SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-101229; File No. SR-CBOE-2024-042)

October 1, 2024

Self-Regulatory Organizations; Cboe Exchange, Inc.; Notice of Filing of a Proposed Rule Change to Amend its Rules to Permit Orders Comprised of Options and Futures Legs ("Future-Option Orders")

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on September 17, 2024, Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") filed with the Securities and Exchange Commission ("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

Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") proposes to amend its Rules to permit orders comprised of options and futures legs ("future-option orders"). The text of the proposed rule change is provided in Exhibit 5.

The text of the proposed rule change is also available on the Exchange's website (http://www.cboe.com/AboutCBOE/CBOELegalRegulatoryHome.aspx), at the Exchange's Office of the Secretary, 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 Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the

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

[2]   17 CFR 240.19b-4.

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.   <u>Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change</u>

       1.   <u>Purpose</u>

The Exchange proposes to amend its Rules to permit future-option orders, which would

be comprised of both options and futures legs. The Exchange understands it is common for

investors to engage in hedging or other investment strategies that involve options and related

futures products. However, to execute those investment strategies, investors must submit the

options order to the Exchange and separately submit the futures order to a designated contract

market ("DCM") on which the futures trade. For example, market participants may obtain

positions in Cboe Volatility Index ("VIX") options through transactions on the Exchange and

hedge those positions entering into a separate transaction on Cboe Futures Exchange, LLC's

("CFE") centralized market in VIX futures ("VX futures"). Separate executions of this sort

create additional risks, including risk that one order will execute while the other does not and

price risk resulting from the time it takes to complete both transactions. The Exchange

understands that due to those risks and the complexities of multi-part transactions, market

participants may instead transact in the over-the-counter ("OTC") market or not obtain a hedge at

all. The proposed rule change adopts a mechanism to facilitate the execution of these cross-

product transactions in a simple, efficient manner that reduces these execution and price risks.

The Exchange first proposes to adopt a definition of a future-option order. Specifically,

the proposed rule change amends Rule 1.1 to define a "future-option order"[3] as an order to buy

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[3]   As proposed, a "future-option order" is deemed an inter-regulatory spread order for purposes of the Rules.

or sell a stated number of units of an underlying or a related futures contract(s) coupled with the purchase or sale of an option contract(s) on the Exchange.[4] The Exchange would designate in which classes future-option orders would be available.[5]

The proposed definition of a future-option order includes a risk offset requirement. A user may only submit a future-option order if it satisfies the applicable risk offset requirement. The Exchange believes a risk offset requirement will provide market participants with sufficient flexibility to execute legitimate strategies comprised of options and futures while preventing a market participant from using the proposed execution mechanism to execute a futures trade outside of the normal trading process on the applicable designated contract market by combining the future leg(s), for example, with an inexpensive out-of-the-money option leg.

Rule 1.1 defines an inter-regulatory spread order as an order involving the simultaneous purchase and/or sale of at least one unit in contracts each of which is subject to different regulatory jurisdictions at stated limits, or at a stated differential, or at market prices on the floor of the Exchange. The proposed rule change modernizes this definition to apply it to the Exchange in general, as opposed to the floor of the Exchange (the definition of inter-regulatory spread order was adopted when all trading on the Exchange occurred in open outcry).

[4]   The proposed definition of a future-option order is similar to the definition of a stock-option order. Rule 1.1 defines a "stock-option order" as an order to buy or sell a stated number of units of an underlying or a related security coupled with either (a) the purchase or sale of option contract(s) on the opposite side of the market representing either the same number of units of the underlying or related security or the number of units of the underlying security necessary to create a delta neutral position or (b) the purchase or sale of an equal number of put and call option contracts, each having the same exercise price and expiration date, and each representing the same number of units of stock as, and on the opposite side of the market from, the underlying or related security portion of the order. The primary difference is the stock-option order definition requires the order to be delta neutral, while the proposed definition of a future-option order requires the order to have a risk offset within a specified range (as described below).

[5]   Pursuant to Rule 1.5, the Exchange announces all determinations it makes pursuant to the Rules via specifications, Notices, or Regulatory Circulars with appropriate advanced notice, which will be posted on the Exchange's website, or as otherwise provided in the Rules; electronic message; or other communication method as provided in the Rules. The Exchange intends to initially permit future-option orders overlying VIX. However, the Exchange may expand the availability of future-option orders to other underlying securities or indexes in the future. If required, the Exchange and would submit rule filings in connection with any such expansion; for example, the Exchange may determine that a different risk offset requirement than what is proposed in this filing is appropriate for another underlying based on the characteristics of the overlying options and futures.

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Pursuant to paragraph (a) of the proposed definition of future-option order, the System will accept a future-option order if the future leg(s) provides no less than 10% and no greater than 125% risk offset to the option leg(s).[6] A future-option order satisfies this risk offset requirement if the net delta value of the order is no greater than -0.10 and no less than -1.25. The delta value of an option leg equals the expected change in the price of that options contract given a $1.00 change in the price of the underlying security or index. The delta value of a future leg equals the amount set forth in the rules or contract specifications of the designated contract market ("DCM") on which the future contract trades. The delta value of each option and future leg is multiplied by the applicable multiplier. The sum of the future legs delta values divided by the sum of the option legs delta values, which equals the net delta value for the order.

