SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-82612; File No. SR-ISE-2017-111)

February 1, 2018

Self-Regulatory Organizations; Nasdaq ISE, LLC; Order Approving a Proposed Rule Change to Establish a Nonstandard Expirations Pilot Program

I. Introduction

On December 21, 2017, Nasdaq ISE, LLC ("ISE" or "Exchange") filed with the Securities and Exchange Commission ("Commission" or "SEC"), 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 establish a Nonstandard Expirations Pilot Program. The proposed rule change was published for comment in the Federal Register on January 12, 2018.[3] The Commission received no comments on the proposed rule change.

This order approves the proposal for a pilot period of twelve months.

II. Description of the Proposal

The Exchange proposes to permit the listing and trading, on a pilot basis, of p.m.-settled options on broad-based indexes with nonstandard expiration dates for a period of twelve months (the "Nonstandard Expirations Pilot Program" or "Pilot Program") from the date of approval of this proposed rule change. The Pilot Program would permit both weekly expirations ("Weekly Expirations") and end of month ("EOM") expirations similar to those of the a.m.-settled broad-based index options, except that the exercise settlement value will be based on the index value derived from the closing prices of component stocks. The proposal is substantially similar to Chicago Board Options Exchange ("CBOE") Rule 24.9(e), Nonstandard Expirations Pilot

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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. 82458 (Jan. 8, 2018), 83 FR 1636.

Program[4] as well as the Nonstandard Expirations Pilot Program of the Exchange's affiliate Nasdaq PHLX LLC ("Phlx") Rule 1101A.[5]

A. Weekly Expirations

The Exchange proposes to add new Supplementary Material .07(a), Weekly Expirations, to Rule 2009. Under the proposed new rule the Exchange would be permitted to open for trading Weekly Expirations on any broad-based index eligible for standard options trading to expire on any Monday, Wednesday, or Friday (other than the third Friday-of-the-month or days that coincide with an EOM expiration). Weekly Expirations would be subject to all provisions of ISE Rule 2009 and would be treated the same as options on the same underlying index that expire on the third Friday of the expiration month. Unlike the standard monthly options, however, Weekly Expirations would be p.m.-settled. New series in Weekly Expirations could be added up to and including on the expiration date for an expiring Weekly Expiration.

The maximum number of expirations that could be listed for each Weekly Expiration (i.e., a Monday expiration, Wednesday expiration, or Friday expiration, as applicable) in a given class would be the same as the maximum number of expirations permitted for standard options on the same broad-based index. Weekly Expirations would not need to be for consecutive Monday, Wednesday, or Friday expirations as applicable. However, the expiration date of a non-

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4 See Securities Exchange Act Release Nos. 78531 (August 10, 2016), 81 FR 54643 (August 16, 2016) (SR-CBOE-2016-046) (Order approving expansion of CBOE's Nonstandard Expirations Pilot Program to include Monday Expirations); 76909 (January 14, 2016), 81 FR 3512 (January 21, 2016) (SR-CBOE-2015-106) (Order approving expansion of CBOE's Nonstandard Expirations Pilot Program to include Wednesday Expirations); 62911 (September 14, 2010), 75 FR 57539 (September 21, 2010) (SR-CBOE-2009-075) (Order approving CBOE's Nonstandard Expirations Pilot Program).

5 See Securities Exchange Act Release No. 82341 (December 15, 2017), 82 FR 60651 (December 21, 2017) (Order approving Phlx's Nonstandard Expirations Pilot Program).

consecutive expiration would not be permitted beyond what would be considered the last expiration date if the maximum number of expirations were listed consecutively.

Weekly Expirations that are first listed in a given class could expire up to four weeks from the actual listing date. If the last trading day of a month were a Monday, Wednesday, or Friday and the Exchange were to list EOMs and Weekly Expirations as applicable in a given class, the Exchange would list an EOM instead of a Weekly Expiration in the given class. Other expirations in the same class would not be counted as part of the maximum number of Weekly Expirations for a broad-based index class. If the Exchange were not open for business on a respective Monday, the normally Monday expiring Weekly Expirations would expire on the following business day. If the Exchange were not open for business on a respective Wednesday or Friday, the normally Wednesday or Friday expiring Weekly Expirations would expire on the previous business day.

B. EOM Expirations

Under the proposal, the Exchange could open for trading EOMs on any broad-based index eligible for standard options trading to expire on the last trading day of the month. EOMs would be subject to all provisions of Rule 2009 and treated the same as options on the same underlying index that expire on the third Friday of the expiration month. However, the EOMs would be p.m.-settled and new series in EOMs could be added up to and including on the expiration date for an expiring EOM.

