SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-82949; File No. SR-CBOE-2018-016)

March 27, 2018

Self-Regulatory Organizations; Cboe Exchange, Inc.; Order Approving a Proposed Rule Change
to Amend Rules Related to the Complex Order Book

I.   Introduction

On February 2, 2018, Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") filed with

the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the

Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] a proposed rule change to

allow market makers and option specialists to rest orders in the Complex Order Book ("COB")

under certain circumstances. The proposed rule change was published for comment in the

Federal Register on February 16, 2018.[3] The Commission received no comments regarding the

proposal. This order approves the proposed rule change.

II.   Description of the Proposed Rule Change

CBOE Options Rule 6.53C(c)(i) allows the Exchange to determine which classes and

which complex order origin types (i.e., non-broker-dealer public customer, broker-dealers that

are not market-makers or specialists on an options exchange, and/or market-makers or specialists

on an options exchange) are eligible for entry into the COB and whether such complex orders

can route directly to the COB and/or from PAR to the COB. Cboe Options has determined that

the complex orders of market-makers (origin code "M") and market-makers or specialists on an

options exchange ("away market-makers") (origin code "N") in options on the S&P 500 ("SPX"

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[1]   15 U.S.C. 78s(b)(1).

[2]   17 CFR 240.19b-4.

[3]   See Securities Exchange Act Release No. 82689 (February 12, 2018), 83 FR 7092
        ("Notice").

and "SPXW") and the Cboe Volatility Index ("VIX") are not eligible for entry into the COB.[4]

The Exchange proposes to amend Cboe Options Rule 6.53C(c)(i) to provide that in a class in

which the Exchange determines that the complex orders of market-makers and specialists on an

options exchange are not eligible for entry into the COB, the Exchange may determine that

market-makers and specialists may enter their complex orders into the COB under two

circumstances. First, market-makers and specialists will be permitted to enter their complex

orders in the COB if their orders are on the opposite side of a priority customer complex order(s)

resting in the COB with a price not outside the national spread market ("NSM").[5] Cboe Options

notes that, unlike the leg markets in which market-makers provide liquidity through quotes,

market-makers are unable to submit quotes in the COB that indicate to customers the price at

which they are willing to trade.[6] Cboe Options believes that allowing market makers to enter

their orders in the COB will provide priority customers with information about where market

makers are willing to trade, thus creating potential execution opportunities for priority customers

whose orders are not satisfied by the leg markets or other complex orders.[7]

Second, the proposal will allow market-makers and options specialists to enter their

complex orders in the COB if their orders are on the opposite side of order(s) for the same

strategy on the same side that initiated a Complex Order Auction ("COA") if there are "x"

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[4] See Notice, 83 FR at 7092. See also Cboe Options Regulatory Circular RG15-195. To the extent an origin type is not eligible for entry into the COB, complex orders with that origin type may be entered into the Exchange's System as opening-only or immediate-or-cancel because these orders would not rest in the COB when the Exchange is open for trading.

[5] See Cboe Options Rules 6.53C(c)(i)(A)(1) and 1.1(bbbb) (defining "national spread market").

[6] See Notice, 83 FR at 7093.

[7] See id. See also Notice, 83 FR at 7094, Examples 1 and 2.

number of COAs within "y" milliseconds, counted on a rolling basis (the Exchange will determine the number "x" (which must be at least two) and time period "y" (which may be no more than 2,000)).[8] Cboe Options believes that it may be difficult for market-makers to respond to multiple auctions that occur within a short time period while managing risk related to the amount executed during those auctions.[9] In this regard, the Exchange states that market-makers have complicated risk modeling associated with their trading activity, which factors in the size, price, and frequency at which they trade with orders.[10] To help ensure that a market-maker does not trade with potentially erroneous orders and become overexposed to risk, the Exchange states that a market-maker may set its risk controls to stop responding to COAs when multiple COAs in a strategy occur within a short timeframe (e.g., a market-maker may program its system to respond only to a specific number of auctions within a time period), which reduces auction liquidity and potential price improvement for COA orders.[11] The Exchange notes, however, that multiple non-erroneous auctions in a strategy may occur within a short time period if, for example, a market participant's algorithmic trading breaks up a large order into a number of smaller orders.[12] Accordingly, the proposal will allow a market-maker that determines that it is appropriate to trade with COA orders under these circumstances to submit an order to the COB

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[8] See Cboe Options Rule 6.53C(c)(i)(A)(2).