For VIX future-option orders, the System will calculate the risk offset described above using the net delta value for each "group" of option legs and future legs with the same expiration date. The net delta value of each group must be no greater than -0.10 and no less than -1.25.[7] For example, suppose a VIX future-option order is submitted with the following components:

- Sell 1 Dec VX future[8] with a delta of -1

- Buy 2 Jan VX futures with delta of 1

- Buy 16 Dec VIX option[9] calls with a delta of 0.50

- Buy 35 Jan VIX option puts with a delta of -0.60

[6]   The user must include a delta value for each option leg of the order when submitting a future-option order. See Rule 1.1 (proposed paragraph (b)(2) of definition of future-option order). While a user may use any methodology it chooses to calculate the delta value of option legs, the value must be reasonable and will be subject to surveillance by the Exchange's regulatory division. The System will use the user-submitted delta values to calculate the risk offset for the entire order.

[7]   If any option contract leg or future contract leg cannot be grouped with any future leg(s) or option leg(s), respectively, the System rejects a VIX future-option order.

[8]   VX futures have a contract multiplier of 1,000.

[9]   VIX options have a contract multiplier of 100.

The 1 short Dec VX future is grouped with the 16 long Dec VIX calls, which group has a net delta of /(-1 x 1,000)/(16 x .50 x 100) = -1,000/800 = -0.125. The 2 long Jan VX futures are grouped with the 35 short Jan VIX puts, which group has a net delta of (2 x 1,000)/(35 x -0.60 x 100) = -2,000/2,100 = -0.9524. This order would satisfy the risk offset requirement, as both groups have a net delta between -0.10 and -1.25. If the System determines that a complex strategy comprised of future and option legs satisfies the risk offset requirement, it accepts all future-option orders for that complex strategy for the remainder of that trading day. This will prevent a situation in which the Exchange accepts a future-option order for a specific complex strategy on a trading day but cannot execute against future-option orders for the same complex strategy submitted later that trading day but no longer satisfies the risk offset requirement because the delta values have changed since the initial order was submitted.[10]

The proposed rule change also amends the definition of "complex order" in Rule 1.1 to provide that unless the context otherwise requires, the term complex order will include future-option orders.[11]

As proposed in Rule 5.33(o), when a user submits a future-option order to the Exchange:

- if the User is also a member of the DCM on which the applicable future trades and the Exchange has established electronic communication with the DCM, the Exchange will electronically communicate the future component of the future-option order to the DCM on behalf of the User[12]; or

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[10] It is for this reason a user may not designate a future-option order submitted for electronic processing as GTC or GTD. See proposed Rule 1.1 (proposed paragraph (b)(1) of definition of future-option order).

[11] The term complex order already includes cross-product orders such as stock-option orders and security future-option orders.

[12] Unlike stock, a future trades on one DCM, which would make such direct communication with the DCM possible. This would only be available if the DCM and Exchange established electronic communication between the two markets to permit this direct communication of the futures component.

- if the User is not also a member of the DCM on which the applicable future trades or opts out of the direct communication described in the above bulleted paragraph (or such direct communication is unavailable), the User must designate a specific futures commission merchant ("FCM") or introducing broker ("IB") with which it has entered into an agreement pursuant to proposed Rule 5.33, Interpretation and Policy .05 (the "designated FCM/IB") to which the Exchange will communicate the futures component of the future-option order on behalf of the user.[13] Proposed Interpretation and Policy .05 provides that if the user is not also a member of the DCM on which the applicable future trades or opts out of the direct communication (or such direct communication is unavailable), to submit a future-option order to the Exchange for execution, a user must enter into an agreement with one or more FCMs or IBs that are not affiliated with the Exchange, which FCM/IB(s) the Exchange has identified as having connectivity to electronically communicate the futures components of future-option orders to the designated contract market on which the futures trade.[14] This will provide users with flexibility to pick which FCM/IB will communicate the futures components of their orders for execution (if an FCM/IB is necessary for communication of the futures component to the DCM).[15]

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[13] As is the case with any order submitted to the Exchange, only authorized Users and associated persons of Users may establish connectivity to and access the Exchange to submit orders. See Rule 5.5(a). A "User" is defined as a Trading Permit Holder ("TPH") or Sponsored User who is authorized to obtain access to the System pursuant to Rule 5.5. See Rule 1.1 (definition of User). The Exchange currently has no Sponsored Users, so the term "User" at present is synonymous with the term "TPH." The User and any individuals associated with the User that submits a future-option order must have any required futures industry registrations and comply with applicable rules of the designated contract market on which the futures trades and the Commodity Futures Trading Commission ("CFTC").

[14] This requirement is substantially identical to that required for stock-option orders.

[15] The Exchange intends to establish an arrangement with one or more FCMs/IBs that are members of the

The proposed rule change first amends Rule 5.33 to describe how future-option orders may execute electronically on the Exchange. The proposed rule change adds future-option order to the list of types of complex orders that may be accepted for electronic trading.[16] Specifically, the proposed rule change amends Rule 5.33(b)(5) to reference the proposed definition of future-option order in Rule 1.1 and state that only future-option orders in the classes designated by the Exchange[17] with no more than the applicable number of legs are eligible for electronic processing.[18] Future-option orders submitted for electronic processing may execute pursuant to a complex order auction ("COA") if eligible as described in Rule 5.33(d) or in the complex order book ("COB") as described in Rule 5.33(e) and will execute in the same manner as other complex orders, except as described below.