The maximum number of expirations that could be listed for EOMs in a given class would be the same as the maximum number of expirations permitted for standard options on the same broad-based index. EOM expirations would not need to be for consecutive end of month expirations. However, the expiration date of a non-consecutive expiration may not be beyond what would be considered the last expiration date if the maximum number of expirations were listed consecutively. EOMs that are first listed in a given class could expire up to four weeks from the actual listing date. Other expirations would not be counted as part of the maximum numbers of EOM expirations for a broad-based index class.

C. Contract Terms and Trading Rules

The Exchange proposes that Weekly Expirations and EOMs would be subject to the same rules that currently govern the trading of standard monthly broad-based index options, including sales practice rules, margin requirements, and floor trading procedures. Contract terms for Weekly Expirations and EOMs would be the same as those for standard monthly broad-based index options, except that the exercise settlement value will be based on the index value derived from the closing prices of component stocks. Since Weekly Expirations and EOMs will be a new type of series, and not a new class, the Exchange proposes that Weekly Expirations and EOMs shall be aggregated for any applicable reporting and other requirements.[6] Pursuant to proposed Supplementary Material .07(d) of Rule 2009, transactions in Weekly Expirations and EOMs could be effected on the Exchange between the hours of 9:30 a.m. (Eastern Time) and 4:15 p.m. (Eastern Time).

The Exchange represents that it has analyzed its capacity and believes that it and the Options Price Reporting Authority have the necessary systems capacity to handle any additional

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6 See Rule 2006(a)(13) which sets forth the reporting requirements for certain market indexes that do not have position limits, including NDX. The Exchange is adding Nonstandard Expirations to Rule 2004(d) to reflect the aggregation requirement. The Exchange notes that the proposed aggregation is consistent with the aggregation requirements for other types of option series (e.g. quarterly expiring options) that are listed on the Exchange and which do not expire on the customary “third Friday”.

traffic associated with the listing of the maximum number nonstandard expirations permitted under the Pilot Program.

D. Pilot Program Annual Report

As part of the Pilot Program, the Exchange proposes to submit a Pilot Program report to the Commission at least two months prior to the expiration date of the Pilot Program (the "annual report"). The annual report will contain an analysis of volume, open interest and trading patterns. In addition, for series that exceed certain minimum open interest parameters, the annual report will provide analysis of index price volatility and, if needed, share trading activity. The annual report will be provided to the Commission on a confidential basis.

Analysis of Volume and Open Interest

For all Weekly Expirations and EOM series, the annual report will contain the following volume and open interest data for each broad-based index overlying Weekly Expiration and EOM options:

(1) Monthly volume aggregated for all Weekly Expiration and EOM series,

(2) Volume in Weekly Expiration and EOM series aggregated by expiration date,

(3) Month-end open interest aggregated for all Weekly Expiration and EOM series,

(4) Month-end open interest for EOM series aggregated by expiration date and open interest for Weekly Expiration series aggregated by expiration date,

(5) Ratio of monthly aggregate volume in Weekly Expiration and EOM series to total monthly class volume, and

(6) Ratio of month-end open interest in EOM series to total month-end class open interest and ratio of open interest in each Weekly Expiration series to total class open

interest.

In addition, the annual report will contain the information noted above for standard Expiration Friday, a.m.-settled series, if applicable, for the period covered in the annual report as well as for the six-month period prior to the initiation of the Pilot Program.

Upon request by the SEC, the Exchange will provide a data file containing: (1) Weekly Expiration and EOM option volume data aggregated by series, and (2) Weekly Expiration open interest for each expiring series and EOM month-end open interest for expiring series.

Monthly Analysis of Weekly Expiration and EOM Trading Patterns

In the annual report, the Exchange also proposes to identify Weekly Expiration and EOM trading patterns by undertaking a time series analysis of open interest in Weekly Expiration and EOM series aggregated by expiration date compared to open interest in near-term standard Expiration Friday a.m.-settled series in order to determine whether users are shifting positions from standard series to Weekly Expiration and EOM series. In addition, to the extent that data on other weekly or monthly p.m. settled products from other exchanges is publicly available, the annual report will also compare open interest with these options in order to determine whether users are shifting positions from other weekly or monthly p.m.-settled products to the Weekly Expiration and EOM series. Declining open interest in standard series or the weekly or monthly p.m.-settled products of other exchanges accompanied by rising open interest in Weekly Expiration and EOM series would suggest that users are shifting positions.

