SIG
SUSQUEHANNA

July 8, 2020

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Release No. 34-89062; File No. SR-CBOE-2020-050
Release No. 34-89058; File No. SR-CBOE-2020-051

Dear Ms. Countryman:

Susquehanna International Group, LLP ("SIG")[1] appreciates the opportunity to comment jointly on the above-referenced Cboe Exchange, Inc. ("CBOE" or the "Exchange") rule filings regarding its Automated Improvement Mechanism ("AIM" or "AIM Auction"). These filings propose, respectively: (1) to allow the account of a CBOE Market Maker with an appointment in the applicable option class to participate as principal interest or a solicited order ("Initiating Order") against a broker's agency order ("Agency Order") in an AIM Auction (the "MM Proposal"); and (2) to allow the Exchange to determine maximum size requirements for Agency Orders in SPX submitted through AIM and through the Complex Automated Price Improvement Mechanism ("C-AIM" or "C-AIM Auction")(the "Max Size Proposal").[2] For the reasons noted below, SIG supports the first proposal, but opposes the second.

SIG agrees with the Exchange proposal "to permit orders for the accounts of Market-Makers with an appointment in the applicable class to be solicited for the Initiating Order submitted for execution against an Agency order in a proprietary index option class into a simple AIM Auction pursuant to [CBOE] Rule 5.37 or a simple FLEX AIM Auction pursuant to [CBOE] Rule 5.73."[3] As discussed below, the circumstances that formed the basis for the current prohibition against appointed Market Makers from participating as an Initiating Order in an AIM or FLEX AIM Auction have materially changed, which change not only obviates the rationale for said prohibition, but works an unreasonable inequity against said Market Makers and unduly curtails liquidity to customer orders.

[1] SIG affiliated companies have operated as registered market makers and brokers in the U.S. securities markets for over 30 years, and collectively participate in a significant percentage of daily consolidated volume.
[2] A third rule filing (Release No. 34-89063; File No. SR-CBOE-2020-052) was submitted by the Exchange on the same date, June 12, 2020, regarding the minimum increment for C-AIM and FLEX AIM responses to SPX Combo Orders; however, SIG's comments address only the first two filings, as noted above.
[3] MM Proposal, p. 3.

As noted by the Exchange, the prohibition against appointed Market Makers' participation in Initiating Orders was because the Exchange initially only permitted appointed Market Makers (and Trading Permit Holders representing customers at the top of the Book) to submit responses to AIM and FLEX AIM Auctions. However, the Exchange now permits any user to submit responses to simple AIM and FLEX AIM Auctions. In its rule filing, the Exchange itself highlights the consequent unreasonable inequity, that "while market participants other than appointed Market-Makers may contribute liquidity to these crossing auctions as either contra orders or responses, appointed Market-Makers, who are the primary source of liquidity on the Exchange in their appointed classes, are limited in the manner in which they may provide liquidity to these auctions."[4]

Under the change in circumstances by which the CBOE now permits any user to submit responses to simple AIM and FLEX AIM Auctions, the legacy prohibition no longer makes sense. Moreover, said prohibition unduly constrains available liquidity and, as the Exchange points out, it believes that providing appointed Market Makers with an additional way to participate in electronic auctions will expand available liquidity for these auctions, which may increase execution and price improvement opportunities for customers' orders.[5]

In its MM Proposal, the Exchange made several statements regarding the alignment of electronic auctions with open outcry trading and the creation of additional liquidity and price improvement opportunities via electronic auctions. It noted, "The Exchange believes there is no reason to restrict Market-Makers' ability to provide liquidity into electronic auctions when they are able to similarly provide that liquidity in open outcry trading."[6] It also stated, "The Exchange also believes the proposed rule change will promote just and equitable principles of trade and remove impediments to and perfect the mechanism of a free and open market and a national market system because it will further align open outcry and electronic crossing auctions and the execution and price improvement opportunities available in both auctions …"[7]

We agree with these Exchange acknowledgements, particularly that the alignment of open outcry trading and electronic crossing auctions promotes just and equitable principles of trade and removes impediments to and perfects the mechanism of a free and open market. Accordingly, we oppose the Exchange's Max Size Proposal as it contravenes these acknowledged tenets.

While SIG wholeheartedly supports the inclusion of SPX options in AIM and C-AIM Auctions, we believe that the proposed ability of the Exchange to impose maximum Agency Order size limits in SPX contravenes just and equitable principles of trade as an unnecessary impediment to a free and open market.

The reasons cited by the CBOE for its proposal are: (1) the level of complexity, risk, and notional value of the SPX may limit retail customer participation to simpler strategies and smaller-sized orders; (2) increased smaller size order flow tends to attract market maker responses, as such orders are generally easier to hedge than larger orders, which may encourage market makers to compete to provide price improvement in an electronic auction process; (3) the Exchange's trading floor may be better for crosses in SPX with more complex orders, complicated strategies and larger size; and (4) based on a sample of

[4] *Id*, pp. 3-4.
[5] *Id*., p. 4.
[6] *Id*., p. 6.
[7] *Id*., p. 10.

