

TPHs on all their transactions that clear in the customer range at the OCC.

The Exchange believes the proposal to eliminate obsolete language with respect to past ORF rates maintains clarity in the rules and alleviates potential confusion, thereby protecting investors and the public interest.

#### *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 not necessary or appropriate in furtherance of the purposes of the Act. This proposal does not create an unnecessary or inappropriate intra-market burden on competition because the ORF applies to all customer activity, thereby raising regulatory revenue to offset regulatory expenses. It also supplements the regulatory revenue derived from non-customer activity. This proposal does not create an unnecessary or inappropriate inter-market burden on competition because it is a regulatory fee that supports regulation in furtherance of the purposes of the Act. The Exchange is obligated to ensure that the amount of regulatory revenue collected from the ORF, in combination with its other regulatory fees and fines, does not exceed regulatory costs.

#### *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**

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>9</sup> and paragraph (f) of Rule 19b-4<sup>10</sup> thereunder. At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission will institute proceedings to determine whether the proposed rule change should be approved or 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 No. SR-C2-2018-017 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 No. SR-C2-2018-017. 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 (<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 No. SR-C2-2018-017, and should be submitted on or before September 13, 2018.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>11</sup>

**Eduardo A. Aleman,**  
*Assistant Secretary.*

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### **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-83870; File No. SR-CBOE-2018-056]

#### **Self-Regulatory Organizations; Cboe Exchange, Inc.; Notice of Filing of a Proposed Rule Change To Adopt Exchange Rule 6.57, Risk-Weighted Assets ("RWA") Transactions**

August 17, 2018.

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 8, 2018, Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") 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 to adopt Rule 6.57 to facilitate the reduction of SPX options positions maintained by Cboe Options Market-Makers.

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 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

<sup>9</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>10</sup> 17 CFR 240.19b-4(f).

<sup>11</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.

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 adopt Rule 6.57 to facilitate the reduction of SPX options positions maintained by Cboe Options Market-Makers. Specifically, the Exchange proposes to allow Trading Permit Holders ("TPHs") to execute a risk-weighted asset package ("RWA Package") on the trading floor provided that the requirements set forth in Rule 6.57 are satisfied.

Market-Makers are the primary source of liquidity for listed options; as such, Market-Maker liquidity is critically important to a functioning options market. However, bank capital regulations that govern bank-affiliated clearing firms are negatively impacting the ability of Market-Makers clearing through bank-affiliated clearing firms to provide liquidity. The Exchange believes reducing open SPX options positions enables Market-Makers to continue to provide the liquidity that is critical to the options markets because reducing open SPX positions helps to reduce risk-weighted assets (RWA) attributable to SPX options positions. The Exchange developed Rule 6.56 (Compression Forums) to facilitate the reduction of open options positions in SPX (and concomitant RWA). Although the compression forums have seen limited success in reducing open SPX positions, the compression forums do not provide an adequate mechanism for Market-Makers to reduce open SPX positions across numerous options series in one large transaction, and the Exchange believes the ability for Market-Makers to efficiently and effectively reduce open SPX positions across numerous options series in one large transaction will help to reduce the risk of market dislocation, especially during periods of increased volume and volatility.

Compression forums are an inadequate, inefficient mechanism to close open SPX positions across numerous options series in one transaction partly because the files the Exchange generates pursuant to Rule 6.56 only identify individual series, call spreads, put spreads, and box spreads for which there is offsetting interest. This means that the SPX positions identified by the Exchange pursuant to Rule 6.56 have, at most, four legs (by definition box spreads have four legs

