are designed to preserve the self-regulatory function of the national securities exchanges they control, which includes ISE).

<sup>29</sup> 15 U.S.C. 78(b)(1).

<sup>30</sup> See Notice, *supra* note 3, at 20514–17; and Amendment No. 1.

Additionally, up to two Staff Directors<sup>40</sup> may be elected to the Board.<sup>41</sup> A Director may not be subject to a statutory disqualification.<sup>42</sup> A Director will be removed upon a determination by the Board, by a majority vote of the remaining Directors, that the Director no longer satisfies the classification for which the Director was elected and that the Director's continued service on the Board would violate the board composition requirements.<sup>43</sup>

As discussed in more detail below,<sup>44</sup> the current Board was elected at the Exchange's 2017 annual election of its Board (the "2017 Annual Election," and such Board the "2017 Board"), which was held on June 19, 2017, pursuant to the Current Governing Documents. When the New Governing Documents become operative, the 2017 Board will appoint a Nominating Committee and a Member Nominating Committee.<sup>45</sup> The

Director with direct ties to the securities industry as a result of connections to a broker-dealer, the Exchange or its affiliates, FINRA, or certain service providers to such entities. See Notice, *supra* note 3, at 20516 n.69. See also New By-Laws, Article I(m).

<sup>40</sup> See New By-Laws, Article I(m); see also Notice, *supra* note 3, at 20516 n.72 and accompanying text.

<sup>41</sup> See Current LLC Agreement, Article II, Section 2.2.

<sup>42</sup> See New LLC Agreement, Section 9(a).

<sup>43</sup> See New By-Laws, Article III, Section 2(b). If the remaining term of office of a removed Director is not more than six months, the Board will not be deemed to be in violation of the Article III, Section 2(a) composition requirements during the vacancy by virtue of such vacancy. See *id.*

<sup>44</sup> See *infra* notes 65–68, 70–71, and accompanying text.

<sup>45</sup> See Notice, *supra* note 3, at 20517. The Nominating Committee will consist of no fewer than six and no more than nine members. The number of Non-Industry members on the Nominating Committee shall equal or exceed the number of Industry members on the Nominating Committee. If the Nominating Committee consists of six members, at least two shall be Public members, and if the Nominating Committee consists of seven or more members, at least three shall be Public members. The Member Nominating Committee shall consist of no fewer than three and no more than six members. All members of the Member Nominating Committee shall be a current associated person of a current Exchange Member, and the Board will appoint such individuals after appropriate consultation with representatives of Exchange Members. See New By-Laws, Article III, Sections 6(b)(i) and (iii). See also Notice, *supra* note 3, at 20520–21 (discussing the compositional requirements for, and responsibilities of, the Nominating Committee and Member Nominating Committee).

An "Industry member" will be a member of any committee appointed by the Board that is associated with a broker-dealer as defined in the New By-Laws, Article I(n). A "Non-Industry member" will be defined as a member of any committee appointed by the Board who is (i) a Public member; (ii) an officer or employee of an issuer of securities listed on the Exchange; or (iii) any other individual who would not be an Industry member. See New By-Laws, Article I(x). A "Public member" will be defined as a member of any committee appointed by the Board who has no material business relationship with a broker or dealer, the Company

Member Nominating Committee will nominate candidates for each Member Representative Director position on the Board,<sup>46</sup> as well as nominate candidates for appointment by the Board for each vacant or new position on a committee that is to be filled with a "Member Representative member"<sup>47</sup> under the New By-Laws.<sup>48</sup> If an Exchange Member<sup>49</sup> submits a timely and duly executed written nomination to the Secretary of the Exchange, additional candidates may be added to the List of Candidates<sup>50</sup> for the Member Representative Director positions.<sup>51</sup> These candidates, together with candidates nominated by the Member Nominating Committee, will then be presented to Exchange Members for election.<sup>52</sup> The Nominating Committee

or its affiliates, or FINRA. See New By-Laws, Article I(aa).

<sup>46</sup> Pursuant to the New By-Laws, Member Representative Directors shall be elected to the Board on an annual basis. See New By-Laws, Article II, Section 1(a).

<sup>47</sup> Pursuant to the New By-Laws, a "Member Representative member" will be defined as a member of any committee appointed by the Board who has been elected or appointed after having been nominated by the Member Nominating Committee pursuant to the By-Laws. See New By-Laws, Article I(s). As discussed further below, the required inclusion of such representatives on certain committees, and the process by which they are to be selected, is designed to comply with the fair representation requirements of Section 6(b)(3) of the Act. See *infra* note 102 and accompanying text. See also Amendment No. 1.

In Amendment No. 1, the Exchange clarifies the description of the functions of the Member Nominating Committee. Specifically, the Exchange clarifies that the new Member Nominating Committee is responsible for: (i) The nomination for election of Member Representative Directors to the Board and (ii) the nomination for appointment of Member Representative members to the committees requiring such members. See Amendment No. 1.

<sup>48</sup> See New By-Laws, Article III, Section 6(b).

<sup>49</sup> "Exchange Member" will be defined as any registered broker or dealer that has been admitted to membership in the national securities exchange operated by ISE. See New By-Laws, Article 1(u).

<sup>50</sup> "List of Candidates" will be defined as the list of candidates for Member Representative Director positions to be elected on an Election Date. See New By-Laws, Article 1(p).

"Election Date" will be defined as a date selected by the Board on an annual basis, on which Exchange Members may vote with respect to Member Representative Directors in the event of a Contested Election. See New By-Laws, Article 1(k). See also *infra* note 52, for the definition of "Contested Election."

<sup>51</sup> See New By-Laws, Article II, Section 1(b). See also Amendment No. 1.

<sup>52</sup> If there is only one candidate for each Member Representative Director position to be elected on the annual election date, the Member Representative Directors shall be elected by ISE Holdings as the Sole LLC Member. If, as a result of the nomination and petition process, there are more Member Representative Directors candidates than the number of positions to be elected, each Exchange Member shall have the right to cast one vote for each Member Representative Director, and the candidates who receive the most votes shall be elected to the Member Representative Director

will nominate candidates for all other vacant or new Director positions on the Board.<sup>53</sup>

The Commission believes that the proposed composition of the Exchange's Board satisfies the requirements in Section 6(b)(3) of the Act,<sup>54</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.<sup>55</sup> 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>56</sup> and that they can help to ensure that no single group of market participants has the ability to systematically disadvantage others through the exchange governance

positions. An Exchange Member, however, either alone or together with its affiliates, may not cast votes representing more than 20% of the votes cast for a candidate. See New By-Laws, Article II, Section 1(c) and Section 2. See also New By-Laws, Article 1(g) (defining "Contested Election" as an election for one or more Member Representative Directors for which the number of candidates on the List of Candidates exceeds the number of positions to be elected).

Under the Exchange's Current Governing Documents, six directors on the Board are officers, directors, or partners of Exchange members, and are elected by a plurality of the holders of Exchange Rights ("Exchange Directors"), of which two must be elected by holders of PMM Rights, two must be elected by holders of CMM Rights, and two must be elected by holders of EAM Rights. See Notice, *supra* note 3, at 20510. See also Current Constitution, Article III, Section 3.2. The Exchange states that this current structure was adopted to comply with the fair representation requirements of Section 6(b) of the Act. See Notice, *supra* note 3, at 20510. Because they give members a voice in the Exchange's use of its self-regulatory authority, the Exchange believes that Exchange Directors serve the same function as Member Representative Directors on the boards of the Nasdaq Exchanges. See *id.*

The Exchange notes that the Commission has previously found the Nasdaq LLC Agreement's (1) 20% Member Representative Director requirement, and (2) election process, provide fair representation of Nasdaq members, consistent with the requirements of Section 6(b) of the Act. See Notice, *supra* note 3, at 20510 n.18 (citing Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550, 3553 (January 23, 2006) ("Nasdaq Exchange Order") (granting the exchange registration of Nasdaq Stock Market, Inc.). The Commission notes that the Board compositional requirements and the process for electing Member Representative Directors in the New Governing Documents are based on the parallel requirements in the Nasdaq LLC Agreement.

<sup>53</sup> See New By-Laws, Article III, Section 6(b).

<sup>54</sup> 15 U.S.C. 78f(b)(3).