The proposed rule change adopts rule 5.33(f)(1)(C) to provide that users may express bids and offers for a future-option order in any decimal price the Exchange determines, which will permit the Exchange to accommodate the available pricing of futures. The minimum increment for the option leg(s) of a future-option order is $0.01 or greater, which the Exchange may determine on a class-by-class basis, regardless of the minimum increments otherwise applicable to the option leg(s),[19] and the future leg(s) of a future-option order may be executed in

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applicable designated contract market, pursuant to which arrangement those FCMs/IBs will have connectivity to the Exchange to receive the futures components of future-option orders and communicate those to the applicable designated contract market for execution of these futures components.

[16]   The proposed rule change also amends Rule 5.70(b) to provide that the Exchange may make future-option orders available for flexible (FLEX) options trading.

[17]   This flexibility with respect to classes is necessary given the Exchange would need to establish a relationship with appropriate DCMs on which futures trade before it would be able to accept future-option orders that contain futures legs that trade on those DCMs.

[18]   The proposed rule change also provides that future-option orders will execute (electronically) in the same manner as other complex orders except as otherwise specified in Rule 5.33.

[19]   This is consistent with the permissible pricing of options legs of complex orders and stock-option orders. See Rule 5.4(b) and 5.33(f)(A) and (B).

any decimal price permitted in the designated contract market on which the applicable futures

trade. Smaller minimum increments are appropriate for future-option orders as the future

component may be able to trade at finer decimal increments permitted by the designated contract

market on which the futures trade. The Exchange notes that even with the flexibility provided in

the proposed rule, the individual options legs must trade at increments allowed by the

Commission.

The proposed electronic execution process of future-option orders is substantially similar

to that of stock-option orders. Proposed Rule 5.33(o)(2) provides that a future-option order may

execute against other future-option orders (or COA Responses, if applicable), but may not

execute against orders in the simple book.[20] If a future-option order can execute upon entry or

following a COA, or if it can execute following evaluation while resting in the COB pursuant to

Rule 5.33(i), the System executes the option component (which may consist of one or more

option legs) of a future-option order against the option component of other future-option orders

resting in the COB or COA responses pursuant to the allocation algorithm applicable to the class

(pursuant Rule 5.33(d)(5)(A)(ii)), as applicable, but does not immediately send the user a trade

execution report, and then automatically communicates the future component(s) to the DCM or

the designated FCM/IB, as applicable, for execution at the DCM on which the futures trade. If

the System receives an execution report for the future component from the DCM or the

designated FCM/IB, as applicable, the Exchange sends the user the trade execution report for the

future-option order, including execution information for the future and option components. If

the System receives a report from the DCM or the designated FCM/IB, as applicable, that the

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[20]   See also proposed Rule 5.33(g)(5) (which provides that future-option orders, like stock-option orders, may
not leg into the simple book).

future component(s) cannot execute,[21] the Exchange nullifies the option component trade and notifies the user of the reason for the nullification. If a future-option order is not marketable, it rests in the COB (if eligible to rest) or routes to PAR for manual handling, subject to a user's instructions. The Exchange believes this proposed process is reasonable, because the options and futures components of a future-option order are submitted for execution as part of the same investment strategy. Given this, if the future component does not execute, the Exchange believes it is reasonable to expect that a user that submitted a future-option order to request nullification of the options trade (as permitted by Rule 6.5). If the future component does not execute, rather than require the user that submitted the future-option order to contact the Exchange to request nullification of the option component execution pursuant to Rule 6.5, the proposed rule eliminates this requirement for the user to make such request. Instead, the proposed rule change provides that the Exchange will automatically nullify the option transaction if the future component does not execute. The Exchange believes such nullification without a request from the user is consistent with the purpose of future-option orders, as contingent execution at or near the same time (and thus reduction in price and execution risk) is one of the primary goals of future-option orders (as further discussed below).

Future-option orders may also be submitted for execution (if eligible) in the complex automated improvement mechanism ("C-AIM") as described in Rule 5.38 or complex solicitation auction mechanism ("C-SAM) as described in Rule 5.40. Processing of future-option

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[21]   Execution of the futures components will need to satisfy requirements of the applicable designated contract market, including informational and reporting time requirements, risk controls, and price restrictions (such as needing to be within the daily quotation range). Pursuant to Rule 5.33(k), trading in any complex strategy (including one that comprises a future-option order) is suspended if any component of a complex strategy (including a future leg) is halted. Therefore, if trading in a future is halted, it could not execute and would result in the future-option order not being executed.

orders through C-AIM or C-SAM will occur in the same manner as any other complex orders

submitted into those execution mechanisms.

Proposed Rule 5.33(o)(2) provides that a future-option order may only execute if the

price complies with subparagraph (f)(2)(B). The proposed rule change amends Rule 5.33(f)(2)

to describe the permissible execution prices and priority of future-option orders, which is

substantially similar to that of stock-option orders. Specifically, proposed Rule 5.33(f)(2)(C)

states for a future-option order with one option leg, the option leg may not trade at a price worse

than the individual component price on the simple book or at the same price as a priority

customer order on the simple book. For a future-option order with more than one option leg, the

option legs must trade at price pursuant to Rule 5.33(f)(2)(A), which is the permissible execution

prices and priority for complex orders comprised of option legs. The System, therefore, will not

execute a future-option order at a net price: (1) that would cause any option component of the

complex strategy to be executed at a price of zero; (2) that would cause any option component of

the complex strategy to be executed at a price worse than the individual component prices on the

simple book; (3) worse than the price that would be available if the complex order legged into

the simple book; or (4) worse than the synthetic best bid or offer ("SBBO")[22] or equal to the