and put/call spreads have two legs), whereas the proposed RWA Package will, by definition, contain at least 50 legs, which alone demonstrates that the proposed RWA Package is a more efficient mechanism for closing open SPX positions across numerous options series in one large transaction. Moreover, the process of executing the offsetting positions identified by the Exchange pursuant to Rule 6.56 is much less efficient than the instant RWA Package proposal. For example, under Rule 6.56 the Exchange identifies offsetting positions for individual firms that submit their SPX positions in accordance with Rule 6.56. Depending on the size of the SPX portfolio submitted by the firm the Exchange may identify 100s of different boxes, call spreads, put spreads, and individual series. In addition, there will be multiple different potential counterparties for the identified positions. In order to execute just one of the identified positions the firm can seek out the potential counterparty with offsetting interest (if the firm agrees to let their identities be unmasked pursuant to Rule 6.56(a)(5)); represent the individual position (whether it be one of the boxes, call spreads, put spreads, or individual lines); negotiate a suitable execution price; and execute the transaction. This process must then be repeated over and over again in order to reduce open positions across a large portfolio of SPX options positions. In contrast, as discussed in more detail below, an RWA Package will, by definition, represent a large portfolio of SPX options positions in one large transaction (at least 50 series, etc.) as opposed to, for example, representing an individual box spread in a compression forum that contains four legs.

The Exchange believes that the ability for Market-Makers to efficiently and effectively reduce open SPX positions across numerous options series in one large transaction will help to reduce the risk of market dislocation, especially during periods of increased volume and volatility. The Exchange Market-Makers will be able to continue providing liquidity during such times (increasing the RWA attributed to the Market-Makers) because they will know that they will have the opportunity to subsequently reduce their open SPX positions (and concomitant RWA) across numerous options series in one large transaction. Without such a mechanism a Market-Maker may be forced to limit their market-making activity during periods of high volume and volatility in order to prevent

significant increases in RWA attributed to the Market-Maker, which is a scenario that may lead to market dislocation. In short, in order to help reduce the risk of market dislocation the Exchange proposes to adopt Rule 6.57 to provide a mechanism for Market-Makers to reduce open SPX options positions across numerous SPX options series in one large transaction.

The Exchange proposes to define an RWA Package as a set of SPX options positions with at least: 50 options series; 10 contracts per options series; and 10,000 total contracts.<sup>3</sup> The Exchange believes that in addition to the other requirements of Proposed Rule 6.57 (described in detail below), requiring an RWA Package to contain at least 50 options series; at least 10 contracts per options series; and at least 10,000 total contracts will help to ensure that these transactions are executed for the purpose of reducing RWA attributable to open positions and will result in a significant net reduction of RWA. The Exchange believes limiting RWA Packages to SPX options positions will similarly help to ensure that these transactions are executed for the purpose of reducing RWA because an SPX options contract has a large notional value, which exacerbates the negative impact of bank capital regulations.

Proposed Rule 6.57(b) provides that Trading Permit Holders ("TPHs") may execute an RWA Package (an "RWA transaction") in the SPX crowd on the trading floor in accordance with paragraph (c) if: (1) The RWA transaction is initiated for the account(s) of a Cboe Options Market-Maker, provided that an RWA Package consisting of SPX options from multiple Market-Maker accounts may not be in separate aggregation units or otherwise subject to information barrier or account segregation requirements;<sup>4</sup> (2) the RWA transaction results in a change in beneficial ownership (*i.e.*, an RWA transaction between a Cboe Options Market-Maker and an entity unaffiliated with the Cboe Options Market-Maker); and (3) the Cboe Options Market-Maker certifies that as of the beginning of the extended trading hours session (*i.e.*, 2:00 a.m. Chicago time) on the trade date in which the RWA Package is received by the Exchange under

<sup>3</sup> See Proposed Rule 6.57(a).

<sup>4</sup> This prohibits positions in accounts among different trading units for which accounts are otherwise required to be maintained separately to be represented as an RWA Package. Various rules (for example, Regulation SHO in certain circumstances) require accounts to be maintained separately, and the proposed rule change is consistent with those rules.

paragraph (c) the Cboe Options Market-Maker held the positions identified in the RWA Package and that the RWA Package represents a net reduction of RWA attributed to the Market-Maker based on the positions held prior to the beginning of extended trading hours. The purpose of this filing is to facilitate the closing of open positions in order to reduce RWA attributed to Market-Maker positions, which is negatively impacting liquidity provision by Market-Makers. Thus, the Exchange believes it's reasonable to limit the types of accounts for which an RWA transaction may be initiated to the account(s) of Market-Makers because, as previously noted, Market-Makers are the primary source of liquidity in the listed options market. In addition, the requirement that the RWA transaction be initiated for the "account(s)" of a Cboe Options Market-Maker is designed to, for example, allow a Cboe Options Market-Maker to represent positions for the market-making firm's universal account or represent positions for individual (or multiple) Cboe Market-Maker accounts.

