

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-80211; File No. SR-ISEMercury-2017-04)

March 10, 2017

Self-Regulatory Organizations; ISE Mercury, LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Harmonize Liability Caps and Related Reimbursement Requirements

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on February 27, 2017, ISE Mercury, LLC (“ISE Mercury” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 705 (Limitation of Liability) to harmonize its liability caps and related reimbursement requirements with those of NASDAQ BX, Inc. (“BX”), NASDAQ PHLX LLC (“Phlx”) and NASDAQ Stock Market LLC (“NSM” and together with BX and Phlx, the “Nasdaq Exchanges”).

The text of the proposed rule change is available on the Exchange’s Website at www.ise.com, at the principal office of the Exchange, and at the Commission’s Public Reference Room.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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 Exchange 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

The purpose of this proposed rule change is to amend Rule 705 (Limitation of Liability) to harmonize the Exchange's existing liability caps and related reimbursement requirements for claims under Rule 705(d) with the caps and requirements set forth in the rules of the Nasdaq Exchanges.³ The Exchange and its affiliates, International Securities Exchange, LLC and ISE Gemini, LLC (together, the "ISE Exchanges"), were recently acquired (the "Acquisition") by Nasdaq, Inc. ("HoldCo").⁴ In the context of the Acquisition, the ISE Exchanges are working to align certain rules with rules of the Nasdaq Exchanges in order to provide consistent standards across the six exchanges operated by HoldCo (the "HoldCo Affiliated Exchanges"). As part of this effort, the proposal set forth below harmonizes the Exchange's liability caps and the related reimbursement requirements with those of the Nasdaq Exchanges in order to provide uniform standards and requirements for users of the HoldCo Affiliated Exchanges.⁵

³ See BX Rule 4626(b) and Phlx Rule 1015. See also NSM Rule 4626(b).

⁴ 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).

⁵ International Securities Exchange, LLC and ISE Gemini, LLC will each file a proposed rule change with the Commission to adopt similar requirements.

Rule 705 in its current form generally states that the Exchange is not liable for any losses due to the Exchange's negligence or unintentional actions, but also provides in Rule 705(d) that notwithstanding this general limitation on liability, the Exchange may compensate its members for losses resulting directly from the malfunction of the Exchange's physical equipment, devices and/or programming. Subsections (d)(1) – (d)(3) of Rule 705 contains express conditions governing the voluntary payments made by the Exchange under these limited circumstances. Specifically, the Exchange's payments for any and all system failures on a single trading day are capped at \$250,000 under subsection (d)(1). The rule text states that for the aggregate of all claims made by all market participants related to the use of the Exchange on a single trading day, the Exchange's payments shall not exceed \$250,000. Subsection (d)(2) further provides that if the cumulative claims exceed the \$250,000 cap, this amount would be proportionally allocated among all such claims. Finally, subsection (d)(3) specifies that in order for a member to be eligible to receive payment under this Rule, claims for payment must be made in writing and submitted no later than the opening of trading on the next business day after the loss. Once in receipt of a claim, the Exchange is required to verify that: (i) a valid order was accepted into the Exchange's systems; and (ii) an Exchange system failure occurred during the execution or handling of that order. A system failure will be deemed to have occurred when there is a malfunction of the Exchange's physical systems, devices or software.

The Exchange now proposes to amend the existing rule text in Rule 705(d) to adopt the same liability caps and reimbursement requirements as the Nasdaq Exchanges.⁶ Proposed Rule 705(d) would provide that the Exchange may, notwithstanding the general limitations on liability contained in Rule 705(a), compensate users of the Exchange for losses directly resulting from the

⁶ See note 4 above.

actual failure of the System,⁷ or any other Exchange quotation, transaction reporting, execution, order routing or other systems or facility to correctly process an order, quote, message, or other data, provided that the Exchange has acknowledged receipt of the order, quote, message, or data. This limited exception in proposed Rule 705(d) would be subject to certain conditions and requirements contained in proposed subsections (d)(1) – (3).

Subsection (d)(1) proposes that the aggregate payments for all compensation claims made by all market participants related to the use of the Exchange during a single calendar month would not exceed the larger of \$500,000, or the amount of the recovery obtained by the Exchange under any applicable insurance policy.⁸ Under this proposal, the Exchange will eliminate the existing \$250,000 daily cap on liability and consider all such claims on a monthly basis, subject to proposed \$500,000 monthly liability cap. Each Nasdaq Exchange currently analyzes total eligible liability claims on a per-month look-back basis. The Exchange's proposal to adopt an identical claims process, in effect, would allow ISE Mercury an increased capability to compensate a market participant up to the monthly cap of \$500,000 even though the losses occurred on a single day or were across multiple days for a single participant.