SBBO when there is a priority customer order on any leg comprising the SBBO and, if a

conforming complex order,[23] at least one option component of the complex order must execute at

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[22]   The proposed rule change adds subparagraph (3) to the definition of SBBO in Rule 5.33(a) to provide that
        the SBBO is the best net bid and best net offer on the Exchange for a complex strategy calculated using, for
        future-option orders, the BBO for each component (or the national best bid or offer ("NBBO") for a
        component if the BBO for that component is not available) and the daily quotation range for each future
        component. Similarly, the proposed rule change adds subparagraph (3) to the definition of synthetic
        national best bid or offer ("SNBBO") in Rule 5.33(a) to provide that the SNBBO is the national best net bid
        and net offer for a complex strategy calculated using, for future-option orders, the NBBO for each option
        component and the daily quotation range for each future component.

[23]   The proposed rule change amends the definition of "conforming complex order" in Rule 1.1 to provide that
        a future-option order is conforming (1) if the ratio on the options legs is greater than or equal to one-to-
        three (.333) or less than or equal to three-to-one (3.00) or (2) the options legs comprise an Index Combo

a price that improves the best bid or offer ("BBO") for that component by at least one minimum

increment or, if a nonconforming complex order,[24] the option component(s) of the complex order

for the leg(s) with a priority customer order at the BBO must execute at a price that improves the

price of that priority customer order(s) on the simple book by at least one minimum increment.[25]

Pursuant to these proposed changes, the option component(s) of a future-option order will

ultimately trade in the same manner and in accordance with the same priority principles as they

would if they had been submitted without a future leg.

The proposed rule change also amends Rules in Chapter 5, Section G of the Rulebook to

describe how future-option orders may execute in open outcry on the Exchange's trading floor,

which is substantially similar to the open outcry execution process of stock-option orders.

Specifically, the proposed rule change amends Rule 5.83(b) to provide that the Exchange may

make future-option orders available for PAR routing for manual handling (as is the case for other

complex orders, including stock-option orders). The proposed rule change further amends this

provision to provide that the Exchange may determine (as it can for other nonconforming

complex orders and non-conforming stock-option orders) to make nonconforming future-option

orders not eligible for electronic processing, in which case such orders would only be eligible for

manual handling and open outcry trading. The proposed rule change amends Rule 5.85(g) to

provide that a bid or offer that is identified to the trading crowd as part of a future-option order is

made and accepted subject to the following conditions (which are the same conditions applicable

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order (as defined in Rule 5.33(b)).

[24]   The proposed rule change amends the definition of "nonconforming complex order" in Rule 1.1 to provide
that a future-option order is nonconforming if the ratio of its options legs is less than one-to-three (.333) or
greater than three-to-one (3.00) (unless the options legs comprise an Index Combo order).

[25]   All-or-none complex orders (including future-option orders) may only execute at prices better than the
SBBO.

to stock-option orders): (1) at the time the future-option order is announced, the TPH initiating the order must disclose to the crowd all legs of the order and identify the specific market(s) on which and the price(s) at which the non-option leg(s) of the order is to be filled; and (2) concurrent with the execution of the options leg of the order, the initiating TPH and each TPH that agrees to be a contra-party on the non-option leg(s) of the order must take steps immediately to transmit the non-option leg(s) to the identified market(s) for execution.[26] Proposed Rule 5.85(b)(3) provides, however, that (like the stock component of stock-option orders) a floor broker or PAR official may, subject to a User's instructions, route the future component of a future-option order represented in open outcry to the DCM or an Exchange-designated FCM/IB not affiliated with the Exchange for execution at a designated contract market on which the futures trade in accordance with proposed Rule 5.33, Interpretation and Policy .05.[27] The Exchange also proposes to add subparagraph (5) to Rule 5.85(g) (which is substantially similar to Rule 5.85(g)(4) for stock-option orders) to provide that a TPH or PAR official may route the future component of an eligible future-option order represented in open outcry from PAR directly to a designated FCM/IB (as defined in Rule 5.33(o)) not affiliated with the Exchange for electronic execution at the designated contract market on which the futures trade (1) in accordance with the order's terms, and (2) as a single order or as a paired matching order (including with orders transmitted from separate PAR workstations). TPHs seeking to route the future component of a future-option order represented in open outcry through PAR to an

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[26] The proposed rule change also updates Rule 5.85(g)(2) to provide that a trade representing execution of the options leg of a future-option order may be cancelled at the request of any TPH that is a party to that trade only if market conditions in any of the non-Exchange market(s) prevent the execution of the non-option leg(s) at the price(s) agreed upon.

[27] The proposed rule change also makes a nonsubstantive amendment to Rule 5.85(b)(3) to correct the current cross-reference to Rule 5.11 to Rule 5.33, Interpretation and Policy .04, which is the applicable rule to be referenced.

Exchange-designated FCM/IB not affiliated with the Exchange for electronic execution at the designated contract market on which the futures trade must comply with proposed Rule 5.33(o).[28] The Exchange proposes to amend Rule 5.91(g) to provide that as they currently can for complex orders (including stock-option orders), floor brokers may leg future-option orders where one of the legs is executed on the Exchange.