In addition, the change in beneficial ownership and certification requirements help to ensure that RWA transactions will reduce a Market-Maker's RWA. With regards to the certification requirement it's necessary to identify a point in time at which the Market-Maker holds positions that are to be closed. The Exchange proposes that the point in time be prior to the opening of extended trading hours (*i.e.*, 2:00 a.m. Chicago time) on the Exchange because this will enable Cboe Options Market-Makers to identify their settled options positions (*i.e.*, positions they hold after the close of regular trading hours and prior to the open of extended trading hours).

Provided that paragraph (b) is satisfied the Exchange proposes to allow RWA Packages to be executed in accordance with the procedure set forth in paragraph (c). Proposed paragraph (c) provides that: (1) After the opening of regular trading hours and prior to 10:00 a.m. Chicago time, the Cboe Options Market-Maker (or broker) must submit the RWA Package to the Exchange in a form and manner prescribed by the Exchange. The submission must contain: (i) A list of individual SPX options series and the size of each options series; (ii) the contact information for the individual that will represent the position on the trading floor; and (iii) if prior to submitting an RWA Package to the Exchange the Market-Maker (or broker) has received a bid or offer for the RWA Package, the proposed net debit or credit price for the

RWA Package.<sup>5</sup> The Exchange believes requiring RWA Packages to be received by the Exchange after the opening of regular trading hours and prior to 10:00 a.m. Chicago time will help to ensure that RWA transactions can be executed during regular trading hours, given that proposed requirement of a two hour request for quotes ("RFQ") period, which is described more fully below. In addition, requiring the RWA Package submission to contain a list of individual SPX options series, the size of each options series, and the contact information for the individual representing the RWA Package will enable market participants to bid/offer for the RWA Package on the trading floor.

Upon the Exchange's receipt of the RWA Package, the Exchange will (i) electronically notify TPHs (electronically and via trading floor loudspeaker) as soon as practicable of the identity of the individual representing the RWA Package in the SPX trading crowd, which can be either a Market-Maker or Floor Broker, provided the individuals are available to accept bids/offers for the RWA Package; (ii) post in an electronic format on a TPH-accessible site the list of individual components of the RWA Package, the net Package price, and the contact information for the individual representing the RWA Package on the floor, which post will not include the identity of the Market-Maker for whom the RWA transaction is initiated (unless the Market-Maker is representing the RWA Package on the trading floor); and (iii) notify TPHs that the RWA Package has been posted and the time at which the two-hour request-for-quote ("RFQ") period concludes.<sup>6</sup> The Exchange believes providing the RWA Package on a TPH accessible website will give TPHs sufficient information to price RWA packages. In addition, identifying the individual representing the RWA Package on the trading floor and providing a two hour RFQ period will enable TPHs to respond to RWA Packages. The Exchange believes masking the identity of the Market-Maker for whom the RWA transaction is initiated (unless the Market-Maker is representing the RWA Package on the trading floor) will encourage Market-Makers to initiate RWA transactions.

The Exchange proposes that the two-hour RFQ Period commence upon on [sic] the Exchange's notification to the SPX trading crowd of the identity of the individual representing the RWA

