

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-66383; File No. SR-EDGX-2012-04)

February 10, 2012

Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend EDGX Rule 1.5(q)

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 1, 2012, the EDGX Exchange, Inc. (the "Exchange" or "EDGX") filed with the Securities and Exchange Commission (the "SEC" or 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

EDGX Exchange, Inc. ("EDGX" or the "Exchange"), proposes to amend its rules regarding registration, qualification and continuing education requirements for Authorized Traders of Members that engage solely in proprietary trading. EDGX proposes to amend Rules 2.3 and 11.4 and the Interpretations to Rule 2.5 to recognize a new category of limited representative registration for proprietary traders. The Exchange proposes to expand its registration requirements to include the Proprietary Traders Qualification Examination ("Series 56") as one of the applicable qualification examinations as determined by the Exchange. The Exchange also proposes to permit Authorized Traders of Members who engage solely in proprietary trading to obtain the Series 56 license in order to effect transactions on the Exchange. In addition, the

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

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

Exchange proposes to amend Rule 2.3 to make it substantially similar to the rules of the Financial Industry Regulatory Authority (“FINRA”) and other Self-Regulatory Organizations (“SROs”) to require Members to register two registered Principals.<sup>3</sup> The text of the proposed Proprietary Traders Qualification Examination Content Outline is attached as Exhibit 3 and the text of the proposed rule changes is attached as Exhibit 5.<sup>4</sup> These documents are available on the Exchange’s website at [www.directedge.com](http://www.directedge.com), at the Exchange’s principal office, and at the Public Reference Room of the Commission.

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

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

1. Purpose

Background

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<sup>3</sup> The Exchange notes that it will continue to require per Exchange Rule 2.3(c) that all Authorized Traders who are to function as Principals on the Exchange to [sic] be registered consistent with amended paragraph (c)(2) of Rule 2.3.

<sup>4</sup> The Commission notes that the Outline and the text of the proposed rule change are attached to the filing, not to this Notice.

In July 2011, NASDAQ filed a proposed rule change with the Commission to recognize a new category of limited representative registration for proprietary traders.<sup>5</sup> In addition, in August 2011, NASDAQ filed a related proposed rule change to use the content outline for the Series 56 examination that would be applicable to proprietary traders.<sup>6</sup>

For the purposes of this category of limited representative registration, NASDAQ Rule 1011(o) defines a proprietary trading firm as a firm that embodies the following characteristics: the Member is not required by Section 15(b)(8) of the Exchange Act (the “Act”) to become a FINRA member but is a member of another registered securities exchange not registered solely under Section 6(g) of the Act; all funds used or proposed to be used by the Member for trading are the Member’s own capital, traded through the Member’s own accounts; the Member does not, and will not have “customers”;<sup>7</sup> all Principals and Authorized Traders of the Member acting or to be acting in the capacity of a trader must be owners of, employees of, or contractors to the Member. In addition, NASDAQ Rule 1032(c) defines a proprietary trader as an Authorized Trader whose activities in the investment banking or securities business are limited solely to proprietary trading; passes an appropriate qualification examination; and is an associated person of a proprietary trading firm as defined in NASDAQ Rule 1011(o). NASDAQ Rule 1032(c)

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<sup>5</sup> See Securities Exchange [sic] Release No. 64958 (July 25, 2011), 76 FR 45629 (July 29, 2011) (SR-NASDAQ-2011-095). See also Securities Exchange [sic] Release No. 65041 (August 5, 2011), 76 FR 49822 (August 11, 2011) (SR-NASDAQ-2011-107).

<sup>6</sup> See Securities Exchange [sic] Release No. 65040 (August 5, 2011), 76 FR 49809 (August 11, 2011) (SR-NASDAQ-2011-108).

<sup>7</sup> NASDAQ Rule 0120(g) states, “the term customer shall not include a broker or dealer.”

identifies the Series 56 as the appropriate qualification examination for proprietary traders' limited representative registration. Furthermore, NASDAQ's proposed category of limited representative registration expressly excludes those associated persons that deal with the public and states those associated persons should continue to register as General Securities Representatives after obtaining the Series 7 license.