The proposed rule change amends Rule 5.85(b)(3) to describe the priority that will apply to future-option orders executed on the Exchange's trading floor. Specifically, the proposed rule change provides that future-option orders have priority over bids (offers) of in-crowd market participants but not over priority customer bids (offers) in the book. Specifically, future-option orders, like stock-option orders, will have priority over bids and offers of in-crowd market participants on the trading floor. Further, the options legs of conforming and nonconforming future-option orders may be executed at the same net debit and credit prices as the options legs of stock-option orders. Pursuant to proposed Rule 5.85(b)(4), a conforming future-option order may be executed at a net debit or credit price without giving priority to equivalent bids (offers) in the individual series legs that are represented in the trading crowd or in the book if the price of at least one option leg of the order improves the corresponding bid (offer) of a priority customer order(s) in the book by at least one minimum trading increment as set forth in Rule 5.4(b).[29]

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[28] If any TPH that is a party to a trade representing the execution of the options leg of a future-option order requests, if market conditions in any of the non-Exchange market(s) prevent the execution of the non-option leg(s) at the price(s) agreed upon, the execution of the option leg may be cancelled. See proposed Rule 5.87, Interpretation and Policy .03. This is consistent with what is permissible for stock-option orders, as well as the proposed electronic processing of future-option orders set forth in proposed Rule 5.33(o).

[29] In other words, if there is a priority customer order on every leg comprising the SBBO, at least one option leg of the future-option order must execute at a price that improves the price of the priority customer order on the simple book for that leg by at least one minimum increment. This is the same priority that applies to a conforming complex order (comprised of all option legs) as set forth in Rule 5.85(b)(1), and thus the options legs of a conforming future-option order will execute subject to the same priority as they would if they had been submitted without a future leg.

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Additionally, pursuant to proposed Rule 5.85(b)(5), a nonconforming future-option order may be executed at a net debit or credit price without giving priority to equivalent bids (offers) in the individual series legs that are represented in the trading crowd or in the book if each option leg of the order betters the corresponding bid (offer) of a priority customer order(s) in the book on each leg by at least one minimum trading increment as set forth in Rule 5.4(b).[30]

The Exchange proposes to amend Rule 6.5, Interpretation and Policy .07 to describe how a future-option order may qualify as an obvious error. As proposed, future-option orders will be handled in a similar manner as stock-option orders for purposes of Rule 6.5. Specifically, if the option leg of a future-option order qualifies as an obvious error under Rule 6.5(c)(1) or catastrophic error under Rule 6.5(d)(1), then the option leg that is an obvious or catastrophic error will be adjusted in accordance with Rule 6.5(c)(4)(A) or (d)(3), respectively, regardless of whether one of the parties is a customer. However, the option leg of any customer future-option order will be nullified if the adjustment would result in an execution price higher (lower) for buy (sell) transactions than the customer's limit price on the future-option order, and the Exchange will attempt to nullify the future leg. Whenever a DCM nullifies the futures leg(s) of a future-option order or whenever the future leg(s) cannot be executed, the Exchange will nullify the option leg upon request of one of the parties to the transaction or in accordance with Rule 6.5(c)(3).

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[30]   In other words, if there is a priority customer order on any leg(s) comprising the SBBO, the component(s) of the future-option order for the option leg(s) with a priority customer order at the BBO must execute at a price that improves the price of that priority customer order(s) on the simple book by at least one minimum increment. This is the same priority that applies to a nonconforming complex order (comprised of all option legs) as set forth in Rule 5.85(b)(2), and thus the options legs of a nonconforming future-option order will execute subject to the same priority as they would if they had been submitted without a future leg.

Finally, the proposed rule change adds Interpretation and Policy .02 to Rule 6.6 to clarify that TPHs may update only the option component of a future-option order trade using Clearing Editor (and as permitted by Rule 6.6). Any updates to the future component would need to be done in accordance with the Rules of the applicable DCM (if permissible).

Execution of the options components of future-option orders will be subject to Commission jurisdiction, and execution of the futures components of future-option orders will be subject to Commodity Futures Trading Commission ("CFTC") jurisdiction. Further, each of the Exchange and the designated contract market on which the futures component of a future-option order trades will regulate conduct relating to future-option orders and trades with respect to compliance with its rules, including bringing disciplinary actions for violations of its rules. Before authorizing a class of future-option orders to trade on the Exchange, the Exchange would enter into an information sharing agreement with the designated contract market on which the applicable future trades that encompasses information relating to future-option orders and trades.[31] This would allow for the sharing of information between the Exchange and the DCM to permit the Exchange (and the DCM) to have access to all order, trade, regulatory, and other data relating to these orders and trades.

2.   Statutory Basis

The Exchange believes the proposed rule change is consistent with the Securities Exchange Act of 1934 (the "Act") and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.[32] Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)[33] requirements

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[31]   The Exchange already has one in place with CFE for purposes of VIX future-option orders.

[32]   15 U.S.C. 78f(b).

[33]   15 U.S.C. 78f(b)(5).

that the rules of an 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, 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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)[34] requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes the proposed rule change will 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 because it will provide investors with greater opportunities to manage risk. The proposed rule change would provide investors with a more efficient mechanism to execute options and related future products, which investors regularly trade as part of hedging and other investment strategies. The proposed execution mechanism for future-option orders will make the trading and hedging process for investment strategies comprised of option and future components more efficient, which will reduce execution, legging, and price drift risk that otherwise accompanies the current execution process for these strategies. For example, today, investors looking to execute an investment strategy comprised of option and future components must do so through separate trades – one for the options and one for the futures. This creates risk that one trade occurs but the other does not, which may leave an investor with an unhedged position. Additionally, separate transactions create risk because market conditions may change between the time it takes to execute both transactions, which may

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[34]   Id.