Package on the floor.<sup>7</sup> The Exchange believes the two-hour period is sufficient to allow TPHs to review, price, and bid/offer for the RWA Package because the RWA Package will be available in an electronic format on a TPH-accessible website, which enables TPHs to more readily examine and price the positions in the RWA Package. Furthermore, the Exchange understands that firms have access to electronic systems that will aid them in evaluating the SPX positions contained in an RWA Package and to make a reasonable assessment of the price at which the firm is will to execute the RWA Package. The Exchange also proposes that upon the conclusion of the RFQ period, the individual representing the RWA Package in the SPX trading crowd may (but is not required to) accept a bid or offer for the RWA Package, and the RFQ response that represents the best bid or offer on a net debit or credit basis for the RWA Package has priority. The Exchange also proposes in the event equal bids or offers are received, the first RFQ response at the best bid or offer on a net debit or credit basis for the RWA Package has priority.<sup>8</sup> The Exchange notes that the contemplated priority is simply price/time priority, which is a common priority mechanism in the options industry. For example, Rule 6.45(i)(A) describes price-time priority in the context of resting orders and quotes in the electronic book. The best bid/offer for the RWA Package during the two hour RFQ period has priority over inferior prices, and if two bid/offers are made at the same price, the bid/offer that is made first then has priority—all of which is consistent with the price-time priority described in Rule 6.45(i)(A).<sup>9</sup> The Exchange notes that an individual responding to an RWA Package with a better bid/offer than a previous bid/offer is necessarily improving the bid/offer price for at least part of the RWA Package (*i.e.*, at least one individual options series in the RWA Package) because an improved net debit/credit price necessarily means at least one individual options series has received a better price.

The Exchange also notes that an RWA Package is similar to a complex order in that a market participant cannot seek to trade against only certain components of the RWA Package (*e.g.*, respond with a

<sup>7</sup> See Proposed Rule 6.57(c)(3).

<sup>8</sup> See *id.*

<sup>9</sup> The Exchange notes that if the RWA Package submission contains a bid/offer as contemplated by paragraph (c) to Rule 6.57 and a matching bid/off is made for the RWA Package in the SPX trading crowd, the bid/offer contained in the original submission has priority.

<sup>5</sup> See Proposed Rule 6.57(c)(1).

<sup>6</sup> See Proposed Rule 6.57(c)(2).

bid/offer for half of the options series instead of all of the options series in the RWA Package). Complex orders similarly cannot be split up into individual options series by an individual responding to a complex order. For example, if a complex order has three legs (*i.e.*, three separate series), a market participant responding to the complex order cannot respond with a bid/offer for leg #1, but not legs #2 or #3. Instead, the complex order is bid/offered upon based on a net debit/credit basis for the complex order as is contemplated for RWA Packages. For example, if an RWA Package is for 50 legs, a market participant responding to the RWA Package cannot respond with a bid/offer for legs #1 through #25, but not legs #26 through #50.

In addition, like complex orders, market participants may bid/offer for an RWA Package in whole or in a permissible ratio if the package can be divided into a proportional share. For example, if a complex order consisting of one leg for two contracts and another leg for two contracts is represented on the floor, a counterparty may bid/offer for 100% of the order (*i.e.*, two contracts for each leg) or the counterparty may bid/offer for a proportional share of the complex order in the 1:1 ratio of the order (*i.e.*, one contract for each leg in this example). Similarly, if an RWA Package has 50 SPX options series and 200 contracts per options series, a market participant may bid/offer for 100 contracts per leg or some other proportional share of the RWA Package in the ratio of the package. However, as with complex orders, if the RWA Package cannot be divided into a proportional share, market participants must bid/offer for the entire RWA Package. For example, if a complex order consists of one leg for one contract and another leg for two contracts, the complex order cannot be proportionally subdivided to permit a partial trade in the ratio of the order (*i.e.* 1:2); thus, market participants must bid/offer for the full size of the complex order (*i.e.*, one contract on leg #1 and two contracts on leg #2). With regards to RWA Packages, if, for example, one leg is for 11 contracts and 49 other legs are for 200 contracts, the leg for 11 contracts cannot be proportionally subdivided to permit a partial trade in the ratio of the order (*i.e.*, 11:200); thus, market participants would be required to bid/offer for the entire RWA package in this example.