<sup>55</sup> The Commission also notes that it previously found the compositional requirements for the board of directors of Nasdaq, upon which ISE's proposed requirements are based, to be consistent with Act. See Nasdaq Exchange Order, *supra* note 52, at 3553.

<sup>56</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").

process.<sup>57</sup> As it has previously stated, the Commission believes that public directors can provide unbiased perspectives, which may enhance the ability of the Board to address issues in a non-discriminatory fashion and foster the integrity of the Exchange.<sup>58</sup>

The Commission also believes that the proposed requirement that at least 20% of the Directors be Member Representative Directors, and the means by which they will be chosen by Exchange Members, is consistent with Section 6(b)(3) of the Act,<sup>59</sup> because it provides for the fair representation of members in the selection of directors and the administration of ISE. Section 6(b)(3) of the Act requires that “the rules of the exchange assure a fair representation of its members in the selection of its directors and administration of its affairs and provide that one or more directors shall be representative of issuers and investors and not be associated with a member of the exchange, broker, or dealer.”<sup>60</sup> As the Commission previously has noted, this statutory requirement helps to ensure that members have a voice in the Exchange’s use of its self-regulatory authority, and that the Exchange is administered in a way that is equitable to all those persons who trade on its markets or through its facilities.<sup>61</sup> In addition, the Commission believes that the requirement that at least one director be a Public Director and one an issuer representative satisfies the requirements of Section 6(b)(3) of the Act.<sup>62</sup>

## 2. Transition From Current Board Election Process to the New Election Process

In its filing, the Exchange states that, when it was acquired by Nasdaq, Inc., there were a number of harmonizing changes to its Board that resulted in a complete overlap of directors on the ISE

Boards and the Nasdaq Exchanges (the “Post-Acquisition Board”).<sup>63</sup> ISE also states its belief that the Post-Acquisition Board satisfied the composition requirements contained in both the Current Constitution and the New By-Laws.<sup>64</sup> The Exchange states that the terms of the Directors on the Post-Acquisition Board ended at the 2017 Annual Election,<sup>65</sup> and that all of the Directors on the 2017 Board are Directors that served on the Post-Acquisition Board. The Exchange believes that the 2017 Board satisfies both the board composition requirements in the Current Governing Documents, as well as in the New Governing Documents,<sup>66</sup> and that once the New Governing Documents become operative, no additional actions with respect to the 2017 Board will be required under the Delaware Limited Liability Company Act.<sup>67</sup> Pursuant to the proposal, the 2017 Board will serve until the Exchange’s first annual election of Directors in accordance with the processes under the New Governing Documents in 2018 (“2018 Board”).<sup>68</sup>

The Commission believes the Exchange’s proposal to allow the 2017 Board to continue serving until the 2018 Board would be elected pursuant to the process in the New Governing Documents is consistent with the Act, and in particular Section 6(b)(3) of the Act.<sup>69</sup> The Exchange states that, although the 2017 Board was not nominated or voted upon in accordance with the New Governing Documents, it believes that the composition of the 2017 Board is consistent with the Act, as it still provides for the fair

representation of members and has one or more directors that are representative of issuers and investors and not associated with a member of the exchange, broker, or dealer. Specifically, the Exchange states that six Directors are officers, directors, or partners of Exchange members, as required by Section 3.2(b) of the Current Constitution, and were elected by a plurality of the holders of “Exchange Rights.”<sup>70</sup> These Exchange Directors were subject to the full petition and voting process by membership in accordance with Articles II and III of the Current Constitution, which process the Commission previously found to satisfy the requirements of the Act.<sup>71</sup> The Exchange believes that the Exchange Directors serve the same function as the Member Representative Directors under the proposed board structure, as both directorships give Exchange members a voice in the Exchange’s use of its self-regulatory authority.<sup>72</sup> The Exchange also notes that only its corporate governance structure would change under the proposed rule change, and that its membership has remained substantially the same both before and after the 2017 Annual Election.<sup>73</sup> Additionally, the Commission notes that, under the Current Governing Documents, the 2017 Board will be required to include two Directors that are “Public Directors.”<sup>74</sup>

<sup>70</sup> See Amendment No. 1. See also Notice, *supra* note 3, at 20510 and 20513–14 (discussing the Exchange’s current process for the nomination and election of Directors, including the Exchange Directors).

“Exchange Rights” currently means, collectively, PMM Rights, CMM Rights, and EAM Rights, which are the trading and other rights associated with the Exchange’s three classes of membership. See Rule 100(a)(17); Current LLC Agreement, Article VI; and Current Constitution, Section 13.1(q). See also Rules 100(a)(11), 100(a)(14), and 100(a)(36); and Current Constitution, Sections 13.1(g), 13.1(j), and 13.1(bb). Under the New Rules, “Exchange Rights” will be defined in New Rule 100(a)(19) as the PMM Rights, CMM Rights, and EAM Rights, which will be defined in New Rules 100(a)(39), 100(a)(11), and 100(a)(15), respectively, and as discussed further below. See *infra* Section III.C. (discussing amendments to the Exchange’s Rules).

<sup>71</sup> See Amendment No. 1; Securities Exchange Act Release No. 42455 (February 24, 2000), 65 FR 11401 (March 2, 2000) (“ISE Exchange Approval”) (granting ISE’s application for registration as a national securities exchange); and ISE HoldCo Order, *supra* note 9, at 25265.

<sup>72</sup> See Notice, *supra* note 3 at 20517. See also Amendment No. 1.

<sup>73</sup> See Amendment No. 1.

<sup>74</sup> See Current Constitution, Section 3.2(b).

Pursuant to the Exchange’s Current Constitution, a “Public Director” means a non-industry representative who has no material relationship with a broker or dealer or any affiliate of a broker or dealer or the Exchange or any affiliate of the Exchange. See Current Constitution, Sections 3.2(b) and 13.1(cc).

<sup>57</sup> See, e.g., Securities Exchange Act Release No. 68341 (December 3, 2012), 77 FR 73065, 73067 (December 7, 2012) (“MIAX Exchange Order”) (granting the exchange registration of the Miami International Securities Exchange LLC).

<sup>58</sup> See, e.g., Securities Exchange Act Release No. 53382 (February 27, 2006), 71 FR 11251, 11261 (March 6, 2006) (order approving the New York Stock Exchange, Inc.’s business combination with Archipelago Holdings, Inc.); Nasdaq Exchange Order, *supra* note 52, at 3553; and Securities Exchange Act Release No. 62716 (August 13, 2010), 75 FR 51295, 51298 (August 19, 2010) (approving the application of BATS Y-Exchange, Inc. for registration as a national securities exchange).

<sup>59</sup> 15 U.S.C. 78f(b)(3).

<sup>60</sup> *Id.*

<sup>61</sup> See, e.g., Nasdaq Exchange Order, *supra* note 52; and Securities Exchange Act Release No. 58375 (August 18, 2008), 73 FR 49498 (August 21, 2008) (order granting the exchange registration of BATS Exchange, Inc.).

<sup>62</sup> 15 U.S.C. 78f(b)(3).

<sup>63</sup> See Notice, *supra* note 3, at 20516.

<sup>64</sup> See Amendment No. 1.

<sup>65</sup> The Exchange states that it held its 2017 Annual Election on June 19, 2017, in accordance with the nomination, petition, and voting processes set forth in the Current Governing Documents. See *id.*

<sup>66</sup> The Commission notes that if the Board of Directors in place at the time the New Governing Documents become effective does not satisfy the requirements in the New Governing Documents, the Exchange would need to comply with the procedures for removing Directors and filling vacancies pursuant to the New Governing Documents. See, e.g., *supra* notes 43, 46, and 51–53 and accompanying text.

<sup>67</sup> See Amendment No. 1. As discussed above, the Exchange proposes that, if approved, the New Governing Documents would be made effective no later than by the end of the third quarter of 2017. See Amendment No. 1; see also *supra* note 18 and accompanying text.

<sup>68</sup> See Notice, *supra* note 3, at 20517. See also Amendment No. 1.

<sup>69</sup> See *supra* notes 54–62 and accompanying text (discussing the requirements of Section 6(b)(3) and the Commission’s belief that the compositional requirements for the Board of Directors, and the process for electing such Directors under the New Governing Documents, are consistent with those requirements).