NASDAQ worked with FINRA and certain other exchanges, many of which have recently enhanced their registration requirements to require the registration of associated persons,<sup>8</sup> to develop the content outline and qualification examination for proprietary traders. The Series 56 examination program is shared by NASDAQ and the following SROs: Boston Options Exchange, C2 Options Exchange, Incorporated; Chicago Board Options Exchange, Incorporated ("CBOE"); Chicago Stock Exchange, Incorporated; International Securities Exchange, LLC ("ISE"); NASDAQ OMX BX, Inc.; NASDAQ OMX PHLX LLC; National Stock Exchange, Incorporated; New York Stock Exchange, LLC ("NYSE"); NYSE AMEX, Incorporated; and NYSE ARCA, Incorporated. Members of FINRA, NASDAQ and the SROs referenced above developed criteria for the Series 56 examination program, which CBOE filed with the SEC on June 17, 2011.<sup>9</sup>

#### Adoption of Series 56 by the Exchange

The Exchange believes the Series 56 will assist the Exchange in ensuring it has proper registration, qualification and continuing education requirements for associated persons of Members because the Series 56 examination was designed to test a candidate's

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<sup>8</sup> See Securities Exchange Act Release Nos. 63843 (February 4, 2011), 76 FR 7884 (February 11, 2011) (SR-ISE-2011-155); and 63314 (November 12, 2010), 75 FR 70957 (November 9, 2010) (SR-CBOE-2010-084).

<sup>9</sup> See supra note 3. [sic] See also Securities Exchange Act Release No. 64699 (June 17, 2011), 76 FR 36945 (June 23, 2011) (SR-CBOE-2011-056).

knowledge of proprietary trading in general and the industry rules applicable to trading of equity securities and listed options contracts. The Series 56 examination covers, among other things, recordkeeping and recording requirements, types and characteristics of securities and investments, trading practices and display execution and trading systems. While the Series 56 examination is primarily dedicated to topics related to proprietary trading, the Series 56 examination also covers some general concepts relating to customers.

The qualification examination consists of 100 multiple choice questions. Candidates have 150 minutes to complete the exam. The content outline, which the Exchange attached as Exhibit 3,<sup>10</sup> describes the following topical sections comprising the examination: Personnel, Business Conduct and Recordkeeping and Reporting Requirements, 9 questions; Markets, Market Participants, Exchanges and SROs, 8 questions; Types and Characteristics of Securities and Investments, 20 questions; Trading Practices and Prohibited Acts, 50 questions; and Display, Execution, and Trading Systems, 13 questions. Representatives from the SROs mentioned above also intend to meet on a periodic basis to evaluate and update, as necessary, the Series 56 examination program.

In addition, NASDAQ and some other SROs have filed or will file similar proposals with the Commission to amend current rules to recognize a new category of limited representative registration for proprietary traders and to permit members engaged solely in proprietary trading to obtain the Series 56 license in order to effect trades on the

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<sup>10</sup> See note 4.

applicable exchanges.<sup>11</sup> The Exchange proposes to implement the Series 56 examination program upon availability in FINRA's Web CRD<sup>®</sup> system,<sup>12</sup> notification to its Members and subject to the satisfaction of applicable continuing education requirements, as described in Interpretations .04 and .05 to Rule 2.5.

The Exchange believes that acceptance of the Series 56 qualification examination will benefit both the Exchange and the applicable proprietary traders affected by the proposal. Accordingly, pursuant to the amended rules, as proposed, the Exchange would recognize a new category of limited representative registration for proprietary traders. In addition, the Exchange would expand its registration, qualification and continuing education requirements to include the Series 56 examination as one of the applicable qualification examinations as determined by the Exchange. The Exchange would also permit Authorized Traders of Members who engage solely in proprietary trading to obtain the Series 56 license in order to effect transactions on the Exchange. The Exchange proposes to add Interpretation .06 to Rule 2.5 to incorporate the Series 56 qualification examination as a limited representative registration for proprietary traders, and proposes to identify the characteristics required to satisfy the Exchange's definition of a proprietary trading firm and a proprietary trader, which are modeled after NASDAQ's rules, as discussed above.

In addition, the Exchange proposes to amend Rule 2.3(c)(2) to make it substantially similar to the rules of FINRA and other SROs to require Members to

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<sup>11</sup> See supra notes 2, 3, 6 and 7.

