

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72957; File No. SR-CBOE-2014-015]

### Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change Relating to Complex Orders

September 2, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on August 19, 2014, Chicago Board Options Exchange, Incorporated (the "Exchange" or "CBOE") filed with the Securities and Exchange Commission (the "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

The Exchange proposes to amend its rules related to complex orders. The text of the proposed rule change is available on the Exchange's Web site (<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 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. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

The Exchange proposes to amend its rules related to complex orders to: (i) Simplify the definitions of the complex

order types that may be made available on a class-by-class basis and remove references to certain specific complex order types that will no longer be defined; (ii) with respect to complex orders in open outcry, set forth applicable ratios and order ticket requirements for an order to be eligible for complex order priority within applicable priority rules; and (iii) with respect to complex orders in open outcry, make explicit the priority applicable when there are other complex orders or quotes represented at the same net price, whether such other orders or quotes are in the complex order book ("COB") or being represented in open outcry.

First, with respect to definitions, the Exchange proposes to amend Rule 6.53 to remove the definitions of spread order, combination order, straddle order and ratio order and replace them with a more general definition of a complex order (which includes a stock-option order and a security future-option order) to simplify the descriptions of the complex order types that may be made available on a class-by-class basis. The proposed definition of a "complex order" is any order for the same account as defined below:

- A "complex order" is any order involving the execution of two or more different options series in the same underlying security occurring at or near the same time within an applicable ratio that may be determined by the Exchange and for the purpose of executing a particular investment strategy.

- A "stock-option order" is proposed to be defined as an order to buy or sell a stated number of units of an underlying stock or a security convertible into the underlying stock ("convertible security") coupled with either (a) the purchase or sale of options contract(s) on the opposite side of the market representing either (i) the same number of units of the underlying stock or convertible security, or (ii) the number of units of the underlying stock necessary to create a delta neutral position, but in no case in a ratio greater than an applicable ratio that may be determined by the Exchange (where the ratio represents the total number of units of the underlying stock or convertible security in the option leg to the total number of units of the underlying stock or convertible security in the stock leg) or (b) the purchase or sale of an equal number of put and call option contracts, each having the same exercise price, expiration date and each representing the same number of units of stock as, and on the opposite side of the market from, the underlying stock or

convertible security portion of the order.<sup>3</sup>

- The proposed rule change moves the definition of a "security future-option order" from Rule 1.1(zz) to Rule 6.53 so that all definitions of the various types of complex orders are located in the same place within the rules.<sup>4</sup> This proposed complex order definition is in part modeled after the definition of a complex order (including a stock-option order) already contained in Rule 6.53C(a). The Exchange proposes conforming changes to Rules 6.9 (including Interpretation and Policy .03), 6.42, Interpretation and Policy .01, 6.45(e), 6.45A(b)(ii), 6.45B(b)(ii), 6.48(b), 6.73(c), 6.74(d)(iii) and 8.51 to harmonize these rules with the proposed changes in Rule 6.53 to consistently reference the proposed new

<sup>3</sup> Rule 1.1(ii) currently 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 (i) 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 (ii) the purchase or sale of an equal number of put and call option contracts, each having the same exercise price, 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 proposed rule change deletes this definition and references the proposed definition in Rule 6.53 to eliminate the confusion of having two separate definitions. The current definition and proposed definition are substantially similar. However, the Exchange believes the language in the proposed definition is more consistent with the language in other rules, including Rules 6.53C (related to electronic handling of complex orders) and 6.80 (related to order protection, which relates to the Options Order Protection and Locked/Crossed Markets Plan, also commonly referred to as the Options Distributive Linkage Plan).

<sup>4</sup> Rule 1.1(zz) defines a "security future-option order," which is deemed a type of Inter-regulatory Spread Order as that term is defined in Rule 1.1(ll), as an order to buy or sell a stated number of units of a security future or a related security convertible into a security future ("convertible security future") coupled with either (i) the purchase or sale of option contract(s) on the opposite side of the market representing either the same number of the underlying for the security future or convertible security future or the number of units of the underlying for the security future or convertible security future necessary to create a delta neutral position or (ii) the purchase or sale of an equal number of put and call option contracts, each having the same exercise price, expiration date and each representing the same number of the underlying for the security future or convertible security future, as and on the opposite side of the market from, the underlying for the security future or convertible security future portion of the order. Rule 1.1(ll) 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 deletes the definition in Rule 1.1(zz) and references the definition in the proposed new location in Rule 6.53.

