

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-89016; File No. SR-CboeEDGA-2020-005)

June 4, 2020

Self-Regulatory Organizations; Cboe EDGA Exchange, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to Amend the Rule Relating to MidPoint Discretionary Orders to Allow Optional Offset or Quote Depletion Protection Instructions

I. Introduction

On February 28, 2020, Cboe EDGA Exchange, Inc. (the “Exchange” or “EDGA”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend EDGA Rule 11.8(e), which describes the handling of MidPoint Discretionary Orders entered on the Exchange. The proposed rule change was published for comment in the Federal Register on March 10, 2020.<sup>3</sup> On April 16, 2020, pursuant to Section 19(b)(2) of the Act,<sup>4</sup> the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.<sup>5</sup> On May 20, 2020, the Exchange filed Amendment No. 1 to the proposed rule change, which replaced and superseded the proposed rule change as

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

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

<sup>3</sup> See Securities Exchange Act Release No. 88323 (March 5, 2020), 85 FR 13957.

<sup>4</sup> 15 U.S.C. 78s(b)(2).

<sup>5</sup> See Securities Exchange Act Release No. 88664, 85 FR 22465 (April 22, 2020). The Commission designated June 8, 2020 as the date by which the Commission shall approve or disapprove, or institute proceedings to determine whether to disapprove, the proposed rule change.

originally filed.<sup>6</sup> The Commission received no comment letters on the proposal. The Commission is publishing this notice to solicit comments on Amendment No. 1 from interested persons, and is approving the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

## II. Description of the Proposal, as Modified by Amendment No. 1

A MidPoint Discretionary Order (“MDO”) is a limit order to buy that is pegged to the national best bid (“NBB”), with discretion to execute at prices up to and including the midpoint of the national best bid or offer (“NBBO”), or a limit order to sell that is pegged to the national best offer (“NBO”), with discretion to execute at prices down to and including the midpoint of the NBBO.<sup>7</sup> The Exchange proposes to amend EDGA Rule 11.8(e) to introduce two optional instructions that Users<sup>8</sup> would be able to include on MDOs entered on the Exchange. First, the Exchange would allow Users to enter MDOs with an offset to the NBBO, similar to orders entered with a Primary Peg Instruction today.<sup>9</sup> Second, the Exchange would allow Users to enter MDOs that include a Quote Depletion Protection (“QDP”) instruction that would disable discretion (i.e., the order’s ability to execute at a more aggressive price than its ranked price) for

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<sup>6</sup> In Amendment No. 1, the Exchange revised the proposal to: (1) modify the circumstances that would enable or refresh a QDP active period (see infra note 15); (2) set the QDP active period as 2 milliseconds; (3) include additional justification in support of the proposed rule change, including data in support of the QDP functionality; and (4) make technical and conforming changes. Amendment No. 1 is available at <https://www.sec.gov/comments/sr-cboeedga-2020-005/srcboeedga2020005-7240760-217168.pdf>

<sup>7</sup> See EDGA Rule 11.8(e).

<sup>8</sup> A “User” is any member or sponsored participant who is authorized to obtain access to the Exchange’s trading system. See EDGA Rule 1.5(ee).

<sup>9</sup> See EDGA Rule 11.6(j)(2).

a limited period in certain circumstances where the best bid or offer displayed on the EDGA Book<sup>10</sup> is executed below one round lot.

*Offset Instruction*

As proposed, MDOs entered with an offset would function in the same manner as currently implemented for Primary Peg orders entered with an offset pursuant to Rule 11.6(j)(2). First, a User entering an MDO would be able to select an offset equal to or greater than one minimum price variation (“MPV”) above or below the NBB or NBO to which the order is pegged (“Offset Amount”). Second, the Offset Amount for an MDO that is to be displayed on the EDGA Book would need to result in the price of such order being inferior to or equal to the inside quote on the same side of the market.<sup>11</sup> The offset functionality would be an optional feature that Users could include when entering an MDO for trading on the Exchange.

In addition, the Exchange proposes to make conforming changes to EDGA Rule 11.8(e) to account for the offset functionality. Specifically, the Exchange proposes to amend language in the introductory paragraph to Rule 11.8(e) and subparagraphs (e)(6) and (8).<sup>12</sup> According to the Exchange, these changes reflect the proposed operation of MDOs entered with an offset and would not otherwise impact the handling of MDOs entered on the Exchange.<sup>13</sup>

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<sup>10</sup> The “EDGA Book” is the electronic file of orders for the Exchange’s trading system. See EDGA Rule 1.5(d).