### 3. Committees of the Board

Pursuant to the New By-Laws, the Exchange may establish committees composed solely of Directors. Specifically, the Exchange may establish an Executive Committee and a Finance Committee, and shall establish a Regulatory Oversight Committee ("ROC").<sup>75</sup> The Exchange shall also establish certain committees not composed solely of Directors. Specifically, the Exchange shall establish a Nominating Committee and a Member Nominating Committee, which would be elected on an annual basis by ISE Holdings, as the Sole LLC Member,<sup>76</sup> and a Quality of Markets Committee ("QMC").<sup>77</sup> The New LLC Agreement will provide that, to the extent provided in the resolution of the Board, any committee that consists solely of one or more Directors shall have and may exercise all the powers and the authority of the Board in the management of the business and affairs of the Exchange.<sup>78</sup> The powers of any such committee would, however, be limited with respect to approving any matters pertaining to the self-regulatory function of the Exchange or relating to the structure of the market the Exchange regulates.<sup>79</sup>

The term "non-industry representative" means any person who would not be considered an "industry representative," as well as (i) a person affiliated with a broker or dealer that operates solely to assist the securities-related activities of the business of non-member affiliates, or (ii) an employee of an entity that is affiliated with a broker or dealer that does not account for a material portion of the revenues of the consolidated entity, and who is primarily engaged in the business of the non-member entity. *See* Current Constitution, Section 13.1(w).

The term "industry representative" means a person who is an officer, director, or employee of a broker or dealer or who has been employed in any such capacity at any time within the prior three (3) years, as well as a person who has a consulting or employment relationship with or has provided professional services to the Exchange and a person who had any such relationship or provided any such services to the Exchange at any time within the prior three (3) years. *See* Current Constitution, Section 13.1(t).

<sup>75</sup> *See* New By-Laws, Article III, Section 5.

The Exchange states that the proposed provisions relating to the standing committees are substantially similar to the provisions in Section 9(g) of the Nasdaq LLC Agreement with respect to standing committees. *See* Amendment No. 1.

<sup>76</sup> *See* New By-Laws, Article III, Section 6(b). *See also supra* note 45 (describing the compositional requirements of these committees).

The Board may also designate additional committees consisting of one or more Directors or other persons. *See* New LLC Agreement, Section 9(g).

<sup>77</sup> *See* New By-Laws, Article III, Section 6(c). *See also infra* note 102 and accompanying text (describing the compositional requirements of the QMC).

<sup>78</sup> *See* New LLC Agreement, Section 9(g)(v).

<sup>79</sup> *See id.* *See also* Amendment No. 1. The Exchange notes that the proposed limitation is

The Exchange proposes that the Executive Committee be an optional committee, to be appointed only if deemed necessary by the Board.<sup>80</sup> Because the Executive Committee will have the powers and authority of the Board in the management of the business and affairs of the Exchange between meetings of the Board, its composition must reflect that of the Board. Accordingly, if established, the number of Non-Industry Directors on the Executive Committee must equal or exceed the number of Industry Directors and the percentages of Public Directors and Member Representative Directors must be at least as great as the corresponding percentages on the Board as a whole.<sup>81</sup>

The Board would retain oversight of the financial operations of the Exchange instead of delegating these functions to a standing committee, but would have the option to appoint a Finance Committee at the Board's discretion.<sup>82</sup> The Finance Committee would advise the Board with respect to the oversight of the financial operations and conditions of the Exchange, including recommendations for the Exchange's annual operating and capital budgets and proposed changes to the rates and fees charged by the Exchange.

The Exchange proposes to eliminate its current Finance and Audit Committee and to have the committee's functions performed by Nasdaq, Inc.'s Audit Committee ("Nasdaq Audit Committee"), which is composed of at least three directors of Nasdaq, Inc., all of whom must satisfy the standards for independence set forth in Section 10A(m) of the Act<sup>83</sup> and Nasdaq's rules.<sup>84</sup> The Exchange notes that the Nasdaq Audit Committee has broad authority to review the financial information that will be provided to shareholders of Nasdaq, Inc. and others; systems of internal controls; and audit, financial reporting, and legal and

based on substantially similar language in Section 5.2(ii) of MRX's Constitution and is intended to assure the fair administration and governance of the Exchange. The Exchange does not have this limitation in Section 5.2 of its Current Constitution with respect to any Board committees set up by Board resolution, and is therefore proposing to follow the more current MRX standard. *See* Amendment No. 1.

<sup>80</sup> *See* New By-Laws, Article III, Section 5(a).

<sup>81</sup> *See id.*

<sup>82</sup> *See* New By-Laws, Article III, Section 5(b).

<sup>83</sup> *See* U.S.C. 78j-1(m).

<sup>84</sup> *See* Nasdaq, Inc. By-Laws, Section 4.13(g).

The current Finance and Audit Committee must be composed of at least three (3) and not more than five (5) directors, all of whom must be non-industry representatives and must be "financially literate" as determined by the Board. *See* Current Constitution, Article V, Section 5.5.

compliance processes.<sup>85</sup> The Exchange states that, to the extent the current Finance and Audit Committee oversees the Exchange's financial reporting process, its activities are duplicative of the activities of the Nasdaq Audit Committee, which is also charged with providing oversight over financial reporting and independent auditor selection for Nasdaq, Inc. and all of its subsidiaries.<sup>86</sup> The Exchange also notes that the unconsolidated financial statements of the Exchange will still be prepared for each fiscal year.<sup>87</sup>

The Exchange will also have a Regulatory Oversight Committee ("ROC") under the New Governing Documents, which will have broad authority to oversee the adequacy and effectiveness of the Exchange's regulatory and self-regulatory responsibilities.<sup>88</sup> The ROC will consist of three members, each of whom must be a Public Director and an "independent director," as defined in Nasdaq Rule 5605.<sup>89</sup>

Pursuant to the New By-Laws, the Exchange will also have a Chief Regulatory Officer ("CRO"), as it does currently.<sup>90</sup> The new CRO will have general responsibility for the supervision of the regulatory operations

<sup>85</sup> *See* Notice, *supra* note 3, at 20519.

<sup>86</sup> *See id.*

<sup>87</sup> *See id.* The Commission notes that registered national securities exchanges have an ongoing requirement to comply with the requirements of Form 1, which include filing audited financial statements with the Commission on an annual basis. *See* Form 1, General Instructions A.2 and Exhibit I, 17 CFR 249.1; and 17 CFR 240.6a-2(b)(1) (requiring a national securities exchange to file each year, as an amendment to its Form 1, Exhibit I (which requires a Form 1 applicant to file audited financial statements), as of the latest fiscal year of the exchange).

<sup>88</sup> *See* New By-Laws, Article III, Section 5(c). Currently, the Exchange's regulatory oversight activities are performed by the Exchange's Corporate Governance Committee, which will not exist under the new governance structure. *See* Notice, *supra* note 3, at 20520.

The Exchange also states that regulatory oversight functions formerly performed by the Finance and Audit Committee may be assumed by the ROC, and that like the ROCs of the Nasdaq Exchanges, the ISE ROC, because of its broad authority to oversee the adequacy and effectiveness of the Exchange's self-regulatory responsibilities, will be able to maintain oversight over controls in tandem with the Nasdaq Audit Committee's overall oversight responsibilities.

<sup>89</sup> *See* New By-Laws, Article III, Section 5(c).

<sup>90</sup> *See* Notice, *supra* note 3, at 20521 (noting that, although not expressly in its Current Governing Documents, the position of chief regulatory officer has long existed at the Exchange). *See also* New By-Laws, Article IV, Section 7.