Provisional Analysis of Index Price Volatility and Share Trading Activity

For each Weekly Expiration and EOM expiration that has open interest that exceeds certain minimum thresholds, the annual report will contain the following analysis related to index price changes and, if needed, underlying share trading volume at the close on expiration dates:

(1) a comparison of index price changes at the close of trading on a given expiration date with comparable price changes from a control sample. The data will include a calculation of percentage price changes for various time intervals and compare that information to the respective control sample. Raw percentage price change data as well as percentage price change data normalized for prevailing market volatility, as measured by an appropriate index agreed by the Commission and the Exchange, will be provided; and

(2) if needed, a calculation of share volume for a sample set of the component securities representing an upper limit on share trading that could be attributable to expiring in-the-money Weekly Expiration and EOM expirations. The data, if needed, will include a comparison of the calculated share volume for securities in the sample set to the average daily trading volumes of those securities over a sample period.

The minimum open interest parameters, control sample, time intervals, method for selecting the component securities, and sample periods will be determined by the Exchange and the Commission.

III. Discussion and Commission's Findings

After careful review of the proposed rule change, the Commission finds that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange.[7] Specifically, the Commission finds that the

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

proposed rule change is consistent with Section 6(b)(5) of the Act,[8] 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 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 to protect investors and the public interest.

While the Commission has had concerns about the adverse effects and impact of p.m.-settlement upon market volatility and the operation of fair and orderly markets on the underlying cash market at or near the close of trading, it has approved on a limited basis p.m.-settlement for cash-settled options.[9] More specifically, the Commission approved on a pilot basis CBOE's nearly identical and Phlx's identical Nonstandard Expirations Pilot Programs.[10]

Like Phlx, the Exchange patterns its proposal after CBOE's and includes the same additional data element that Phlx includes in the annual report: an analysis of publically available data concerning trading patterns with respect to other p.m.-settled products from other exchanges. In all other aspects, the Exchange's proposed and Phlx's and CBOE's existing

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8 15 U.S.C. 78f(b)(5).

9 See, e.g., Securities Exchange Act Release Nos. 31800 (February 1, 1993), 58 FR 7274 (February 5, 1993) (SR-CBOE-92-13) (Order approving CBOE's listing of p.m.-settled, cash-settled options on certain broad-based indexes); 61439 (January 28, 2010), 75 FR 5831 (February 4, 2010) (SR-CBOE-2009-087) (Order approving CBOE's listing of p.m.-settled FLEX options on a pilot basis); 70087 (July 31, 2013), 78 FR 47809 (August 6, 2013) (SR-CBOE- 2013-055) (Order approving the addition of p.m.-settled mini-SPX index options to the SPXPM Pilot for p.m.-settled SPX index options); 81293 (August 2, 2017), 82 FR 37138 (August 8, 2017) (SR-Phlx-2017-04) (Order approving Phlx to list and trade of p.m.-Settled NASDAQ-100 Index(R) Options on a Pilot Basis).

10 See supra notes 4-5.

Nonstandard Expirations Pilot Programs are identical.

The Commission believes that the Exchange's proposal strikes a reasonable balance between the Exchange's desire to offer a wider array of investment opportunities and the need to avoid unnecessary proliferation of options series that may burden certain liquidity providers and further stress options quotation and transaction infrastructure. The Exchange's proposed twelve-month Pilot Program will allow for both the Exchange and the Commission to continue monitoring the potential for adverse market effects of p.m.-settlement on the market, including the underlying cash equities markets, at the expiration of these options.

The Commission notes that the Exchange will provide the Commission with the annual report analyzing volume and open interest of EOMs and Weekly Expirations that will also contain information and analysis of EOMs and Weekly Expirations trading patterns and index price volatility and share trading activity for series that exceed minimum parameters. This information should be useful to the Commission as it evaluates whether allowing p.m.-settlement for EOMs and Weekly Expirations has resulted in increased market and price volatility in the underlying component stocks, particularly at expiration. The Pilot Program information should help the Commission and the Exchange assess the impact on the markets and determine whether changes to these programs are necessary or appropriate. Furthermore, the Exchange's ongoing analysis of the Pilot Program should help it monitor any potential risks from large p.m.-settled positions and take appropriate action, if warranted.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[11] that the proposed rule change (SR-ISE-2017-111) be approved for a pilot period of twelve months.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[12]

Eduardo A. Aleman
Assistant Secretary

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11 15 U.S.C. 78s(b)(2).

12 17 CFR 200.30-3(a)(12).