<sup>12</sup> See [www.finra.org/Industry/Compliance/Registration/CRD/](http://www.finra.org/Industry/Compliance/Registration/CRD/)

register at least two registered Principals.<sup>13</sup> The proposed amendment applies to firms seeking admission as Members and existing Members, and states that each Member, except a sole proprietorship or a proprietary trading firm with 25 or fewer Authorized Traders (“Limited Size Proprietary Firm”),<sup>14</sup> shall have at least two officers or partners who are registered as Principals with respect to the Member’s equities securities business and, at a minimum, one such Principal shall be the Member’s Chief Compliance Officer (“CCO”).<sup>15</sup>

The Exchange proposes additional amendments to Rule 2.3(c)(3) and (4) to require Members to register a CCO and a Financial/Operations Principal (“FINOP”) in order to make the Exchange’s rules substantially similar to the rules of FINRA and other SROs. In addition, this more accurately reflects the heightened level of accountability inherent in the duty of overseeing compliance by a Member of the Exchange, and in the oversight and preparation of financial reports and the oversight of those employed in financial and operational capacities at each Member firm. The proposed amendments state each Member shall designate a CCO on the Schedule A of Form BD, and requires [sic] the individual designated as a CCO to register with the Exchange and pass the General Securities Principal Examination (Series 24). Similarly, the proposed amendments to Rule 2.3 require each Member subject to Rule 15c3-1 of the Act to

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<sup>13</sup> The Exchange proposes to communicate this amendment to Members by publishing an Information Circular on the Exchange’s website. Existing Members shall receive additional time to satisfy this requirement.

<sup>14</sup> The Exchange proposes to create an exception to Rule 2.3(c)(2) where a Limited Size Proprietary Firm must register at least one Principal with the Exchange. In addition, the Exchange may waive the two Principal requirement in situations that indicate conclusively that only one Principal associated with the Member should be required.

<sup>15</sup> The Commission notes that EDGX is an equities exchange.

designate a FINOP, and requires [sic] the individual designated as a FINOP to successfully complete the Financial and Operations Principal Examination (Series 27), and register in that capacity with the Exchange as prescribed by the Exchange.

The Exchange proposes to make other ministerial amendments to Rule 2.3 to accommodate the placement of the proposed amendments outlined in this rule filing.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,<sup>16</sup> in general, and furthers the objectives of Section 6(c)(3)(B) of the Act.<sup>17</sup> Under that section, it is the Exchange's responsibility to prescribe standards of training, experience, and competence for Exchange Members and their associated persons, in particular, by offering an alternative qualification examination for proprietary traders that more closely reflects the practical knowledge that is a pre-requisite to proprietary trading. Pursuant to this statutory obligation, the Exchange requests to recognize a new category of limited representative registration for proprietary traders and to permit Authorized Traders of Members who engage solely in proprietary trading to obtain the Series 56 license. The Exchange believes the Series 56 examination establishes that Authorized Traders of Members have attained specified levels of competence and knowledge generally applicable to proprietary trading.

The Exchange believes that the requirement that persons functioning in certain supervisory capacities, including CCO and a FINOP, be registered through the WebCRD<sup>®</sup> system and be subject to higher qualification standards appropriately reflects the enhanced responsibility of their roles and is consistent with the Act. The general

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<sup>16</sup> 15 U.S.C. 78f(b).

<sup>17</sup> 15 U.S.C. 78f(c)(3)(B).



requirement that Members must have a minimum of two Principals responsible for oversight of Member organization activity, who must be registered as such and pass a principal exam, should help the Exchange strengthen the regulation of its Member firms, and prepare those individuals for their responsibilities. The nature of the firm, however, may dictate that more than two Principals are needed to provide appropriate supervision. In addition, the requirement for each Member to have a CCO who must register and pass the Series 24 exam and a FINOP who must register and pass the Series 27 exam is appropriate based on the heightened level of accountability inherent in the duty of overseeing compliance by a Member of the Exchange, and in the oversight and preparation of financial reports and the oversight of those employed in financial and operational capacities at each Member firm.

The Exchange believes that this proposal will enhance its ability to ensure an effective supervisory structure for those conducting business on the Exchange. The requirements apply broadly and are intended to help close a regulatory gap which has resulted in varying registration, qualification, and supervision requirements across markets. The Exchange believes that the changes proposed to its rules will strengthen its regulatory structure and should enhance the ability of its Authorized Traders and Members to comply with the Exchange's rules as well as with the federal securities laws.