In addition to the CRO, pursuant to the New LLC Agreement, the Exchange's officers will include: a Chief Executive Officer, a President, Vice Presidents, a Chief Regulatory Officer, a Secretary, an Assistant Secretary, a Treasurer, and an Assistant Treasurer. *See* New By-Laws, Article IV, Sections 4-11.

of the Exchange and will meet with the ROC in executive session at regularly scheduled meetings of the ROC, and at any time upon request of the CRO or any member of the ROC.<sup>91</sup>

The ROC will assess the Exchange's regulatory performance, assist the Board in reviewing the regulatory plan and the overall effectiveness of the Exchange's regulatory functions, review the Exchange's regulatory budget and inquire into the adequacy of resources available in the budget for regulatory activities, and be informed about the compensation and promotion or termination of the CRO.<sup>92</sup>

The Exchange also proposes that the Internal Audit Department of Nasdaq, Inc. ("Nasdaq Internal Audit Department") would report to the Board on all Exchange-related internal audit matters and direct such reports to the new ROC.<sup>93</sup> In addition, to ensure that the Board retains authority to direct the Nasdaq Internal Audit Department's activities with respect to the Exchange, the Nasdaq Internal Audit Department's written procedures will stipulate that the ROC may, at any time, direct the Nasdaq Internal Audit Department to conduct an audit of a matter of concern and report the results of the audit both to the ROC and the Nasdaq Audit Committee.<sup>94</sup>

The Exchange also proposes to eliminate its current Compensation Committee and its Corporate Governance Committee.<sup>95</sup> The Compensation Committee is primarily charged with reviewing and approving compensation policies and plans for the Chief Executive Officer and other senior executive officers of the Exchange.<sup>96</sup> Under the new governance structure, the functions of the Compensation Committee will be performed by Nasdaq, Inc.'s management compensation committee or, to the extent that policies, programs, and practices must be established for any Exchange officers or employees who are not also officers or employees of Nasdaq, Inc., the full Board.<sup>97</sup> The Corporate Governance Committee is primarily charged with: (i) Nominating candidates for all vacant or new non-

industry representative positions on the Board, (ii) overseeing the Exchange's regulatory activities and program, and (iii) overseeing and evaluating the governance of the Exchange.<sup>98</sup> Under the new governance structure, the functions of the Corporate Governance Committee will be performed by the new Nominating Committee, the new ROC, or, if required, the full Board.<sup>99</sup>

As discussed above, the Nominating Committee and Member Nominating Committee will have responsibility for, among other things, nominating candidates for election to the Board. On an annual basis, the members of these committees will nominate candidates for the succeeding year's respective committees to be elected by ISE Holdings.<sup>100</sup>

Finally, the Quality of Markets Committee ("QMC") will have the following functions: (i) To provide advice and guidance to the Board on issues relating to the fairness, integrity, efficiency, and competitiveness of the information, order handling, and execution mechanisms of the Exchange from the perspective of investors, both individual and institutional, retail firms, market making firms, and other market participants; and (ii) to advise the Board with respect to national market system plans and linkages between the facilities of the Exchange and other markets.<sup>101</sup> At least 20% of the QMC must be composed of Member Representative members, and the Non-Industry members on the QMC must equal or exceed the sum of Industry members and Member Representative members.<sup>102</sup>

<sup>98</sup> See *id.* at 20520. See also Current Constitution, Section 5.4.

<sup>99</sup> See Notice, *supra* note 3, at 20520.

<sup>100</sup> See New By-Laws, Article III, Section 6(c). See also *supra* notes 46–53 and accompanying text. Additional candidates for the Member Nominating Committee may be nominated and elected by Exchange Members pursuant to a petition process. See *supra* notes 49–52 and accompanying text.

The Commission notes that under the New By-Laws, the Member Nominating Committee shall nominate candidates for each Member Representative Director position to be elected by Exchange Members or the Sole LLC Member, and for appointment by the Board for each vacant or new position on any committee that is to be filled with a Member Representative member. See New By-Laws, Article III, Section 6.

<sup>101</sup> See New By-Laws, Article III, Section 6(c)(i).

<sup>102</sup> See New By-Laws, Article III, Section 6(c)(ii). See also Notice, *supra* note 3, at 20521; Amendment No. 1.

The Exchange also states that the function of Member Representative members on committees is to provide members a voice in the administration of the Exchange's affairs on certain committees that are responsible for providing advice on any matters pertaining to the Exchange's self-regulatory function or relating to its market structure. See Amendment No. 1. In order to ensure that its members have the opportunity to formally provide

The Commission believes that the Exchange's proposed committees, which are similar to the committees maintained by other exchanges,<sup>103</sup> are designed to help enable the 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>104</sup> The Commission further believes that the Exchange's proposed committees, including their composition and the means by which committee members will be chosen, are consistent with Section 6(b)(3) of the Act because relevant committees provide for the fair representation of members in the administration of the Exchange's affairs.<sup>105</sup>

#### 4. Regulatory Independence

Certain provisions in ISE's Current Governing Documents, and those of its Upstream Owners, are designed to help maintain the independence of the regulatory functions of the Exchange.<sup>106</sup> The New Governing Documents similarly include provisions designed to help maintain the independence of the regulatory functions of ISE,<sup>107</sup> which provisions are substantially similar to those included in the governing documents of other exchanges.<sup>108</sup> Specifically:

- The Exchange Board will be required, when evaluating any proposal, to take into account all factors that the Board deems relevant, including, without limitation, (1) the potential impact on: The integrity, continuity, and stability of the national securities exchange operated by the Exchange and the other operations of the Exchange; the ability to prevent fraudulent and manipulative acts and practices; and

input on matters that are important to them, the Exchange states that at least 20% of the persons serving on any such committees will be individuals who will have been appointed by the Member Nominating Committee and will be representative of the Exchange's membership. See *id.*

<sup>103</sup> See, e.g., Nasdaq By-Laws Article III, Sections 5–6; BX By-Laws, Article IV, Sections 4.13–14; Phlx By-Laws, Article V, Sections 5–2 to –3.

<sup>104</sup> 15 U.S.C. 78f(b)(1).

<sup>105</sup> See 15 U.S.C. 78f(b)(3).

<sup>106</sup> See, e.g., Nasdaq Acquisition Order, *supra* note 4, at 41613–16; Securities Exchange Act Release No. 56955 (December 13, 2007), 72 FR 71979 (December 19, 2007) (SR–ISE–2007–101) (order approving acquisition of ISE Holdings by Eurex Frankfurt); and ISE HoldCo Order, *supra* note 9, at 25263–64.

<sup>107</sup> See Notice, *supra* note 3, at 20524. The Commission notes that the Exchange did not propose any amendments to the governing documents of its Upstream Owners.

<sup>108</sup> See, e.g., Nasdaq Exchange Order, *supra* note 52; MIAX Exchange Order, *supra* note 57; Mercury Exchange Approval, *supra* note 28.

<sup>91</sup> See New By-Laws, Article IV, Section 7. The CRO may also serve as the General Counsel of the Exchange. *Id.*

<sup>92</sup> See New By-Laws, Article III, Section 5(c).

<sup>93</sup> See Notice, *supra* note 3, at 20519 & n.95 (citing the Regulatory Oversight Committee Charter of Nasdaq, Phlx, and BX, available at <http://ir.nasdaq.com/corporate-governance-document.cfm?DocumentID=1097>).

<sup>94</sup> See *id.* at 20519.

<sup>95</sup> See *id.* at 20519–20.

<sup>96</sup> See *id.* at 20519. See also Current Constitution, Section 5.6.

<sup>97</sup> See Notice, *supra* note 3, at 20519.



investors and the public, and (2) whether such proposal 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 the perfection of the mechanisms for a free and open market and a national market system.<sup>109</sup>

• All books and records of ISE reflecting confidential information pertaining to the self-regulatory function of the Exchange (including but not limited to disciplinary matters, trading data, trading practices, and audit information) shall be retained in confidence by ISE and its officers, directors, employees and agents; shall not be made available to persons other than to those officers, directors, employees, and agents of ISE that have a reasonable need to know; and will not be used for any non-regulatory purpose.<sup>110</sup>

<sup>109</sup> See New By-Laws, Article III, Section 3. See also Amendment No. 1. In Amendment No. 1, the Exchange proposes to clarify in Article III, Section 3 of the New By-Laws the factors to be considered by the Board when evaluating any proposal. See *id.* Further, the Exchange states that Article III, Section 3 of the New By-Laws recognizes the Exchange's status as a self-regulatory organization, and the provisions of Section 3, taken together, are designed to reinforce the notion that the Exchange is not solely a commercial enterprise, but rather a self-regulatory organization registered pursuant to, and subject to the obligations imposed by, the Act. See Notice, *supra* note 3, at 20517; Amendment No. 1.