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

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

definition of a complex order.<sup>5</sup> As a result of the proposed changes to Rule 6.53, the Exchange proposes to update related cross-references in Rules 6.53, 6.53C, Interpretation and Policy .08, 6.74(d)(iii), 7.12(b)(i)(E), 24.A.5 and 24B.5.<sup>6</sup> The Exchange notes that the “applicable ratios” referenced above that may be determined by the Exchange are or are proposed to be further described in various other Exchange Rules (e.g., Rule 6.53C with respect to electronic trading and Rules 6.45, 6.45A and 6.45B with respect to open outcry trading (proposed changes discussed below)).

Second, with respect to complex orders represented and executed in open outcry, the Exchange is proposing to amend Rules 6.45 (pertaining to the priority of bids and offers and allocation of trades in non-CBOE Hybrid System classes), 6.45A (pertaining to the priority of bids and offers and allocation of trades in equity options traded on the CBOE Hybrid System) and 6.45B (pertaining to the priority of bids and offers and allocation of trades in index and ETF options traded on the CBOE Hybrid System).<sup>7</sup> The proposed changes set forth applicable ratios and order ticket requirements for complex orders to be eligible for complex order priority when represented and executed in open outcry.<sup>8</sup> Currently, Exchange and/or

TPH system limitations may prevent a multi-part order with more than a certain number of legs from being entered on a single order ticket for representation and execution in open outcry as a complex order. For example, orders entered via the Exchange-sponsored PULSe workstation and Floor Broker Workstation (“FBW”) are currently limited to four legs. As a result, complex orders with more than the applicable leg limitation that are represented in open outcry must be split up and entered on multiple order tickets.

For consistency in processing and in order to enhance the Exchange’s audit trail, the Exchange proposes to amend Rules 6.45(e), 6.45A(b)(ii) and 6.45B(b)(ii) to require that, to be eligible for open outcry complex order priority, a complex order (as proposed to be defined in Rule 6.53 and as discussed above) must be within the applicable ratio (discussed below) and must be for either:

- Twelve (12) legs or less (one leg of which may be for an underlying security or security future, as applicable) and entered on a single order ticket at time of systemization; or
- more than twelve (12) legs (one leg of which may be for an underlying security or security future, as applicable) and split across multiple order tickets<sup>9</sup> if the Trading Permit Holder (“TPH”) representing the complex order identifies for the Exchange the order tickets that are part of the same complex order (in a form and manner prescribed by the Exchange). The Exchange will announce

COA. Under the same provisions, the Exchange may determine on a class-by-class basis within certain parameters the applicable ratio of a complex order or stock-option order that is eligible for processing via COB and COA. Currently, the Exchange has limited COB and COA to orders of no more than four (4) legs and ratios equal to or greater than one-to-three (.333) and less than or equal to three-to-one (3.00) (and, for stock-option orders, ratios no greater than eight-to-one (8.00)). Under this current structure, orders with more than four (4) legs or that do not satisfy the ratio requirements are not eligible for electronic processing via COB or COA, but would instead be routed for handling in open outcry. The proposed rule change adds language to the introductory paragraph of Rule 6.53C(a) to explicitly state that the definitions of complex orders contained in that rule apply only for purposes of the electronic handling of complex orders pursuant to that rule, notwithstanding the proposed broader definition of complex order contained in Rule 6.53. Because there are two separate definitions of complex orders, the Exchange believes this additional language will bring clarity to the rules about when the definition of complex orders in Rule 6.53C(a) applies, which is in the context of electronic trading.

<sup>9</sup>The Exchange notes that it is not imposing requirements on how a complex order with more than 12 legs should be split across multiple tickets, other than the requirement discussed above that each ticket identify the other applicable tickets.

by Regulatory Circular whether it permits complex orders with more than 12 legs and, if so permitted, the form and manner in which the TPH must link the multiple order tickets.

As discussed above, complex orders represented in open outcry must be within an applicable ratio to be eligible for complex order priority. The proposed rule change amends Rules 6.45(e), 6.45A(b)(ii) and 6.45B(b)(ii) to set forth this applicable ratio. The Exchange proposes that the applicable ratio be as follows:

- For a complex order involving two or more different options series, any ratio that is equal to or greater than one-to-three (.333) and less than or equal to three-to-one (3.00);
- for a stock-option order, the options leg(s) must (i) represent the same number of units of the underlying stock or convertible security in the stock leg, or (ii) represent the number of units of the underlying stock or convertible security necessary to create a delta neutral position, but in no case in a ratio greater than eight-to-one (8.00), where the ratio represents the total number of units of the underlying stock or convertible security in the options leg to the total number of units of stock or convertible security in the stock leg; and
- for a security futures-option order, the options leg(s) must (i) represent the same number of units of the underlying stock in the security future leg, or (ii) represent the number of units of the underlying stock necessary to create a delta neutral position, but in no case in a ratio greater than eight-to-one (8.00), where the ratio represents the total number of units of the underlying stock in the options leg to the total number of units of stock or convertible security in the security-futures leg.