<sup>11</sup> An MDO defaults to a displayed instruction unless the User includes a non-displayed instruction on the order. See EDGA Rule 11.8(e)(4). Similar to the current handling of orders entered with a Primary Peg instruction, the Exchange is not proposing to accept displayed MDOs with an aggressive offset at this time. See Amendment 1, supra note 6, at 5 n.6.

<sup>12</sup> For a detailed description of these proposed changes, see Amendment 1, supra note 6, at 6-7.

<sup>13</sup> See Amendment 1, supra note 6, at 7.

### *Quote Depletion Protection*

The Exchange also proposes to introduce QDP, an optional instruction that Users could enable on an MDO to limit the order's ability to exercise discretion in certain circumstances.<sup>14</sup> The QDP feature would do this by tracking significant executions of orders that constitute the best bid or offer on EDGA.<sup>15</sup> As proposed, a "QDP Active Period" would be enabled or refreshed for buy (sell) MDOs if the best bid (offer) displayed on the EDGA Book is executed below one round lot.<sup>16</sup> When a QDP Active Period is initially enabled, or refreshed by a subsequent execution of the best bid (offer) then displayed on the EDGA Book, it would remain enabled for two milliseconds.<sup>17</sup> During this QDP Active Period, an MDO entered with a QDP instruction would not exercise discretion. Instead, such an order would be only be executable at its ranked price.<sup>18</sup> The ranked price is always executable unless the User cancels the order from the book.

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<sup>14</sup> Proposed changes related to the introduction of the QDP instruction are reflected in proposed subparagraph (10) under EDGA Rule 11.8(e).

<sup>15</sup> The Exchange initially proposed that the QDP Active Period also could be enabled or refreshed in certain circumstances by significant cancellations. Amendment No. 1 removed this aspect of the proposal.

<sup>16</sup> Rule 611 of Regulation NMS generally limits executions to prices that are at or better than the protected best bid or offer. However, there are circumstances, such as the use of intermarket sweep orders, where an order may be executed at an inferior price. In these circumstances, an execution of the EDGA BBO below one round lot would trigger a QDP Active Period even though that quotation is inferior to the NBBO. See Amendment 1, supra note 6, at 8 n.10.

<sup>17</sup> The QDP Active Period would always last for at least two milliseconds. If the QDP Active Period is refreshed by a subsequent execution, such execution would result in a new two millisecond timer being started. Although the MDO would not exercise discretion during the QDP Active Period, its priority would not be impacted, and any applicable priority at its pegged price would be retained when QDP is enabled. See Amendment 1, supra note 6, at 8 n.12.

<sup>18</sup> An MDO's ranked price is the order's displayed or non-displayed pegged price, which may or may not include an offset, as proposed, or the order's limit price if that limit price

Unless the User chooses otherwise, an MDO to buy (sell) entered with a QDP instruction would default to a non-displayed instruction and would include an Offset Amount equal to one MPV below (above) the NBB (NBO).<sup>19</sup>

### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>20</sup> In particular, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with Section 6(b)(5) of the Act,<sup>21</sup> which requires, among other things, that the rules of a national securities exchange be 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, and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

EDGA proposes to introduce optional instructions that (1) would allow Users to enter MDOs with an offset to the NBB or NBO and (2) enter MDOs with a QDP instruction that would disable discretion for 2 milliseconds where the best bid or offer displayed on the EDGA

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is less aggressive than the applicable pegged price. See Amendment 1, supra note 6, at 8 n.11.

<sup>19</sup> The Exchange also proposes to amend EDGA Rule 11.8(e)(4) to reflect the fact that MDOs entered with a QDP instruction would default to non-displayed. MDOs that are not entered with the QDP instruction would continue to default to a displayed instruction, as currently provided in EDGA Rule 11.8(e)(4). See Amendment 1, supra note 6, at 9 n.13.

<sup>20</sup> 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).

<sup>21</sup> 15 U.S.C. 78f(b)(5).

Book is executed below one round lot. The Exchange asserts that similar offset functionality is already available on the Exchange in both the Primary Peg order type and the Discretionary Range instruction. EDGA further believes that the flexibility to specify an offset would be beneficial for market participants that require additional discretion to manage their order flow on the Exchange.

The Exchange states that the QDP instruction is intended to provide Users with a protective feature that limits an order's ability to exercise discretion in certain circumstances that may indicate that the market is moving against the resting MDO.<sup>22</sup> The Exchange provided data for a ten day period that tested the potential performance of the proposed QDP instruction in protecting Users from a potential negative price move by observing market movements in the two milliseconds following instances where QDP would have been enabled due to the execution of the EDGA best bid or offer. The Exchange concluded that the data showed: (1) MDOs entered with a QDP instruction could benefit from avoiding potentially impactful executions within the order's discretionary range when there are impending price moves; and (2) even though the market might remain static after QDP is enabled, the opportunity cost for disabling discretion in those circumstances is small as QDP would only be enabled for a limited period of time during the trading day.