As previously noted, the Exchange believes that providing a two-hour RFQ period will enable TPHs to respond to RWA Packages. In addition, the Exchange believes it's appropriate for

the best bid or offer made in response to the representation of an RWA Package to have priority; however, recognizing that the best bid or offer may not satisfy the initiator of the RWA transaction, the Exchange believes its appropriate to explicitly provide in subparagraph (3) that individuals representing RWA Packages do not have to accept a bid or offer at the conclusion of the RFQ period, which simply makes it clear that the responses received during an RFQ period are indeed quotes with which the individual representing the RWA Package may execute the RWA Package. In addition, the Exchange believes it's important not to obligate individuals representing RWA Packages to split executions among TPHs that bid or offer at the same price; rather, the Exchange believes the proposal will incentivize TPHs to provide bids or offers that better existing bids or offers because the first in time best bid or offer will have priority. As previously noted, this is consistent with the price-time priority that is common in the options industry.<sup>10</sup>

For example, suppose a market participant submits to the Exchange an RWA Package to buy for 50 SPX series and 200 contracts on each leg, which the Exchange announces to the trading floor and posts to the website. During the RFQ Period, which lasts from 1:00 p.m. to 3:00 p.m., the following offers to buy the RWA Package are represented on the floor:

- 1:10 p.m.: Floor Broker A offers to sell 100 contracts on each leg for a total of \$50,000.
- 1:15 p.m.: Floor Broker B offers to sell 100 contracts on each leg for a total of \$49,000.
- 2:00 p.m.: Floor Broker C offers to sell 100 contracts on each leg for a total of \$50,000.

Pursuant to price-time priority, Floor Broker B made the best offer, and will trade 100 contracts on each leg with the RWA Package for \$49,000, leaving 100 contracts on each leg remaining in the RWA Package. Floor Brokers A and C offered the same price for the same amount. Pursuant to price-time priority Floor Broker A made its offer first, and thus will trade 100 contracts on each leg with the remaining portion of the RWA Package for \$50,000. Floor Broker C will not participate in the trade.

Furthermore, the RWA Package is considered executed (and a contract formed) upon the acceptance of a bid or offer by the individual representing the RWA Package following the conclusion of the RFQ Period. The Exchange

proposes that if the individual representing the RWA Package accepts a bid or offer for the RWA Package, the individual representing the RWA Package on the trading floor must, prior to the close of regular trading hours, cause a report to be submitted to the Exchange in a form and manner prescribed by the Exchange which sets forth the time of the execution of the RWA Package, the net execution price for the RWA Package, and the execution prices for the individual components of the RWA Package.<sup>11</sup> The Exchange believes the reporting requirements will enable the Exchange to maintain an adequate audit trail and, if necessary, review individual RWA transactions.

Additionally, the Exchange proposes to adopt Interpretation and Policy .01 to provide that to the extent applicable, all other Rules of the Exchange, including Rule 6.9(e), apply to the procedure set forth in proposed Rule 6.57. The Exchange also proposes to provide in Interpretation and Policy .01 that the following Rules are either superseded by proposed Rule 6.57 or do not apply to the above procedures: 6.9(a) through (d) and (f), 6.41, 6.44, 6.45, 6.47, and 6.74) [sic] and that there may be other rules of the Exchange that do not, by their terms, apply to the transfer procedure set forth in this Rule 6.57. As previously noted, proposed Rule 6.57 is a special procedure designed to provide a mechanism which allows Cboe Market-Makers to reduce open SPX options positions across numerous options series in one large transaction, and in order to give the effect to the procedures set forth in Rule 6.57 it is necessary for Rule 6.57 to supersede rules that provide for potentially conflicting procedures (*e.g.*, Rules 6.9(a) through (d) and (f), 6.41, 6.44, 6.45, 6.47, and 6.74). The Exchange notes that this is patterned from Rule 6.49A, which also provided that Rule 6.49A supersede Rules 6.41, 6.44, 6.45, 6.47, and 6.74.

Specifically, the Exchange proposes to explicitly provide that Rule 6.9(e) applies to the procedures set forth in Rule 6.57. This reference to Rule 6.9 is patterned from Rule 6.49A, which explicitly referenced Rule 6.9 in its entirety as applying to Rule 6.49A. Contrary to Rule 6.49A, however, the Exchange proposes that only paragraph (e) of Rule 6.9 apply to Rule 6.57 instead of Rule 6.9 in its entirety. Rule 6.9(e) governs trading based on knowledge of imminent undisclosed solicited transactions, and the Exchange believes it's important for such rules to apply to Rule 6.57. The Exchange believes Rule

<sup>10</sup> Cboe Options Rule 6.45 permits price-time priority in certain classes.