In addition, the Exchange believes that the proposed rule change is consistent with the principles of Section 11A(a)(1)(C)(ii) of the Act in that it seeks to assure fair competition among brokers and dealers and among exchange markets. The Exchange believes that the proposed rule will promote uniformity of regulation across markets, thus reducing opportunities for regulatory arbitrage. EDGX's proposed rule change helps

ensure that all persons conducting a securities business through EDGX are appropriately supervised, as the Commission expects of all SROs.

The proposed changes are also consistent with Section 6(b)(5) of the Act,<sup>18</sup> because they would promote just and equitable principles of trade, remove impediments to, and perfect the mechanism of, a free and open market and a national market system, and, in general, protect investors and the public interest, by enabling such persons to qualify for registration with the Exchange by offering an alternative qualification examination that specifically addresses industry topics that establish the foundation for the regulatory and procedural knowledge necessary for such persons electing to register as Proprietary Traders. Similarly, including new requirements for Members to maintain at least two Principals, a CCO and a FINOP, harmonizes the Exchange's rules with substantially similar rules of FINRA and other SROs. Accordingly, the modifications to EDGX Rules 2.3 and 11.4 and the Interpretations to Rule 2.5 promote just and equitable principles of trade, remove impediments to, and perfect the mechanism of, a free and open market and a national market system.

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

The proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from members or other interested parties.

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<sup>18</sup> 15 U.S.C. 78f(b)(5).

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

The Exchange has designated this rule filing as non-controversial under Section 19(b)(3)(A) of the Act<sup>19</sup> and paragraph (f)(6) of Rule 19b-4 thereunder.<sup>20</sup> The Exchange asserts that the proposed rule changes: (1) will not significantly affect the protection of investors or the public interest; (2) will not impose any significant burden on competition; (3) and will not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate. In addition, the Exchange provided the Commission with written notice of its intent to file the proposed rule changes, along with a brief description and text of the proposed rule changes, at least five business days prior to the date of filing.<sup>21</sup> For the foregoing reasons, this rule filing qualifies for immediate effectiveness as a “noncontroversial” rule change under paragraph (f)(6) of Rule 19b-4 because the Series 56 qualification examination has been adopted or will be adopted for use by NASDAQ and other SROs. The Series 56 examination also reflects a collaborative effort to adopt an appropriate qualification examination for a new registration category. In addition, the Exchange’s proposal to include new requirements for Members to maintain at least two Principals, a CCO and a FINOP, harmonizes the Exchange’s rules with substantially similar rules of FINRA and other SROs.

The rule changes as proposed will allow the Exchange to recognize a new category of limited representative registration for proprietary traders. The Exchange

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<sup>19</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>20</sup> 17 CFR 240.19b-4.

<sup>21</sup> 17 CFR 240.19b-4(f)(6).

believes that Authorized Traders of Members who engage solely in proprietary trading, obtain the Series 56 license, and wish to register with EDGA would be disadvantaged by having to wait for the proposed rule changes to become operative. Accordingly, because the Exchange believes that implementation of the standards proposed in this filing is important to its maintenance of a fair and orderly market and is non-controversial, the Exchange requested that the Commission waive the 30-day pre-operative waiting period contained in Rule 19b-4(f)(6)(iii) under the Act.<sup>22</sup> Waiver of this requirement will allow the Exchange to make the examination available as soon as possible to coincide with its availability on other exchanges. The Commission believes that waiver of the 30-day operative delay is consistent with the protection of investors and the public interest because the proposal makes the registration, qualification and continuing education requirements of EDGX comparable to those of the other exchanges and will enable EDGX to recognize the Series 56 exam as a valid qualification for proprietary traders.<sup>23</sup> Therefore, the Commission designates the proposal operative upon filing.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### IV. Solicitation of Comments

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<sup>22</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>23</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form <http://www.sec.gov/rules/sro.shtml>; or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR-EDGX-2012-04 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-EDGX-2012-04. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website <http://www.sec.gov/rules/sro.shtml>. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549k on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without

change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-EDGX-2012-04 and should be submitted by [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>24</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>24</sup> 17 CFR 200.30-3(a)(12).