[9] See Notice, 83 FR at 7093.

[10] See id.

[11] See id.

[12] See id.

that would be available to trade against multiple COA orders up to the amount the market-maker

is willing to trade for the strategy within its risk controls.[13]

The rule will require market-makers and specialists to cancel any unexecuted complex

orders in the COB no later than a specified time (which the Exchange will determine and may be

no more than five minutes) after the time the COB receives the order.[14] Cboe Options states that

it intends to set these parameters at levels that it believes will permit market-makers to have

sufficient time to submit orders into the COB to participate in COAs, a determination that the

Exchange will make based on market-maker feedback, business conditions, and data (including

trading volume data and information regarding the number of executions of market-maker orders

against complex orders).[15] In addition, Cboe Options states the time period within which a

market-maker must cancel its complex order will provide the market-maker with sufficient time

for the opposing customer to potentially re-price its order for execution against the market-

maker's order or for the market-maker's order to execute against an order following a COA.[16]

The Exchange states that it will have surveillance to enforce the proposed rule change,

which will monitor whether market-maker and away market-maker orders have been entered

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[13]   See id. Cboe Options notes that pursuant to Cboe Options Rule 6.53C(d), the order of a market-maker or options specialist resting in the COB on the opposite side of an auctioned order may be available for execution against any contracts of the auctioned order that did not execute during the auction. See id.

[14]   See Cboe Options Rule 6.53C(c)(i)(B). The Exchange will announce to Trading Permit Holders all determinations it makes pursuant to Cboe Options Rule 6.53C via Regulatory Circular. See Cboe Options Rule 6.53C, Interpretation and Policy .01. The Exchange states that it will provide Trading Permit Holders with sufficient advanced notice prior to changing any parameters its sets under the proposal. See Notice, 83 FR at 7093 n.5.

[15]   See Notice, 83 FR at 7093.

[16]   See id. at 7094.

only in the circumstances permitted under the proposal, and whether any unexecuted orders have

been cancelled by the deadline imposed by the proposal.[17]

III.   Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent

with the requirements of the Act and the rules and regulations thereunder applicable to a national

securities exchange.[18] In particular, for the reasons discussed below, the Commission finds that

the proposed rule change is consistent with Section 6(b)(5) of the Act,[19] which requires, 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 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 Commission believes that allowing market-makers and specialists to enter orders in

the COB on the opposite side of the market from priority customer orders resting in the COB, or

on the opposite side of the market when orders on the same side of the market for a particular

strategy have initiated a number of COAs within a short time period, as described more fully

above, is designed to result in the provision of additional liquidity to trade with customer orders,

potentially providing additional execution and price improvement opportunities for those

customer orders. As noted above, CBOE believes that allowing market-makers and specialists to

rest orders in the COB opposite priority customer interest in the COB that is not outside the

NSM could provide an execution opportunity for a priority customer order that has not executed

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[17]   See id. at 7094.

[18]   In approving this proposed rule change, the Commission has considered the proposed
         rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

[19]   15 U.S.C. 78f(b)(5).

against other complex order or leg market interest by providing the customer with information concerning the price at which a market maker is willing to trade with the customer's order; this information currently is not available because the COB has no market maker quotes indicating the price at which liquidity providers are willing to trade against customer orders.[20] Allowing market-makers and specialists to place orders in the COB following a number of COAs for the same strategy on the same side of the market could allow a market maker to determine to provide additional liquidity for customer orders, within the market-maker's risk controls, in circumstances where the market-maker's system has stopped responding to COAs.[21] The Commission notes that Cboe Options has represented that it will have surveillance to monitor compliance with the requirements of the rule.[22]

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[20]   See Notice, 83 FR at 7093.

[21]   See id.

[22]   See id. at 7094.

IV.   Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[23] that the

proposed rule change (SR-CBOE-2018-016) is approved.

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

authority.[24]

Jill M. Peterson
Assistant Secretary

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[23]   15 U.S.C. 78s(b)(2).

[24]   17 CFR 200.30-3(a)(12).