<sup>11</sup> See Proposed Rule 6.57(c)(4).

6.9(a) through (d) and (f) are sufficiently superseded by the procedures set forth in Rule 6.57(c). Specifically, Rule 6.9(a) through (d) sets forth the priority for several different scenarios in which an order and solicited order on the opposite side of that order may be represented on the floor, and the priority that will apply in each scenario. Rule 6.9(a) governs solicited transactions involving a disclosed original order and matching solicited order that improves the market; Rule 6.9(b) governs solicited transactions involving a disclosed original order that is later modified to meet a solicited order improving the market; Rule 6.9(c) governs solicited transactions involving disclosed original order that is later modified to meet a solicited order not improving the market; and Rule 6.9(d) involves solicited transactions involving an undisclosed original order. Additionally, Rule 6.9(f), which requires solicited orders to be marked, would not be necessary, as it would be known that an order was solicited for an RWA Package at the time they were provided to the Exchange in accordance with proposed Rule 6.57.

Pursuant to proposed Rule 6.57, an RWA Package, including any solicited orders to trade against the RWA Package, must be represented in a single way (by notification to the Exchange, which then announces the package to the trading floor). As a result, an RWA Package and corresponding solicited order could never be undisclosed. Additionally, pursuant to the proposed process, if the Market-Maker receives a bid or offer for the RWA Package prior to submitting it to the Exchange (as it would if it had a solicited order), the proposed price must be disclosed. As a result, for every RWA Package with a solicited order, the Exchange will announce them and the proposed price to the crowd at the same time, and thus the solicitation would have occurred before the RWA Package was disclosed to the crowd. Therefore, Rule 6.9(a) would not apply, as that paragraph covers a situation in which an order is disclosed prior to solicitation. There is also no method in the proposed process for modifying the RWA Package or any solicited order. Rule 6.9(b) and (c) address situations in which a represented order is later modified to meet a solicited order, and thus would not apply to RWA Packages. Lastly, Rule 6.9(f) is inapplicable to Rule 6.57 because following the procedures set forth in Rule 6.57 will provide all necessary information for Exchange purposes.

Proposed Rule 6.57(c) also sets forth the specific priority of RWA

Transactions, and thus no other priority rules would apply. The Exchange believes it is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to explicitly identify the priority applicable to RWA Packages in Rule 6.57(c) because it will help to avoid confusion as to the priority applicable to RWA Packages. More importantly, the priority set forth in Rule 6.57(c) is consistent with Exchange Act because the proposed priority is simply price-time priority, which is common in the options industry.

With regards to the instant proposal Rule 6.41—Meaning of Premium Bids and Offers—is inapplicable because Rule 6.41 is already inapplicable to index options such as SPX options. Thus, an RWA Package, which by definition can only contain SPX options, will not be subject to Rule 6.41. The Exchange believes it is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to explicitly provide that Rule 6.57 supersedes Rule 6.41 to avoid any possible confusion regarding the applicability of Rule 6.41 to RWA Package execution.<sup>12</sup>

In addition, Rule 6.44—Bids and Offers in Relation to Units of Trading—is inapplicable to the instant proposal. Rule 6.44 sets forth the meaning of bids and offers for one contract where RWA Packages must be for more than one contract. The Exchange believes it is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to explicitly provide that Rule 6.57 supersedes Rule 6.44 to avoid any possible confusion regarding the applicability of Rule 6.44 to RWA Package execution.

Furthermore, Rule 6.45—Order and Quote Priority and Allocation; Rule 6.47—Priority on Split-Price Transactions Occurring in Open Outcry; and Rule 6.74—Crossing Orders—are superseded by Rule 6.57. Rules 6.45, 6.47, and 6.74 set forth priority in various scenarios, which is superseded by Rule 6.57 because the priority of bids and offers for RWA Packages is set forth in Rule 6.57(c)(3). In the same manner that Rule 6.47 describes the priority for a particular scenario (*i.e.*, split-price) instead of describing that priority in

Rule 6.45, the Exchange believes it best to describe priority for this particular scenario (*i.e.*, RWA Packages) in a separate rule. Additionally, as previously noted, the priority set forth in Rule 6.57 is based on price-time priority, which is a longstanding priority method in the options industry. Moreover, the Exchange believes it is consistent with Exchange Act for the priority of bids/offers in the context of RWA Packages to be based on price-time priority as price-time priority is a common standard in the options industry.