The proposed rule change also adds to the respective rules that, for the purpose of applying the aforementioned ratios to complex orders comprised of both mini-option contracts and standard option contracts, ten (10) mini-option contracts will represent one (1) standard option contract.

The Exchange notes that TPHs may represent in open outcry a complex order with any number of legs and in any ratio. However, if a complex order does not satisfy the applicable number of legs, order ticket and ratio requirements as set forth above, then it will not be eligible for the complex order priority set forth in Rules 6.45(e), 6.45A(b)(ii) or 6.45B(b)(ii).<sup>10</sup> The

<sup>10</sup>Similarly, a complex order submitted for electronic handling must satisfy the ratio and leg requirements set forth in Rule 6.53C(a) to receive

<sup>5</sup> The proposed rule change also deletes the paragraph lettering from the order type definitions and puts the order types in alphabetical order, which the Exchange believes will allow investors to more easily locate the order type definitions within the rules. Other than proposed changes to the definition of complex orders as described above, the proposed rule change makes no substantive changes to the order type definitions.

<sup>6</sup> In addition, cross-references in Rules 6.45, 6.45A and 6.45B to “[s]tock-option orders and security future-option orders, as defined in Rules 1.1(ii)(a) and Rule 1.1(zz)(a), respectively” are proposed to be replaced with the phrase “[s]tock-option orders and security future-option orders that include only one option series leg.”

<sup>7</sup> Under those rules, a complex order may be executed at a net debit or credit price with another TPH without giving priority to equivalent bids (offers) in the individual series legs that are represented in the trading crowd or in the public customer limit order book provided at least one leg of the order betters the corresponding bid (offer) in the public customer limit order book by at least one minimum trading increment as defined in Rule 6.42 (i.e., \$0.10, \$0.05 or \$0.01, as applicable) or \$0.01, which increment is determined by the Exchange on a class-by-class basis. Stock-option orders and security future-option orders have priority over bids (offers) of the trading crowd but not over bids (offers) in the public customer limit order book.

<sup>8</sup> To be eligible for electronic processing via the CBOE Hybrid System’s COB and complex order RFR auction (“COA”), the system already requires that a complex order be entered on a single order ticket to be electronically processed. Under existing Rule 6.53C(a)(1) and (2), the Exchange may determine on a class-by-class basis the applicable number of legs of a complex order or stock-option order that is eligible for processing via COB and

Exchange also notes that it does not propose to amend how complex orders are allocated or the priority afforded to complex orders in open outcry; it is merely modifying the requirements for a complex order to be eligible for the open outcry complex order priority.

With respect to the order ticket requirements, the Exchange also proposes to add to Rule 24.20 (pertaining to SPX Combo Orders) Interpretation and Policy .01 to require that an SPX Combo Order<sup>11</sup> for twelve (12) legs or less be entered on a single order ticket at time of systemization. An SPX Combo Order that contains more than twelve (12) legs may be represented and executed as a single SPX Combo Order in accordance with Rule 24.20 if it is split across multiple order tickets and the TPH representing the SPX Combo Order identifies for the Exchange the order tickets that are part of the same SPX Combo Order (in a manner and form prescribed by the Exchange). The Exchange will announce by Regulatory Circular whether it permits SPX Combo Orders with more than 12 legs and, if so permitted, the form and manner in which the TPH must link the multiple order tickets. The Exchange notes that a TPH may submit an order that does not satisfy these ticket requirements, but such order may not be represented or executed as a single SPX Combo Order in accordance with Rule 24.20. The Exchange also notes that Rules 24.20 already specifies an applicable ratio (defined by the delta as noted above), and it is proposing no changes to the ratio through this rule filing.

Third, with respect to complex orders in classes where the COB is available, the Exchange also proposes to make explicit the open outcry priority applicable when there are other complex orders or quotes represented at the same net price, whether such other orders or quotes are in the COB or being represented in open outcry. Specifically, the Exchange proposes to amend Rules 6.45A and 6.45B<sup>12</sup> to provide that if a

the complex order priority set forth in that rule (which requires at least one leg of the complex order to better the corresponding bid (offer) in the leg series by at least one minimum increment or \$0.01, as applicable.