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make the full package execute in an unfavorable manner for the investor. Investors may

continue to execute these strategies as separate transactions if they so choose. However, the

addition of the proposed execution process (both electronic and open outcry) would provide

investors with an optional, alternative means to execute strategies comprised of future and

options components that would reduce these risks, as it would permit the entire package to be

priced together and will result in an execution only if both the options and futures components

are able to trade. The proposed single execution mechanism, therefore, expands the ability of

market participants to engage in cross-product investment and hedging transactions, which the

Exchange believes will contribute to reduced overall market risk and increased liquidity.

The Exchange believes the proposed rule change is designed to prevent fraudulent and

manipulative acts and practices and to promote just and equitable principles of trade. The

proposed risk offset requirement is designed to provide market participants with sufficient

flexibility to execute legitimate options strategies comprised of options and futures while

preventing misuse of this mechanism, such as a market participant from using the proposed

execution mechanism to execute a futures trade outside of the normal trading process on the

applicable designated contract market by combining the future leg(s), for example, with an

inexpensive out-of-the-money option leg.

As discussed above, the Commission and the CFTC will maintain jurisdiction over

execution of the options and futures components, respectively, of future-option orders. Further,

each of the Exchange and the DCM on which the futures component of a future-option order

trades will regulate conduct relating to future-option orders and trades with respect to

compliance with its rules, including bringing disciplinary actions for violations of its rules.[35]

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[35]   This would include any rules the designated contract market related to the execution of the future

The Exchange is a member of the Intermarket Surveillance Group ("ISG"). The ISG members work together to coordinate surveillance and investigative information sharing in the futures and options markets, and the Exchange would therefore have access to information regarding relevant trading activity from other ISG members, including applicable DCMs (as CFE is) that are also members. Before authorizing a class of future-option orders to trade on the Exchange, if the applicable DCM was not a member of ISG, or if the applicable DCM was a member of ISG but the Exchange still deemed appropriate, the Exchange would enter into an information sharing agreement with the designated contract market on which the applicable future trades that encompasses information relating to future-option orders and trades. This would allow for the sharing of information between the Exchange and the designated contract market to permit the Exchange (and the designated contract market) to have access to all order, trade, regulatory, and other data relating to these orders and trades, and thus facilitate the intermarket surveillance of future-option orders. As a self-regulatory organization, the Exchange recognizes the importance of surveillance, among other things, to detect and deter fraudulent and manipulative trading activity as well as other violations of Exchange rules and the federal securities laws. The Exchange's current rules prohibiting market manipulation and fraudulent, noncompetitive, and disruptive trading practices will apply to future-option orders. The Cboe Regulatory Division will incorporate information it receives from the designated contract market into its surveillance procedures to monitor trading of future-option orders, including to detect any manipulative trading activity. The Exchange believes its surveillance, along with the proposed risk offset requirement, are reasonably designed to detect manipulative trading and enforce compliance with the proposed rules and other Exchange Rules. The Exchange performs ongoing evaluations of

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component of a future-option order.

its surveillance program to ensure its continued effectiveness and will continue to review its surveillance procedures on an ongoing basis and make any necessary enhancements and/or modifications that may be needed for future-option orders.

The Exchange believes the proposed execution process will also promote just and equitable principles of trade. As described above, future-option orders will execute in a substantially similar way as complex orders, including stock-option orders. The proposed priority for future-option orders will protect customer orders in the simple book. As proposed, the option component(s) of a future-option order will ultimately trade in the same manner and in accordance with the same priority principles as they would if they had been submitted without a future leg. Further, the proposed process to nullify the option component execution if the future-option order does not execute is consistent with the purpose of the future-option order. Given the option and future components of a future-option order are submitted as part of the same investment strategy, if the future component does not execute, the Exchange believes it is reasonable to expect that a user that submitted a future-option to request nullification of the options trade in accordance with current Exchange Rules. If the future component does not execute, rather than require the user that submitted the future-option order to contact the Exchange to request nullification of the option component execution, the proposed rule eliminates this requirement for the user to make such request. Instead, the proposed rule change provides that the Exchange will automatically nullify the option transaction if the future component does not execute. The Exchange believes such nullification without a request from the user is consistent with the purpose of future-option orders, as contingent execution at or near the same time (and thus reduction in price and execution risk) is one of the primary goals of future-option orders (as further discussed below).

Additionally, the Exchange believes the availability of future-option orders will 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 because it will provide investors with an alternative to the OTC market for investment strategies comprised of future and option components. The proposed rule change will provide investors with the ability to execute these investment strategies in a listed market environment as opposed to in the unregulated OTC market. The proposed rule change may shift liquidity from the OTC market onto the Exchange (as well as shift swaps and OTC combos from the OTC market onto designated contract markets in the form of futures), which the Exchange believes would increase market transparency as well as enhance the process of price discovery conducted on the Exchange through increased order flow to the benefit of all investors. The Exchange believes it may be a more attractive alternative to the OTC market, because trading these strategies in an exchange environment may benefit market participants in several ways, including but not limited to the following: (1) enhanced efficiency in initiating and closing out positions; (2) increased market transparency; and (3) heightened contra-party creditworthiness due to clearing requirements for listed options and futures.