Proposed subsection (d)(2) specifies how the reimbursement funds would be allocated in the event all of the compensation claims submitted during a single calendar month exceed the \$500,000 monthly cap. Specifically, if all of the claims arising out of the use of the Exchange cannot be fully satisfied because in the aggregate they exceed the limitations provided for in the Rule (\$500,000), then the maximum permitted amount would be proportionally allocated among

⁷ “System” means the electronic system operated by the Exchange that receives and disseminates quotes, executes orders and reports transactions. See the Constitution of ISE Mercury, Section 13.1(ee).

⁸ See BX Rule 4626(b)(1), Phlx Rule 1015(1), and NSM Rule 4626(b)(1) for substantially similar provisions.

all such claims arising during a single calendar month.⁹ This is substantially similar to the existing process where the maximum amount is proportionally allocated among all such claims, except it would be for all claims arising during a one-month period under the proposed rule change rather than during a single trading day under the existing Rule.

Finally, proposed subsection (d)(3) specifies the requirements and procedures applicable to the submission of reimbursement claims. Specifically, all claims for compensation must be submitted in writing no later than 12:00 P.M. ET on the next business day following the day on which the use of the Exchange gave rise to such claims.¹⁰ As such, the Exchange is proposing to extend the deadline to submit compensation claims from the opening of trading on the next business day to 12:00 P.M. ET. The Exchange believes that the extension of time to make such compensation claims increases the ability of market participants to submit claims in a timely manner. Proposed subsection (d)(3) also states that nothing in the Rule obligates the Exchange to seek recovery under any applicable insurance policy. If the Exchange does seek and receive an insurance recovery that is larger than \$500,000, the amount of that recovery would limit the reimbursement funds available for the incident supporting the recovery to the greater recovery amount.¹¹

⁹ See BX Rule 4626(b)(2), Phlx Rule 1015(2), and NSM Rule 4626(b)(5) for substantially similar provisions.

¹⁰ See BX Rule 4626(b)(3) and Phlx Rule 1015(3) for substantially similar provisions. See also NSM Rule 4626(b)(6).

¹¹ There are no other practical differences between the Exchange's existing reimbursement rule and this proposal than as described above. Specifically these differences are: the liability caps (i.e. the greater of \$500,000 or, if the Exchange opts to seek recovery, the recovery amount under any applicable insurance policy), the look-back analysis period of one month, and the later claims deadline of 12:00 PM ET.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,¹² in general, and furthers the objectives of Section 6(b)(5) of the Act,¹³ in particular, in that it is designed to promote just and equitable principles of trade, 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. The proposal supports this policy by establishing a fair and transparent process by which the Exchange can accommodate claims for reimbursement for the failure of specified systems in specified facilities and under specified conditions. The Exchange believes that its proposal to amend Rule 705(d) will continue to promote fairness in the marketplace in situations where one or more firm's claim results from a problem in a function performed by the Exchange's trading system that is solely the fault of the Exchange. As noted above, the proposal would allow the Exchange an increased capability to compensate a market participant up to the monthly cap of \$500,000 even though the losses occurred on a single day or were across multiple days for a single participant. Furthermore, the proposed expansion of time to make such compensation claims would increase the ability of market participants to submit claims in a timely manner.

Lastly, the proposed rule change is intended to align the liability caps and compensation claims requirements with the caps and requirements currently provided by the Nasdaq Exchanges in order to provide consistent rules across the six HoldCo Affiliated Exchanges.¹⁴ Consistent rules, in turn, would simplify the regulatory requirements for members of the Exchange that are also participants on the Nasdaq Exchanges. The Exchange believes that the proposed rule

¹² 15 U.S.C. 78f(b).

¹³ 15 U.S.C. 78f(b)(5).

¹⁴ See note 4 above.

change would provide greater harmonization among similar rules of the HoldCo Affiliated Exchanges, resulting in greater uniformity and more efficient regulatory compliance. As such, the proposed rule change would foster cooperation and coordination with persons engaged in facilitating transactions in securities and would remove impediments to and perfect the mechanism of a free and open market and a national market system.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act because all members would be subject to the same liability caps and reimbursement requirements. The proposed rule change is designed to provide greater harmonization among similar rules across the six HoldCo Affiliated Exchanges, resulting in more efficient regulatory compliance for common members.

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

No written comments were either solicited or received.

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

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act¹⁵ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹⁶

¹⁵ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁶ 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change,

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: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

IV. Solicitation of Comments

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

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-ISEMercury-2017-04 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-ISEMercury-2017-04. 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

or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

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, D.C. 20549 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-ISEMercury-2017-04, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁷

Eduardo A. Aleman
Assistant Secretary

¹⁷ 17 CFR 200.30-3(a)(12).