SPX orders in AIM and C-AIM from a week in April, the Exchange found that price improvement over Agency Order limit prices in these electronic auctions was generally more beneficial on smaller orders than on larger orders. Even if these points were all true, which we do not concede, they do not support the imposition of a maximum order size limit.

CBOE makes the claim that since the specific factors regarding the SPX *may* limit retail customer participation to simpler strategies and smaller-sized orders, *therefore* a maximum order size limit may provide more price improvement opportunities in SPX geared towards retail customers.[8] This is a material, unfounded leap in logic. The prospect that retail customer order flow in electronic auctions may potentially be self-limiting of its own accord is not a ground to impose an artificial limit on electronic auction liquidity, let alone a basis to claim that such artificial limit may provide more price improvement opportunities to such order flow. Indeed, the self-limitation of retail order flow as asserted by the Exchange wholly obviates the need for an artificial order size limit.

Similarly, the prospect that SPX retail customer participation may be self-limited to smaller sized orders and that such order flow tends to attract market maker responses, provides no basis for imposing an artificial order size limit. Again, the opposite is true – the allegedly self-limited small order size of retail customer flow highlights that there is no need for an artificial order size limit.

The Exchange's proffered notion that its trading floor may be better for crosses in SPX with more complex orders, complicated strategies, and larger size likewise does not serve as a basis for artificially limiting the liquidity available to customers in electronic auctions. The Exchange's suggestion that the trading floor may be better is an unproven presumption, as there has been no side-by-side comparison with the electronic auctions. Moreover, if such complicated order flow would naturally gravitate to the floor in any event, because it is supposedly better, then there is again no need for an artificial limitation to engineer this result.

CBOE's observation, based on a sample of SPX orders from a week in April, that price improvement over order limit prices in the AIM and C-AIM auctions was generally more beneficial on smaller orders than on larger orders, again, does not justify the imposition of an artificial order size limit. Brokers have best execution obligations to monitor price improvement, and will route their orders in the manner demonstrated as the best course of action. There is no need to artificially curtail their choices and cut off what may prove to be the best means of handling such brokers' respective orders.

Moreover, CBOE's price improvement observation based on its sample review is of limited value. CBOE does not present any comparison of the reported electronic cross price improvement figures to open outcry SPX trades for similar order sizes, nor to electronic crosses in other CBOE products that have no maximum order size limit. Accordingly, it is unknown whether SPX retail customer flow across different size ranges would receive better, the same, or worse price improvement as between electronic or open outcry auctions.[9]

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[8] Max Size Proposal, p. 3.

[9] Contrary to CBOE's blanket generalization about SPX price improvement trends in its electronic auctions, the Exchange's own reported results reflect that AIM price improvement increased in the 251-500 contract size range over the 51–100 and 101–250 size ranges. Likewise, for C-AIM, price improvement increased as order sizes increased up to 100 contracts; and price improvement for order sizes from 100-500 contracts was greater than price improvement for orders of 1-10 contracts.

CBOE also expressed its belief that not permitting larger orders into the electronic auctions will encourage market makers to continue to provide liquidity in the trading crowd while providing retail customers with price improvement opportunities, which may increase competition for these orders. The Exchange offers no basis for this view, nor for the presumption that market makers would be less inclined and in need of encouragement to continue to provide liquidity in the trading crowd while providing price improvement to retail customers in electronic crosses. As an SPX market maker, SIG's commitment to provide price improvement on the CBOE floor in SPX would not be diminished by its opportunity to provide price improvement in SPX electronic auctions of any size. Indeed, we would look forward to it.

The imposition of a maximum order size in SPX electronic auctions impedes a free and open market by removing choices from the investing public. It precludes the market from determining best execution naturally, and artificially picks winners and losers in the competition for order flow by seeking to steer the flow based on unfounded concerns and leaps in logic, all arising from presumptive scenarios of what retail customers and liquidity providers "may" do. Indeed, CBOE does not explain how the proposal incentivizes retail flow in AIM for SPX by restricting their choices; it appears to be seeking to "fix" a problem that does not exist.

For these reasons, we agree with the Exchange's acknowledgment that the alignment of electronic auctions with open outcry trades promotes just and equitable principles of trade and enhances execution and price improvement opportunities; and accordingly oppose the Max Size Proposal. Again, we support the inclusion of SPX in the Exchange's electronic auctions, and urge that the Exchange not seek to make this needless impediment to a free and open market a pre-condition to such long-overdue inclusion.

Respectfully,

RJM/lm
Richard J. McDonald