The Commission believes that the QDP feature is reasonably designed to allow market participants who utilize MDOs the opportunity to avoid an unfavorable execution when the market moves against a resting MDO. In reaching this conclusion, the Commission evaluated the proposed rule change and the data provided by the Exchange demonstrating correlation between the operation of the QDP feature and price instability on the EDGA market. In

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<sup>22</sup> See Amendment No. 1, supra note 6, at 17-18.

particular, the data indicates that: (i) there is a reasonable likelihood that the market will move against a resting MDO or remain static during a QDP Active Period; and (ii) a QDP Active Period would be active on average less than a half second per trading day per symbol. In addition, the QDP instruction is designed so that, during the QDP Active Period, only the discretion to execute at a more aggressive price would be suppressed and therefore an MDO, whether displayed or non-displayed, would still be accessible to liquidity takers at its ranked price. Finally, no User would be required to use either of the two proposed order instructions for the MDO (i.e., NBBO offset and QDP); it is optional functionality that would be available to Users who believe it may better effect their trading strategies. Therefore, the Commission believes that providing market participants the ability to use this optional tool to potentially improve the quality of their executions would promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.

The Commission also notes that there is current, existing functionality for discretionary orders that is similar, although not identical, to both the offset and QDP instructions on the Exchange<sup>23</sup> and other national securities exchanges.<sup>24</sup> For the NBBO offset in particular, the Commission notes that the proposed offset instruction is a close variant of the discretion and pegging functionality that the Commission has approved under past exchange proposals.<sup>25</sup> These functionalities continue to exist on the Exchange and on other exchanges.<sup>26</sup>

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<sup>23</sup> See, e.g., EDGA Rule 11.6(j)(2).

<sup>24</sup> See, e.g., IEX Rule 11.190(b)(10), Nasdaq Rule 4703(g).

<sup>25</sup> See, e.g., Securities Exchange Act Release No. 73592 (Nov. 13, 2014), 79 FR 68937 (Nov. 19, 2014).

<sup>26</sup> See, e.g., EDGA Rule 11.6(d); EDGA Rule 11.6(j)(2); Nasdaq Rule 4703(g). The

Accordingly, for the foregoing reasons, the Commission believes that this proposed rule change, as modified by Amendment No. 1, is consistent with the Exchange Act. The Commission believes that the proposed rule change is reasonably designed to promote fair and orderly markets, promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market, and, in general, to protect investors and the public interest.

#### IV. Solicitation of Comments on Amendment No. 1 to the Proposed Rule Change

Interested persons are invited to submit written data, views, and arguments concerning whether Amendment No. 1 is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-CboeEDGA-2020-005 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.

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Commission notes that the Exchange and other exchanges offer order types or instructions that would permit an order with discretion or an order with pegging functionality (or both, in some cases) to rest more passively on the exchange's book (e.g., further away from the NBB or NBO). As noted above, the Exchange offers both a Discretionary Range instruction (which would allow a discretionary order to rest passively) and a Primary Peg instruction (which would allow an order to be pegged one or more MPVs away from the NBB or NBO). Other exchange rules permit a discretionary order to be combined with a pegged order and would allow for a passive offset. See, e.g., Nasdaq Rule 4703(g).



All submissions should refer to File Number SR-CboeEDGA-2020-005. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>).

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change.

Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-CboeEDGA-2020-005, and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1

The Commission finds good cause to approve the proposed rule change, as modified by Amendment No. 1, prior to the thirtieth day after the date of publication of notice of the filing of Amendment No. 1 in the Federal Register. In Amendment No. 1, the Exchange further revised the proposal to: (1) modify the circumstances that would enable or refresh a QDP active period; (2) set the QDP active period as 2 milliseconds; (3) include additional justification in support of the proposed rule change, including data in support of the QDP functionality; and (4) make

technical and conforming changes. The changes and additional information in Amendment No. 1 add additional clarity to the original substance of the proposed rule change. In addition, the content of Amendment No. 1 assists the Commission's determination of whether the proposed rule change is consistent with the Act. Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>27</sup> to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

VI. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>28</sup> that the proposed rule change (SR-CboeEDGA-2020-005), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>29</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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<sup>27</sup> 15 U.S.C. 78s(b)(2).

<sup>28</sup> Id.

<sup>29</sup> 17 CFR 200.30-3(a)(12).