<sup>11</sup> An "SPX Combo Order" consists of an order to purchase or sell one or more SPX option series and the offsetting number of SPX combinations defined by the delta, where an "SPX combination" is a purchase (sale) of an SPX call and sale (purchase) of an SPX put having the same expiration date and strike price and a "delta" is the positive (negative) number of SPX combinations that must be sold (bought) to establish a market neutral hedge with one or more SPX option series.

<sup>12</sup> The Exchange may determine to make the COB available on a class-by-class basis for products trading on the CBOE Hybrid System platform.

complex order would trade in open outcry at the same net debit or credit price as another complex order, priority would go first to public customer orders in COB (with multiple public customer orders ranked based on time), then to complex order bids and offers represented in the trading crowd (with multiple bids and offers ranked in accordance with the allocation principles applicable to in-crowd market participants contained in Rule 6.45A(b)(i)(B) and (D), and Rule 6.45B(b)(i)(B) and (D), respectively), and then to all other orders and quotes in the COB (with multiple bids and offers ranked in accordance with the allocation algorithm in effect pursuant to Rule 6.53C).<sup>13</sup> This methodology for prioritizing multiple complex orders for open outcry trading is consistent with the methodology applicable for prioritizing multiple simple orders for open outcry trading and how the Exchange has interpreted and applied complex order priority.<sup>14</sup> The Exchange is merely proposing to reflect this existing interpretation within its rule text for added clarity. The Exchange is proposing no changes to the existing prioritization methodology.

Finally, the proposed rule change makes other non-substantive, technical changes to Rules 6.45A, 6.45B, 6.53, 6.53C, 24A.5 and 24B.5, including deleting extra spaces, adding spaces where necessary, correction of typos and revising rule headings to be consistent with other headings.

The Exchange anticipates that TPHs may desire to make enhancements to their open outcry order management

Because the COB functionality is not available for non-CBOE Hybrid System classes, corresponding changes are not necessary for Rule 6.45(e).

<sup>13</sup> The Exchange notes that, for purposes of this provision, Voluntary Professionals and Professionals, as defined in Rules 1.1(ff) and (ggg), respectively, are treated in the same manner as a broker-dealer in classes where the Voluntary Professional and Professional designations are available.

<sup>14</sup> The Exchange notes that the provisions of Rule 6.45A(b)(i)(D) and 6.45B(b)(i)(D), respectively, applicable to TPHs relying on Section 11(a)(1)(D) of the Securities Exchange Act of 1934 (the "Act") and Rule 11a1-1(T) thereunder (commonly known as the "G" exemption rule") would apply to complex orders in the same manner as it applies to simple orders. Those rules provisions provide that in open outcry, any TPH relying on the G exemption rule as an exemption must yield priority to any bid (offer) at the same price of public customer orders and broker-dealer orders resting in the electronic book, as well as any other bids and offers that have priority over such broker-dealer orders under those rules. Under these provisions, a TPH relying on the G exemption rule would yield priority to simple public customer orders and broker-dealer orders resting in the book and complex public customer orders and broker-dealer orders resting in the COB, as well as any other simple and complex bids and offers that have priority over such broker-dealer orders under those rules.

and execution systems to address the ticket requirements for a multi-legged order to be eligible for priority when represented and executed in open outcry.<sup>15</sup> Therefore, upon approval of this rule change filing, the Exchange will announce the implementation date of the proposed rule change in a Regulatory Circular to be published no later than 90 days following the approval date. The implementation date will be no later than 180 days following the approval date.

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.<sup>16</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>17</sup> requirements 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)<sup>18</sup> requirement that the rules of an exchange not be designed

<sup>15</sup> The Exchange notes that it intends to enhance the Exchange-sponsored PULSe workstation and FBW to support the entry of complex orders with up to twelve (12) legs on a single order ticket. The Exchange notes that TPHs will not be required to make changes to their own or third-party vendor's order entry and execution systems. However, to the extent a TPH wants to represent and execute a multi-part order in open outcry as a complex order, the order must be entered on a single order ticket and cannot exceed twelve (12) legs (or, if the Exchange has determined to make it available, an order for more than twelve (12) legs that is entered on multiple order tickets, which tickets are linked in a form and manner prescribed by the Exchange). For example, if a TPH's order entry and execution system currently only supports the open outcry processing of a complex order with up to four (4) legs, the system would not need to be enhanced if the TPH does not intend to represent and execute complex orders with more than four (4) legs. If the TPH intends to represent and execute complex orders with more than four (4) legs (*i.e.*, complex orders with five (5) to twelve (12) legs), then the TPH may need to enhance its existing system or utilize another order entry and execution system that supports the open outcry processing of such orders on a single order ticket.