<sup>110</sup> The corresponding provision in ISE's Current LLC Agreement prohibits the use of confidential information for any commercial purpose. See Current LLC Agreement, Article IV, Section 4.1(b). The Exchange proposes to modify the standard to prohibit the use of such information for any non-regulatory purpose. See Notice, *supra* note 3, at 20512; New LLC Agreement, Section 16. The Exchange states that this change is intended to replicate Section 4.1(b)(iii) of MRX's LLC Agreement, to emphasize the independence of the Exchange's regulatory function from its commercial interests. See Amendment No. 1.

Pursuant to Amendment No. 1, the Exchange is not proposing that ISE, and the Board on behalf of ISE, shall not have the right to keep confidential from ISE Holdings, as the Sole LLC Member, any information that the Board would otherwise be permitted to keep confidential from the Sole LLC Member pursuant to Section 18–305(c) of the Delaware Limited Liability Company Act, 6 Del. C. § 18–101. Additionally, the Exchange is not proposing that ISE Holdings, as the Sole LLC Member and the Exchange's authorized representative, shall have an explicit right to examine the Exchange's books, records, and documents during normal business hours. See Amendment No. 1. Although such provisions are in the Nasdaq LLC Agreement (see Nasdaq LLC Agreement, Section 16), they are not in the Current Governing Documents of ISE.

The Commission believes that the proposed provisions relating to the books and records of the Exchange are designed to maintain the independence of ISE's self-regulatory function, and are consistent with the Act. The Commission notes

• The Exchange proposes that, as is currently the case, the books and records of ISE must be maintained in the United States<sup>111</sup> and are subject at all times to examination by the Commission pursuant to the federal securities laws and the rules and regulations thereunder.<sup>112</sup>

• Under the New LLC Agreement and New By-Laws, any amendments to those documents will not become effective until filed with, or filed with and approved by, the Commission, as required under Section 19 of the Act and the rules promulgated thereunder.<sup>113</sup>

that these provisions are substantially similar to those the Commission has previously found to be consistent with the Act in the context of the corporate governance structures of other exchanges. See, e.g., MIA Exchange Order, *supra* note 57; Mercury Exchange Approval, *supra* note 28.

The Commission also notes that the governing documents of ISE's Upstream Owners provide that all books and records of ISE reflecting confidential information pertaining to the self-regulatory function of the Exchange will be subject to confidentiality restrictions. See Certificate of Incorporation of ISE Holdings, Article Eleventh; Certificate of Incorporation of U.S. Exchange Holdings, Article Fourteenth; By-Laws of Nasdaq, Inc., Article XII, Section 12.1(b).

<sup>111</sup> See New LLC Agreement, Section 16; see also Current LLC Agreement, Article IV, Section 4.1.

<sup>112</sup> See New LLC Agreement, Section 16. The Commission notes that, as is currently the case, 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 agents of ISE to disclose such information to the Commission. See *id.* See also Current LLC Agreement, Article IV, Section 4.1(b).

The Exchange states that certain provisions in Section 16 of the New LLC Agreement are substantially similar to provisions in Section 16 of the Nasdaq LLC Agreement. See Amendment No. 1. The Exchange also states that it is retaining in the New LLC Agreement certain provisions from its Current LLC Agreement that are not in the governing documents of the Nasdaq Exchanges, such as those relating to where the Exchange's books and records must be maintained and who may access the books and records, in particular those books and records that contain confidential information pertaining to the self-regulatory function of the Exchange. See Notice, *supra* note 3, at 20512 & n.38.

ISE also states that the Nasdaq Exchanges will separately file proposed rule changes to harmonize the books and records provisions in their respective governing documents with the language in Section 16 of the New LLC Agreement. See Notice, *supra* note 3, at 20512 n.38.

<sup>113</sup> See New LLC Agreement, Section 27; New By-Laws, Article VIII, Section 1.

The Commission notes that, although the Current Constitution and Current LLC Agreement do not include a similar, explicit requirement regarding the filing of amendments pursuant to Section 19 of the Act, the Current Constitution and Current LLC Agreement, as rules of the Exchange, are nonetheless subject to the requirements of Section 19 of the Act and the rules and regulations thereunder.

Additionally, pursuant to the New By-Laws, either the Sole LLC Member or the vote of a majority of the whole Board may enact amendments to the By-Laws, and that the Board may adopt emergency by-laws.

• Additionally, as is currently the case pursuant to the Current LLC Agreement,<sup>114</sup> Section 15 of the New LLC Agreement would prohibit the Exchange from using Regulatory Funds to pay dividends.<sup>115</sup>

The Commission believes that the provisions discussed in this section, which are designed to help ensure the independence of the Exchange's regulatory function and facilitate the ability of the 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>116</sup>

The Commission finds that proposed process regarding amendments to the New Governing Documents is consistent with Section 6(b)(1) of the Act, because it reflects the obligation of the Board to ensure compliance with the rule filing requirements under the Act. Additionally, the Commission finds these changes to be consistent with Section 19(b)(1) of the Act and Rule 19b–4 thereunder,<sup>117</sup> which require that a self-regulatory organization file with the Commission all proposed rules, as well as all proposed changes in, additions to, and deletions of its existing rules. These provisions clarify that amendments to the New Governing Documents constitute proposed rule changes within the meaning of Section 19(b)(2) of the Act and Rule 19b–4 thereunder, and are subject to the filing requirements of Section 19 of the Act

<sup>114</sup> See Current LLC Agreement, Article III, Section 3.3.

<sup>115</sup> Specifically, pursuant to Section 15 of the New LLC Agreement, Regulatory Funds shall not be used non-regulatory purposes, but rather shall be used to fund the legal, regulatory, and surveillance operations of the Exchange, and the Exchange shall not make a distribution to the Sole LLC Member (ISE Holdings) using Regulatory Funds. See New LLC Agreement, Section 15.

Consistent with Section 3.3 of the Current LLC Agreement, Schedule A of the New LLC Agreement defines "Regulatory Funds" as fees, fines, or penalties derived from the regulatory operations of the Exchange. However, Regulatory Funds do not include revenues derived from listing fees, market data revenues, transaction revenues, or any other aspect of the commercial operations of the Exchange even if a portion of such revenues are used to pay costs associated with the regulatory operations of the Exchange. See New LLC Agreement, Schedule A.

ISE states that the Nasdaq Exchanges will separately file proposed rule changes to harmonize the distribution provisions in their respective governing documents with the language in Section 15 of the New LLC Agreement. See Amendment No. 1.

<sup>116</sup> 15 U.S.C. 78f(b)(1).

<sup>117</sup> *Id.*; 17 CFR 240.19b–4.



and the rules and regulations thereunder.

The Commission also finds that the prohibition on the use of regulatory fines, fees, or penalties to fund dividends is consistent with Section 6(b)(1) of the Act, because it will further the Exchange's ability to effectively comply with its statutory obligations and is designed to ensure that the regulatory authority of the Exchange is not improperly used.<sup>118</sup> This restriction on the use of regulatory funds is intended to preclude the Exchange from using its authority to raise Regulatory Funds for the purpose of benefiting its shareholders.<sup>119</sup>

### C. Related Rule Amendments

While voting rights with respect to Directors will be governed by the New Governing Documents, as is the case today under the Current Governing Documents,<sup>120</sup> the Current Governing Documents also afford certain additional rights to the holders of PMM Rights and CMM Rights (PMM Rights and CMM Rights, each as defined below, and together, "Market Maker Rights"), namely:<sup>121</sup> (i) the right to vote on any change in, amendment to, or modification of the Core Rights or the definition of "Core Rights";<sup>122</sup> and (ii) the right to transfer or lease Market Maker Rights upon approval of the Exchange.<sup>123</sup> The Exchange represents

that these rights reflect ISE's original membership structure, where the original Market Maker Rights provided the holders thereof with an equity ownership interest in ISE, as well as trading rights on the Exchange.<sup>124</sup> The Exchange states, however, that today the Market Maker Rights do not confer any equity ownership in the Exchange and are, for all practical purposes, rights to trade on the Exchange.<sup>125</sup> As such, the Exchange believes that the provisions governing the trading privileges of PMMs,<sup>126</sup> CMMs,<sup>127</sup> and EAMs<sup>128</sup> are more appropriately located in its Rules rather than its governance documents. Accordingly, the Exchange proposes to import into its Rules certain provisions relating to Market Maker Rights, as well as Exchange Rights,<sup>129</sup> currently found in the Current Governing Documents.<sup>130</sup> The Exchange states that it is amending its Rules to: (i) Clarify any Rules that cross-reference the Current Governing Documents in the rule text, since those documents are being replaced by the New Governing Documents; or (ii) relocate or memorialize in the Rules certain rights and protections afforded to the Market Maker Rights holders,

Article VIII, Section 8.1 and Current Constitution, Article X, Section 10.1.