The Commission previously determined that permitting investors to submit an order for execution to Cboe that included components subject to different regulatory jurisdictions was consistent with the Act.[36] Specifically, in 1988, the Commission approved a Cboe proposed rule change to allow inter-regulatory spread orders (which were defined as the simultaneous purchase and/or sale of at least one unit in contracts each of which is subject to different regulatory jurisdictions at stated limits, or at a stated differential, or at market prices on the floor of the

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[36] Securities Exchange Act Release No. 26271 (November 10, 1988), 53 FR 46727 (November 18, 1988) (SR-CBOE-88-17) ("CBOE-CBOT JV Approval Order"); see also Securities Exchange Act Release No. 24235 (March 19, 1987), 52 FR 9750 (March 26, 1987) (SR-Phlx-86-43).

Exchange) to trade on Cboe's trading floor.[37] The only substantive differences between that

proposal and the proposed rule change regarding future-option orders are as follows:

- The proposed rule change would permit future-option orders in classes authorized

  by the Exchange, dependent upon agreements the Exchange may make with

  applicable DCMs, compared to the prior filing that was limited to orders

  comprised of two options and two related futures.[38] The Exchange believes this is

  reasonable because the proposed rule change will provide the Exchange with the

  ability to expand the availability of future-option order functionality in the future

  to accommodate additional investment strategies of investors, and the proposed

  rules regarding future-option orders would apply in the same manner regardless of

  the underlying components.[39]

- The proposed rule change would permit electronic execution in addition to open

  outcry execution of future-option orders. This merely reflects the advancement in

  the availability of electronic trading since 1988 and provides an additional manner

  of execution for future-option orders.

- The proposed rule change does not create a separate pit on the Exchange's trading

  floor for the related futures as the prior proposal did. Given the advances in

  electronic trading (and the fact that many futures exchanges no longer have open

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[37]   See CBOE-CBOT JV Approval Order.

[38]   Inter-regulatory spreads subject to that proposal were limited to those comprised of S&P 500 Index options and CBOE 50 futures, and S&P 100 Index options and S&P 250 futures.

[39]   As noted above, if the Exchange determines a different risk offset requirement would be appropriate for a different class of future-option orders, it will submit a rule filing as necessary to implement that requirement.

outcry trading), the Exchange believes this is no longer necessary to permit

future-option orders.[40]

These differences have no impact on the fundamental attributes of the underlying product that

the Commission approved in 1988 and that the Exchange proposes in this filing, which is a

multi-part order comprised of an option and a related future submitted to the Exchange for

pricing as a package, with execution of each component contingent on the other. When

approving the prior proposal, the Commission stated that permitting execution of inter-regulatory

spreads (including for hedging purposes) on the Exchange would "contribute to the mechanism

of a free and open market by enhancing . . . market makers' ability to hedge their positions with

futures [and] enable market makers to better accommodate customer orders and to provide

deeper and tighter markets."[41] The Commission further stated that the proposed rule change was

designed to minimize regulatory concerns, and clarifying the regulatory responsibility for each

leg of an inter-regulatory spread (as the current filing does) would "expedite the enforcement of

each jurisdiction's regulations and foster coordination and cooperation between the jurisdictions

involved."[42] Ultimately, the Commission found that the proposal to execute inter-regulatory

spreads on Cboe to be consistent with the requirements of the Act.[43] While some time has

passed since approving inter-regulatory spreads (the Exchange notes the rules permitted

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[40]   As an example, VX futures trade electronically only on CFE. For similar reasons, the Exchange believes
structuring future-option orders as a joint venture is unnecessary, as the individual components will
continue to trade on the applicable market as proposed. As noted above, the Exchange will be able to share
information with the applicable DCM (through ISG or information sharing agreements) for regulatory
purposes. It is possible the Exchange and the designated contract market may enter into other agreements
as appropriate to permit future-option orders (e.g., to establish electronic connections for purposes of
routing the futures component), but such agreements would have no impact on the proposed rules.

[41]   See CBOE-CBOT JV Approval Order at 46729.

[42]   Id. at 46730.

[43]   Id.

execution of inter-regulatory spreads remained in Cboe's Rulebook until 2005,[44] and the definition of an inter-regulatory spreads remains in Cboe's Rulebook[45]), the Exchange is unaware of any changes to Section 6(b)(5) of the Act since the Commission approved that the trading of inter-regulatory spreads that would prevent the Commission from approving future-option orders at this time.

Further, as discussed above, the proposed rules regarding the handling and execution of future-option orders are also substantially similar to that of stock-option orders,[46] and rules previously filed with the Commission for security-future option orders.[47] The only substantive difference between stock-option orders (and security-future option orders) is that one component of a future-option order (the future leg(s)) is not subject to Commission jurisdiction. The Exchange believes market participants who trade want to trade these strategies because they have determined these strategies are the most appropriate to achieve their investment goals should be able to avail themselves of a more efficient and lower risk execution mechanism for these strategies, even though those strategies happen to include a component subject to jurisdiction of another regulator.

Ultimately, the Exchange believes the proposed rule change will 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 because it will provide investors with a

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[44]   See Securities Exchange Act Release No. 52824 (November 22, 2005), 70 FR 72318 (December 2, 2005) (SR-CBOE-2005-69).

[45]   See Rule 1.1 (definition of inter-regulatory spread).

[46]   See Rules 5.33 (including subparagraphs (f)(1)(B) and (2)(B), paragraph (l), and Interpretation and Policy .04), 5.70(b), 5.83(b), and 5.85 (including subparagraphs (b)(3) through (5) and paragraph (g)).