<sup>16</sup> 15 U.S.C. 78f(b).

<sup>17</sup> 15 U.S.C. 78f(b)(5).

<sup>18</sup> *Id.*

to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes that (1) removing the definitions of spread order, combination order, straddle order and ratio order from Rule 6.53 and incorporating the more general definition of a complex order (including a stock-option order (and the elimination of a redundant definition of stock-option order) and a security future-option order) into the Rule and (2) harmonizing rules that reference such definitions simplifies and provides more clarity and uniformity to the rules, which ultimately benefits investors. The Exchange believes the proposed nonsubstantive changes to the rules, include the alphabetization of the order type definitions, further benefits investors, as they improve the readability of and further simplify the rules.

Additionally, the Exchange believes the proposed rule change to limit the eligibility of orders represented and executed in open outcry for complex order priority to orders that satisfy the order ticket and applicable ratio requirements will enhance the Exchange's audit trail. An enhanced audit trail promotes transparency and aids in surveillance, thereby protecting investors. In addition, making explicit the open outcry priority applicable when there are other complex orders or quotes represented at the same net price, whether such other orders or quotes are in the COB or being represented in open outcry, provides added clarity to the rule text in a manner that is consistent with the existing methodology applicable for prioritizing multiple simple orders for open outcry trading and how the Exchange has interpreted and applied complex order priority.

The Exchange notes that TPHs may continue to represent and execute in open outcry a complex order with any number of legs and in any ratio. However, if a complex order does not satisfy the applicable ratio and order ticket requirements as set forth above, then it will not be eligible for the complex order priority set forth in Rules 6.45(e), 6.45A(b)(ii) or 6.45B(b)(ii) (as proposed). The Exchange also notes that it does not propose to amend how complex orders are allocated or the priority afforded to complex orders in open outcry; it is merely modifying the requirements for a complex order to be eligible for the existing open outcry complex order priority (which the Exchange is not proposing to change). The Exchange believes the proposed changes will increase opportunities for execution of complex orders and lead to

tighter spreads on CBOE, which will benefit investors. The Exchange also believes that the proposed rule change is designed to not permit unfair discrimination among market participants, as all market participants may trade complex orders, and the priority eligibility requirements apply to complex orders of all market participants.

In addition, the Exchange believes the proposed rule change is consistent with Section 6(b)(1) of the Act,<sup>19</sup> which provides that the Exchange be organized and have the capacity to be able to carry out the purposes of the Act and to enforce compliance by the Exchange's TPHs (and persons associated with its TPHs) with the Act, the rules and regulations thereunder and the rules of the Exchange. Enhancing the audit trail with respect to open outcry complex order processing will further improve the Exchange's ability to better enforce compliance by the Exchange's TPHs (and persons associated with its TPHs) with the Act, the rules and regulations thereunder and the rules of the Exchange.

The Exchange also believes the proposed rule change furthers the objectives of Section 6(c)(3) of the Act, which authorizes the Exchange to, among other things, prescribe standards of operational capability for its TPHs. The Exchange believes the provisions imposing order ticket requirements in order for a complex order to be eligible for complex order priority is reasonable and sets forth appropriate system requirements for supporting complex order processing for open outcry trades.

#### *B. Self-Regulatory Organization's Statement on Burden on Competition*

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 believes that simplifying its rules related to complex orders promotes fair and orderly markets, as well as assists the Exchange in its ability to effectively attract order flow and liquidity to its market, and ultimately benefits all TPHs and all investors. Complex orders are available to all TPHs (and all non-TPH market participants through TPHs), and the proposed rule change, including the complex order priority eligibility requirements, apply to all complex orders in the same manner.

#### *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 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 (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-CBOE-2014-015 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-2014-015. 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 Web site (<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

<sup>19</sup> 15 U.S.C. 78f(b)(1).

public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site 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; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-CBOE-2014-015 and should be submitted on or before September 29, 2014.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>20</sup>

**Kevin M. O'Neill,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-72959; File No. SR-CME-2014-28]

### Self-Regulatory Organizations; Chicago Mercantile Exchange Inc.; Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 2 Thereto, Related to Enhancements to Its Risk Model for Credit Default Swaps

September 2, 2014.