<sup>124</sup> See Notice, *supra* note 3, at 20510 & n.27 (citing ISE Exchange Approval, *supra* note 71).

The Exchange notes that all of the initial Market Maker Rights provided the rights holders with an equity ownership interest in ISE as well as trading rights on the Exchange. As such, those rights were transferable or leasable to approved persons or entities (*i.e.*, Exchange members or non-member owners as provided in Rule 300(a)). Additionally, in the past, holders of the Market Maker Rights had the right to vote on corporate actions, such as increasing the number of memberships in a class (akin to the voting rights related to "Core Rights" today). The Exchange states that, from the beginning, the holders of EAM Rights had no equity interest in the Exchange and only had rights to trade on the Exchange, and that those rights were not transferable by the holders, and could only be held by Exchange members. The Exchange has since demutualized and reorganized into a holding company structure, all of which resulted in the separation of the equity ownership rights in the Exchange (currently all held by ISE Holdings as the Sole LLC Member) from the trading privileges on the Exchange (currently held by PMMs, CMMs, and EAMs). The holders of PMM Rights and CMM Rights still retain, however, the ability to transfer those rights. See, *e.g.*, Rule 307(a); Current LLC Agreement, Section 6.4; and Current Constitution, Sections 12.1(c), 12.2(c), and 12.3(b). See also Notice, *supra* note 3, at 20510 & n.27, 20511.

<sup>125</sup> See Notice, *supra* note 3, at 20511.

<sup>126</sup> See *infra* note 140 for the definition of the term, "PMM."

<sup>127</sup> See *infra* note 136 for the definition of the term, "CMM."

<sup>128</sup> See *infra* note 138 for the definition of the term, "EAM."

<sup>129</sup> See *supra* note 70 for the definition of the term "Exchange Rights."

<sup>130</sup> The Exchange provides that all the provisions governing the transfer and lease of Market Maker Rights in the Current Governing Documents are substantially set forth in the Rules.

which today are primarily found in the Current Governing Documents.<sup>131</sup> The Exchange represents that the holders of Exchange Rights will continue to have the same trading privileges they currently hold as PMMs, CMMs, and EAMs under its Rules, and the new Board structure of the Exchange will not change any trading privileges.<sup>132</sup>

Specifically, the Exchange proposed changes to its Rules to, among other things:

- Relocate the concept of CMM Rights from the Current LLC Agreement<sup>133</sup> to New Rule 100(a)(11), which will state that the term "CMM Rights" means the transferable rights held by a Competitive Market Maker or a "non-member owner" (as that term is defined in Rule 300(a)),<sup>134</sup> and provide in New Rule 100(a)(11) that there are 160 authorized CMM Rights, as is currently set forth in Section 6.1(a) of the Current LLC Agreement.<sup>135</sup>

- Relocate to New Rule 100(a)(12) the definition of "Competitive Market Maker,"<sup>136</sup> which is currently only defined in Section 13.1(g) of the Current Constitution.

- Relocate the concept of EAM Rights to New Rule 100(a)(15), which will state that the term "EAM Rights" means the non-transferable rights held by an Electronic Access Member.<sup>137</sup>

<sup>131</sup> See Notice, *supra* note 3, at 20511. The Exchange also proposes certain technical, non-substantive changes, such as changing the term "Constitution" to "By-Laws."

<sup>132</sup> See *id.*

<sup>133</sup> See Current LLC Agreement, Article VI, Section 6.2(b).

<sup>134</sup> CMM Rights are transferable rights. The holders of CMM Rights may lease or sell these rights in accordance with the Exchange's rules and Current Governing Documents. As discussed above, all Exchange Rights (*i.e.*, PMM, CMM, and EAM Rights) convey voting rights and trading privileges on the Exchange. From ISE's inception, however, only the holders of the PMM Rights and CMM Rights could transfer the voting rights and trading privileges associated with such Market Maker Rights, while the voting rights and trading privileges associated with the EAM Rights have never been transferable. See *supra* note 124.

The term "non-member owners" is defined as individuals and organizations that are not Members of the Exchange, or that are otherwise Members, but do not seek to exercise trading privileges associated with the Market Maker Rights that they own. See Rule 300(a).

The term "Member" means an organization that has been approved to exercise trading rights associated with Exchange Rights. See current Rule 100(a)(23); New Rule 100(a)(26).

<sup>135</sup> See Current LLC Agreement, Article VI, Section 6.1(a).

<sup>136</sup> The term "Competitive Market Maker" (referred to herein as "CMM") will be defined to mean a Member that is approved to exercise trading privileges associated with CMM Rights. See New Rule 100(a)(12).

<sup>137</sup> EAM Rights are non-transferable. Accordingly, the holders of EAM Rights may not lease or sell these rights (unlike PMM and CMM Rights, which

Continued

<sup>118</sup> See, *e.g.*, Securities Exchange Act Release No. 51029 (January 12, 2005), 70 FR 3233, 3241 (January 21, 2005) (SR-ISE-2004-29) (approving an ISE rule interpretation that requires that revenues received from regulatory fees or regulatory penalties be segregated and applied to fund the legal, regulatory, and surveillance operations of the Exchange and not used to pay dividends to the holders of Class A Common Stock).

<sup>119</sup> See Notice, *supra* note 3, at 20512.

<sup>120</sup> The Commission notes, however, that in the case of a Contested Election for Member Representative Directors, which is discussed above, instead of electing Directors by class, as is the case under the Current Governing Documents, each PMM, CMM, and EAM Rights holder would cast one vote. See *supra* note 52 and accompanying text.

<sup>121</sup> See Notice, *supra* note 3, at 20510.

<sup>122</sup> See Current LLC Agreement, Section 6.3(b) and Current Constitution, Section 10.1. "Core Rights" represent the voting rights with respect to any increase in the number of authorized Market Maker Rights. See Current LLC Agreement, Section 2.2. The number of authorized PMM Rights and CMM Rights are 10 and 160, respectively. See Current LLC Agreement, Section 6.1.

<sup>123</sup> See Current LLC Agreement, Article VI and Current Constitution, Article XII. According to the Exchange, most of the transfer and lease provisions in the Current Governing Documents are also already in the current Rule 300 Series. See Notice, *supra* note 3, at 20510 n.26.

The Commission notes that holders of Exchange Rights also currently have the right to vote on amendments to the Current LLC Agreement or Current By-Laws, if the amendment would alter or change the powers, preferences, or special rights of one or more series of Exchange Rights so as to affect them adversely. See Current LLC Agreement,

- Relocate to New Rule 100(a)(16) the definition of “Electronic Access Member,”<sup>138</sup> which is currently only defined in Section 13.1(l) of the Current Constitution.

- Relocate the definitions for “Exchange Transaction,” “good standing,” and “System” from the Current Constitution to the Rules,<sup>139</sup> and delete Rule 100(a)(22), defining “LLC Agreement,” as that term would no longer be used in the Rules, as amended by the proposed rule change.

- Relocate the concept of PMM Rights from Article VI of the Current LLC Agreement to New Rule 100(a)(39), which will state that the term “PMM Rights” means the transferable rights held by a Primary Market Maker or a “non-member owner” (as that term is defined in Rule 300(a)), and will state that there are 10 authorized PMM Rights, as is currently set forth in Section 6.1(a) of the Current LLC Agreement.

- Relocate to New Rule 100(a)(40) the definition for “Primary Market Maker”<sup>140</sup> from Section 13.1(bb) of the Current Constitution.