[47]   See Securities Exchange Act Release No. 49367 (March 5, 2004), 69 FR 11678 (March 11, 2004) (SR-CBOE-2004-14); see also Securities Exchange Act Release Nos. 46390 (August 21, 2002), 67 FR 55290 (August 28, 2002) (SR-ISE-2002-18); and 48894 (December 8, 2003), 68 FR 70328 (December 17, 2003) (SR-PCX-2003-42).

competitive and efficient market mechanism for executing investment strategies comprised of

future-option orders on the Exchange, which will provide a venue for order exposure and price

discovery. These are bona fide investment strategies that reduce market participants' risk and

facilitate hedging. A robust and competitive market requires that exchanges respond to

investors' evolving needs by constantly improving their offerings. When Congress charged the

Commission with supervising the development of a "national market system" for securities,

Congress stated its intent that the "national market system evolve through the interplay of

competitive forces as unnecessary regulatory restrictions are removed.[48] Consistent with this

purpose, Congress and the Commission have repeatedly stated their preference for competition,

rather than regulatory intervention to determine products and services in the securities markets.[49]

This consistent and considered judgment of Congress and the Commission is correct, particularly

in light of evidence of robust competition in the options trading industry. The fact that an

exchange proposed something new is a reason to be receptive, not skeptical — innovation is the

life-blood of a vibrant competitive market — and that is particularly so given the continued

internalization of the securities markets, as exchanges continue to implement new products and

services to compete not only in the United States but throughout the world. Options exchanges

continuously adopt new and different products and trading services in response to industry

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[48]   See H.R. Rep. No. 94-229, at 92 (1975) (Conf. Rep.).

[49]   See S. Rep. No. 94-75, 94th Cong., 1st Sess. 8 (1975) ("The objective [in enacting the 1975 amendments to
         the Exchange Act] would be to enhance competition and to allow economic forces, interacting within a fair
         regulatory field, to arrive at appropriate variations in practices and services."); Order Approving Proposed
         Rule Change Relating to NYSE Arca Data, Securities Exchange Act Release No. 59039 (December 2,
         2008), 73 FR 74770 (December 9, 2008) ("The Exchange Act and its legislative history strongly support
         the Commission's reliance on competition, whenever possible, in meeting its regulatory responsibilities for
         overseeing the [self-regulatory organizations] and the national market system. Indeed, competition among
         multiple markets and market participants trading the same products is the hallmark of the national market
         system."); and Regulation NMS, 70 FR at 37499 (observing that NMS regulation "has been remarkably
         successful in promoting market competition in [the] forms that are most important to investors and listed
         companies").

demands in order to attract order flow and liquidity to increase their trading volume. This competition has led to a growth in investment choices, which ultimately benefits the marketplace and the public. The Exchange believes that the proposed rule change will help further competition by providing market participants with yet another investment option for the listed options market.

        B.   <u>Self-Regulatory Organization's Statement on Burden on Competition</u>

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange does not believe that the proposed rule change will impose any burden on intramarket competition that is not necessary or appropriate in furtherance of the purposes of the Act, because future-option orders will be available to all TPHs and will execute in the same manner. Future-option orders will be available to all users on a voluntary basis, and users will not be required to use future-option orders to execute investment strategies comprised of option and future components. Users may continue to execute these strategies as they do today by entering an option order on the Exchange and separately executing the future component on a designated contract market. For users that elect to use the proposed functionality, the proposed rule change would reduce price and execution risk that currently exists when executing these strategies.

The Exchange does not believe the proposed rule change will impose any burden on intermarket competition that is not necessary or appropriate in furtherance of the purposes of the Act, because other options exchanges may propose similar functionality (and previously have, as noted above). The Exchange understands investors currently execute investment strategies comprised of option and future components today. Investors may continue to do so; however, the proposed rule change merely provides them a simple, efficient, transparent, and competitive

execution mechanism for hedging and other investment strategies that contain options and related futures components.

The Exchange believes the proposed rule change may relieve any burden on, or otherwise promote, competition. The proposed rule change is designed to provide investors with a more efficient and lower risk mechanism to execute investment strategies comprised of futures and options components. The Exchange believes this is an enhancement to executing these investment strategies in a riskier and more complex manner through separate transactions or in the unregulated and opaque OTC market. The proposed rule change would make a more attractive alternative to either of these options by providing investors with the ability to execute these strategies in a single transaction in an exchange environment. This would result in increased market transparency, enhanced efficiency in initiating and closing out positions, and heightened contra-party creditworthiness.

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

The Exchange neither solicited nor received written comments on the proposed rule change.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

A.   by order approve or disapprove such proposed rule change, or

B.   institute proceedings to determine whether the proposed rule change should be 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 (https://www.sec.gov/rules/sro.shtml); or

- Send an email to rule-comments@sec.gov. Please include file number SR-CBOE-2024-042 on the subject line.

Paper Comments:

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

All submissions should refer to file number SR-CBOE-2024-042. 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 website (https://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 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of the filing also will be available for inspection and copying at the principal office

of the Exchange. Do not include personal identifiable information in submissions; you should

submit only information that you wish to make available publicly. We may redact in part or

withhold entirely from publication submitted material that is obscene or subject to copyright

protection. All submissions should refer to file number SR-CBOE-2024-042 and should be

submitted on or before [INSERT DATE 21 DAYS AFTER DATE OF PUBLICATION IN THE

FEDERAL REGISTER].

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

authority.[50]

Vanessa A. Countryman,

Secretary.

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[50]   17 CFR 200.30-3(a)(12).