Pursuant to the Section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act" or "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 2, 2014, Chicago Mercantile Exchange Inc. ("CME") filed with the Securities and Exchange Commission ("Commission") Amendment No. 2 to its previously submitted proposed rule change related to proposed enhancements to its risk model for broad-based index credit default swap ("CDS") products.<sup>3</sup> Amendment No. 2 is intended to describe CME's proposed CDS specific risk model framework applicable only to broad-based index CDS and also provide further description and detail of certain

aspects of the proposed rule change as described in Items I, II and III below, which Items have been prepared primarily by CME (the "CDS Risk Model Filing Amendment").<sup>4</sup> The Commission is publishing this notice to solicit comments on the CDS Risk Model Filing Amendment from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

On August 8, 2014, CME submitted to the Commission the CDS Risk Model Filing pursuant to which CME proposes to enhance its risk model for CDS (the "CDS Risk Model" and such enhanced model, the "Proposed CDS Risk Model") to enable CME to offer clearing of additional CDS instruments.<sup>5</sup> The CDS Risk Model Filing is currently pending regulatory approval by the Commission. The purpose of the CDS Risk Model Filing Amendment is to propose the adoption of a CDS specific risk model framework applicable only to broad-based index CDS (the "CME CDS Risk Model Framework") and also provide further description and detail of certain aspects of the Proposed CDS Risk Model contained within the CDS Risk Model Filing. The CDS Risk Model Filing Amendment should be read in conjunction with the CDS Risk Model Filing. All capitalized terms not defined herein shall have the meaning given to them in the CDS Risk Model Filing.

The text of the proposed amendment is also available at the CME's Web site at <http://www.cmegroup.com>, at the principal office of CME, and at the Commission's Public Reference Room.

#### II. Self-Regulatory Organizations Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, CME included statements concerning the purpose and basis for the proposed amendment and discussed any comments it received on the proposed amendment. The text of these statements may be examined at the places specified in Item IV below. CME has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

#### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

##### (1) Purpose

Pursuant to this CDS Risk Model Filing Amendment, CME proposes to adopt a CME CDS Risk Model Framework for broad-based index CDS and also intends to provide further description and detail of certain aspects of the Proposed CDS Risk Model described in the CDS Risk Model Filing as further discussed below. CME also proposes to make changes to the Manual of Operations for CME Cleared Credit Default Swaps (the "CDS Manual") in connection with the proposed CME CDS Risk Model Framework.

##### 1. CME CDS Risk Model Framework

In connection with the adoption of the Proposed CDS Risk Model, CME also proposes to adopt the CME CDS Risk Model Framework. The proposed CME CDS Risk Model Framework would apply only to broad-based index CDS products cleared by CME and would not apply to security-based swaps. CME will file a proposed rule change with the SEC in the future to implement any proposed CDS risk model applicable to the clearing of security-based swaps. The proposed CME CDS Risk Model Framework contains the details of the Proposed CDS Risk Model and existing policies relating to governance, back testing and stress testing for CDS products.

##### 1.1 Governance

The proposed CME CDS Risk Model Framework would be governed by the CDS Risk Committee, the Stress Testing Committee and senior risk management of CME. CDS Risk Committee approval is required for all material changes to the CDS Risk Model Framework, CDS stress testing framework, and CDS back-testing framework. Any changes to the parameters of the CDS Margin Model or CDS stress tests are approved by the Stress Testing Committee or a senior member of the Stress Testing Committee.

##### 1.2 CDS Risk Model Framework for Cleared CDS

The proposed CME CDS Risk Model Framework includes CME's proposed enhancements to the CDS Risk Model for CDS as set forth in the CDS Risk Model Filing. In addition, CME notes that the Post Credit Risk Requirement within the Proposed CDS Risk Model is the same as the post-default charge in the current CDS Risk Model, but also applies to additional credit events such

<sup>20</sup> 17 CFR 200.30-3(a)(12).

<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. 34-72834 (Aug. 13, 2014), 79 FR 48805 (Aug. 18, 2014) (SR-CME-2014-28) (hereinafter referred to as the "CDS Risk Model Filing").

<sup>4</sup> On August 18, 2014, CME filed Amendment No. 1 to the proposed rule change. CME withdrew Amendment No. 1 on August 29, 2014.

<sup>5</sup> See *supra* note 3.