The Exchange also proposed to add as new paragraphs (d) and (e) in New Rule 300 certain protections in the Current Governing Documents that relate to the Market Maker Rights. First, new paragraph (d) preserves the concept of Core Rights from the Current Governing Documents, and states that any increase in the number of authorized PMM or CMM Rights must be approved by the affirmative vote of the holders of at least a majority of the then outstanding PMM Rights, voting as a class, and the affirmative vote of the holders of at least a majority of the then outstanding CMM Rights, voting as a class, respectively.<sup>141</sup> Second, new paragraph (e) states that any amendments to the New Governing

Documents that would alter or change the powers, preferences, or special rights of one or more series of PMM Rights or CMM Rights must also be approved by the holders of a majority of such PMM or CMM Rights, as applicable. As such, to the extent they relate to the Market Maker Rights holders, paragraph (e) preserves the existing amendment rights from the Current Governing Documents.<sup>142</sup>

The Exchange also proposes to explicitly set forth in its Rules the ownership and voting limitations for the holders of Market Maker Rights.<sup>143</sup> Today, a holder or lessee of Exchange Rights, together with any affiliate, is restricted from owning (or exercising any of the non-trading rights associated with) more than 20% of the PMM Rights or CMM Rights.<sup>144</sup> Consistent with the current limitation, the Exchange proposes to replace the current Supplementary Material .02 to Rule 303 with New Supplementary Material .02, to state that, “[i]n addition to the trading concentration limits contained in [Rule 303], no holder or lessee of Market Maker Rights, together with any affiliate, may gain ownership or voting rights in excess of 20% of the outstanding PMM Rights or CMM Rights, as applicable.”<sup>145</sup> The Exchange

also states that the New Governing Documents will not have any provisions related to the Market Maker Rights.<sup>146</sup>

The Commission notes that, because the only remaining voting rights associated with PMM Rights and CMM Rights will be the Core Rights and the right to vote on certain amendments to the New Governing Documents, as described above, the voting limitation in Supplementary Material .02 to New Rule 303 will only apply to voting on those matters. Voting on the election of Member Representative members will be governed by Article II of the New By-Laws, as described above.<sup>147</sup>

In the context of a lease of Market Maker Rights, the Exchange proposes to add a requirement in New Rule 308 that the holder of Market Maker Rights must, as is currently required by Section 12.4(b) of the Current Constitution, retain the Core Rights associated with such Market Maker Rights and not transfer such voting rights to the lessee. Section 12.4(b) of the Current Constitution also provides that, under a lease agreement, the lessor may retain the voting rights with respect to the PMM Rights and CMM Rights or may transfer such voting rights, other than the Core Rights, to the lessee. Currently, the voting rights associated with the PMM Rights and CMM Rights that may be retained or transferred are the right to vote in the election of Exchange Directors and the right to vote on amendments to the Current Governing Documents that may adversely affect Market Maker Rights.<sup>148</sup> Pursuant to the New Governing Documents, a holder of Market Maker Rights will continue to have the option of retaining or transferring the right to vote on certain amendments to the New Governing

Market Maker Rights holders are voting on Core Rights or on certain amendments to the New Governing Documents, which is how the voting limitation is applied on the Exchange today. See Amendment No. 1. As it relates to voting on the Member Representative Directors only, in the event of a Contested Election, the Exchange states that members will now vote as one class. As such, an Exchange Member (together with any affiliates) may not cast votes representing more than 20% of the votes cast for a candidate. See *id.* See also New By-Laws, Article II, Section 2.

New Supplementary Material .02 to Rule 303 will replace the Current Supplementary Material .02 to Rule 303, which states that in approving any PMM to exercise the trading privileges associated with more than 20% of the outstanding PMM Membership, the Board will not approve any arrangement in which such PMMs would gain ownership or voting rights in excess of those permitted under the Exchange’s Current LLC Agreement or Current Constitution.

<sup>146</sup> See Amendment No. 1.

<sup>147</sup> See *supra* notes 46–53 and accompanying text.

<sup>148</sup> See Amendment No. 1. See also Current LLC Agreement, Article VI, Section 6.3 and Article VIII, Section 8.1; and Current Constitution, Article X, Section 10.1

are transferable). See Current Constitution Article XII, Section 12.3. See also Notice, *supra* note 3, at 20522 n.111.

The current definition of EAM Rights in Rule 100(a)(14) refers to Article VI of the Current LLC Agreement.

<sup>138</sup> The term “Electronic Access Member” (referred to herein as “EAM”) will be defined to mean a Member that is approved to exercise trading privileges associated with EAM Rights. See New Rule 100(a)(16).

<sup>139</sup> “Exchange Transaction” would be relocated from Section 13.1(r) of the Current Constitution to New Rule 100(a)(20), “good standing” from Section 13.1(s) of the Current Constitution to New Rule 100(a)(23), and “System” from Section 13.1(gg) of the Current Constitution to New Rule 100(a)(53).

<sup>140</sup> The term “Primary Market Maker” (referred to herein as “PMM”) will be defined to mean a Member that is approved to exercise trading privileges associated with PMM Rights. See New Rule 100(a)(40).

<sup>141</sup> See New Rule 300(d). See also *supra* note 122 and accompanying text (discussing the current Core Rights).

<sup>142</sup> See New Rule 300(e). See also Current LLC Agreement, Section 8.1 and Current Constitution, Section 10.1. As the Exchange notes, the proposed amendment rights for the Market Maker Rights holders in Rule 300(e) are broader than the ones contained in the Current Governing Documents because they will apply for all amendments that affect the powers, preferences, or special rights of one or more series of PMM Rights or CMM Rights, rather than solely to the amendments that adversely affect these Market Maker Rights. See Notice, *supra* note 3, at 20523 n.114. See also *supra* note 123. The Commission also notes that any such amendment would also be subject to the voting concentration limitation in the New Supplementary Material .02 to Rule 303, described below (see *infra* notes 143–145 and accompanying text), as well as the requirements of Section 19 of the Act and the rules and regulations thereunder (see New LLC Agreement, Section 27; New By-Laws, Article VIII, Section 1).

<sup>143</sup> See New Supplementary Material .02 to Rule 303.

<sup>144</sup> See Current LLC Agreement, Section 6.5(a). See also Amendment No. 1.

Under the Current LLC Agreement, a holder or lessee of Exchange Rights, together with any affiliate, is also restricted from owning (or exercising any of the non-trading rights associated with) more than 20% of the EAM Rights. As discussed above, under the New Governing Documents, a 20% voting limitation will apply to all Exchange Members with respect to participation in Contested Elections, and only holders of PMM and CMM Rights will have a right to vote on certain amendments to the New Governing Documents. See *supra* notes 52 and 142 and accompanying text.

<sup>145</sup> See New Supplementary Material .02 to Rule 303. See also Amendment No. 1.

The Exchange states that this voting limitation will be calculated by class (*i.e.*, 20% of outstanding PMM Rights or CMM Rights, as applicable) when

Documents. With respect to the right to vote in the case of a Contested Election, the Exchange provides that those voting rights will be transferable under a lease agreement for the holders of Market Maker Rights who are also members of the Exchange.<sup>149</sup> Non-member owners, who are required to lease out their Market Maker Rights pursuant to Rule 300(b) will no longer have voting rights with respect to Directors that represent Exchange Members.<sup>150</sup> The Commission notes that the 20% concentration limitation on voting described above will continue to apply in the case of any transfer of the right to vote in Contested Elections.

The Exchange also proposes to amend New Rule 308 to memorialize the manner in which Market Maker Rights may be subleased. Specifically, the Exchange proposes that a lessee of a Market Maker membership in good standing may sublease such membership to a Member with the permission of the owner.<sup>151</sup> The Exchange states that this is consistent with the Exchange's current practice and will not change the manner in which Market Maker Rights are subleased, but will clarify that such rights may be subleased to an Exchange Member only.<sup>152</sup> Additionally, the Exchange proposes to relocate to the New Rules the requirement from the Current Constitution that a lessor of Market Maker Rights must retain the Core Rights.<sup>153</sup>

The Exchange also proposes to clarify that, for the holders of Market Maker Rights who are also members of the Exchange, the right to vote on Directors representing Exchange Members will continue to be transferable under a lease agreement.<sup>154</sup> Non-member owners, who are required to lease out their Market Maker Rights pursuant to Rule 300(b), will not have voting rights with respect to electing Member Representative Directors.<sup>155</sup> The Exchange states that all voting rights other than Core Rights will remain transferable under a lease agreement, and that New Rule 308(b)(4) requires a lease agreement of Market Maker Rights to include provisions for which party will exercise the voting rights associated

with the Market Maker Rights being leased.<sup>156</sup> Accordingly, apart from being relocated from the Current Constitution to the Rules, the Exchange represents that the proposed amendment to New Rule 308 will not change the current transfer rights associated with Market Maker Rights, other than as described above with respect to non-member owners.<sup>157</sup>

The Exchange also proposes to amend New Rule 802(b) to provide that, if a Primary Market Maker fulfills its obligations as a Primary Market Maker under the Rules, the Exchange will not reallocate the options classes to which such Primary Market Maker is appointed, unless otherwise requested by the Primary Market Maker; and would provide that the foregoing will not limit or affect the Exchange's responsibility under Rule 802(d) to reallocate any options classes in the interests of a fair and orderly market.<sup>158</sup> The Exchange states that this proposal is consistent with the manner in which products are allocated to PMMs on the Exchange today.<sup>159</sup> According to the Exchange, today, when ISE lists new options classes, it allocates them to one of its PMMs under Rule 802, and that pursuant to delegated authority by the Board, an Allocation Committee, which consists of employees of the Exchange ("Allocation Committee"), makes allocation decisions according to the guidelines contained in Rule 802.<sup>160</sup> The Exchange also states that the Allocation Committee has not reallocated the products appointed to a PMM since the Exchange's inception for reasons other than as provided in the proposed rule, and as such, the proposed changes are simply to memorialize a longstanding practice on the Exchange.<sup>161</sup>

The Commission believes that the proposed changes to ISE's Rules are consistent with the Act and, in particular Section 6(b)(1) of the Act,<sup>162</sup> which requires among other things that a national securities exchange be so organized and have the capacity to carry out the purposes of the Act. The Commission notes that many of the proposed changes to ISE's Rules are technical in nature, such as renumbering of Rules or conforming terminology to reflect the replacement of the Current Governing Documents with the New Governing Documents.

The Commission also notes that, as described above, the Exchange proposes to relocate definitions and provisions related to Market Maker Rights from the Current Governing Documents into the Rules. The Commission believes that the proposed changes to ISE's Rules that would prohibit a holder or lessee of Market Maker Rights, together with any affiliate, from gaining ownership or voting rights in excess of 20% of the outstanding PMM Rights or CMM Rights, as applicable, are consistent with the Act. The Commission has previously stated that a regulatory concern can arise if a member's interest in an exchange becomes so large as to cast doubt on whether the exchange can fairly and objectively exercise its self-regulatory responsibilities with respect to that member.<sup>163</sup> The Commission has stated, for example, that a member that directly or indirectly controls an exchange might be tempted to exercise that controlling influence by directing the exchange to refrain from diligently monitoring and surveilling the member's conduct or diligently enforcing its rules and the federal securities laws with respect to conduct by the member that violates such provisions.<sup>164</sup> The Commission believes that the proposal would not give rise to concerns about the Exchange's ability to effectively carry out its regulatory responsibilities under the Act because the proposed rules change preserves existing ownership and voting limitations.

#### IV. Accelerated Approval

The Commission finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>165</sup> to approve the proposal, as modified by Amendment No. 1, prior to the 30th day after publication of Amendment No. 1 in the **Federal Register**. In Amendment No. 1, ISE revises the original proposal to make certain changes discussed in greater detail above. Notably, in Amendment No. 1, ISE revises its proposal to (1) make changes to the Exchange's New LLC Agreement and New By-Laws to better align these proposed documents with certain provisions in ISE's existing governing documents and the governing documents of other exchanges, including those concerning limitations on board committee powers, the confidentiality of books and records, the nomination of certain board directors by petition, and the confidentiality of board meetings; (2) revise the proposed

<sup>149</sup> See Amendment No. 1.

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

<sup>151</sup> See *id.*

<sup>152</sup> *Id.* See also New Rule 308.

<sup>153</sup> See Notice, *supra* note 3, at 20523. See also Amendment No. 1; and New Rule 308.

<sup>154</sup> See Amendment No. 1.

<sup>155</sup> As described above, under the New By-Laws, in the case of a Contested Election, each Exchange Member shall have the right to cast one vote for each Member Representative Director. See New By-Laws, Article II, Section 2. See also *supra* note 52; Amendment No. 1.

<sup>156</sup> See Amendment No. 1.

<sup>157</sup> See *id.*

<sup>158</sup> See New Rule 802(b)(2).

<sup>159</sup> See Notice, *supra* note 3, at 20523.

<sup>160</sup> See *id.*

<sup>161</sup> See *id.*

<sup>162</sup> 15 U.S.C. 78f(b)(1).

<sup>163</sup> See, e.g., ISE HoldCo Order, *supra* note 9, at 25262 n.38 and accompanying text.

<sup>164</sup> See, e.g., *id.* at 25262.

<sup>165</sup> 15 U.S.C. 78s(b)(2).

amendments to ISE's rules regarding ownership, voting, and transfer restrictions relating to certain market maker rights on the Exchange; (3) revise the related discussion of the purpose of the proposed changes; (4) add clarification to the description of the proposal regarding the operation of certain provisions; and (5) make certain technical corrections. The Commission believes that Amendment No. 1 does not raise any novel regulatory issues and instead better aligns ISE's proposed New Governing Documents with certain provisions in its Current Governing Documents and the governing documents of other exchanges that were previously approved by the Commission.<sup>166</sup> As discussed more fully above, certain provisions of ISE's New Governing Documents, as modified by Amendment No. 1, are designed to facilitate the ability of ISE to maintain the independence of its self-regulatory function, enable it to operate in a manner that complies with the federal securities laws, and facilitate the ability of ISE and the Commission to fulfill their regulatory and oversight obligations under the Act.<sup>167</sup> The Commission further believes that Amendment No. 1 provides additional clarity in the rule text and the description of the proposal, which is consistent with ISE's original proposal and supports ISE's analysis of how its proposal is consistent with the Act, thus facilitating the Commission's ability to make the findings set forth above to approve the proposal. Accordingly, the Commission finds that good cause exists to approve the proposal, as modified by Amendment No. 1, on an accelerated basis.

## V. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1, including whether Amendment No. 1 is consistent with the Act. Comments may be submitted by any of the following methods:

### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or

- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-ISE-2017-32 on the subject line.

### *Paper Comments*

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-ISE-2017-32. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-ISE-2017-32 and should be submitted on or before August 25, 2017.

## VI. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>168</sup> that the proposed rule change (SR-ISE-2017-32), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>169</sup>

**Eduardo A. Aleman,**  
Assistant Secretary.

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**BILLING CODE 8011-01-P**

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-81269; File No. SR-NYSENAT-2017-03]

### **Self-Regulatory Organizations; NYSE National, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Amending Rule 11.26 To Modify the Date of Appendix B Web site Data Publication Pursuant to the Regulation NMS Plan To Implement a Tick Size Pilot Program**

July 31, 2017.

Pursuant to Section 19(b)(1) <sup>1</sup> of the Securities Exchange Act of 1934 (the "Act") <sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that on July 18, 2017, NYSE National, Inc. (the "Exchange" or "NYSE NAT") filed with the Securities and Exchange Commission (the "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The Exchange proposes to amend Rule 11.26 to modify the date of Appendix B Web site data publication pursuant to the Regulation NMS Plan to Implement a Tick Size Pilot Program ("Plan"). The proposed rule change is available on the Exchange's Web site at [www.nyse.com](http://www.nyse.com), at the principal office of the Exchange, and at the Commission's Public Reference Room.

#### **II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

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

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

<sup>166</sup> See, e.g., Securities Exchange Act Release Nos. 70050 (July 26, 2013), 78 FR 46622 (August 1, 2013) (granting GEMX's (f/k/a Topaz Exchange, LLC) application for registration as a national securities exchange); and Mercury Exchange Approval, *supra* note 28.

<sup>167</sup> See *supra* Section III.B.4 (discussing, for example, certain provisions in ISE's New Governing Documents that are designed to help maintain the independence of the regulatory functions of the Exchange).

<sup>168</sup> 15 U.S.C. 78s(b)(2).

<sup>169</sup> 17 CFR 200.30-3(a)(12).