Importantly, it is critical that RWA Packages be executed without regard to the specific priority set forth in Rule 6.45, 6.47, or 6.74. RWA Packages are, by design, very large and very complicated orders that are specifically intended to help SPX Market-Makers reduce the RWA associated with open SPX positions. Rules 6.45, 6.47, and 6.74, including provisions in those rules that require orders to cede priority to individual legs in the electronic book, are not designed to accommodate the execution of such large, complicated, uniquely purposed orders. Thus, the Exchange believes the significantly large size and complexity of RWA packages make it necessary to deviate from Rules 6.45, 6.47, 6.74.

Additionally, the limited purpose of RWA Packages and the temporary nature of the proposed rule further support the need to permit executions of RWA Packages without regard to the priority in current rules. As discussed above, the purpose of RWA Packages is to reduce the risk-weighted assets attributable to Market-Makers' SPX options positions. Requiring trades against the leg markets may interfere with the desired reduction in RWA associated with the package, and may cause execution of the package to be less efficient. Efficient reductions in RWA pursuant to the proposed rule change may free up capital, which will to enable Market-Makers to continue to provide liquidity to the SPX market, which liquidity benefits all market participants. The Exchange believes the narrow scope of the proposed rule change and the limited, beneficial purpose of RWA Packages make allowing RWA Packages to execute without interacting with pre-existing interest on the electronic book appropriate and important to support the provision of liquidity in the SPX market.<sup>13</sup>

<sup>12</sup> The Exchange notes that Rule 24.8—Meaning of Premium Bids and Offers—applies to index options.

<sup>13</sup> S&P 500 Option Variance Basket Trades, a particular basket of SPX options with a limited purpose, may execute without interacting with pre-Continued

Moreover, the Exchange expects many potential counterparties to be solicited prior to the RWA Package being sent to the Exchange or announced in the SPX trading crowd. These solicitations will likely result in a net package price at which the counterparty is willing to execute the RWA Package. If parties representing RWA Packages were required to cede priority to individual legs in the electronic order book many RWA Packages would likely go unexecuted as the execution of one leg of an RWA Package would disrupt the net execution price and the weighting/risk profile of the RWA package. Additionally, the size and complexity of RWA Packages make it functionally difficult for RWA Packages to interact with the electronic book under normal circumstances. To the extent one leg of an RWA Package could execute with an order in the electronic book, the remaining orders on the electronic book (complex order book or simple order book) are unlikely to have the necessary size and depth across a large portfolio of options to satisfy the terms of an RWA Package. Thus, requiring RWA Packages to follow the priority in Rule 6.45, 6.47, or 6.74 would effectively prevent RWA Packages from being executed.

The Exchange believes it is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to deviate from existing priority rules because doing so will allow RWA Packages to be executed, which, in turn, will help reduce the RWA associated with a Market-Maker's SPX Position, and, in turn, will reduce the risk of market dislocation, especially during periods of increased volume and volatility [sic].

In addition, the Exchange proposes to adopt Interpretation and Policy .02 to provide that nothing in paragraph (a) of Rule 6.57 prevents a Market-Maker from executing transactions (opening or closing) during the RFQ period in the normal operation of the Market-Maker's business. Market-Makers have affirmative obligations, and the Exchange believes the adoption of Interpretation and Policy .02 helps ensure that Rule 6.57 does not prevent Cboe Options Market-Makers from satisfying their affirmative obligations by, for example, buying and selling options series during the RFQ period in the normal course of their operations.

Finally, the Exchange proposes to adopt Interpretation and Policy .03 to

implement Rule 6.57 for a limited term ending two years from the approval date of this rule filing.

## 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.<sup>14</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>15</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>16</sup> 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 will help facilitate the reduction of open SPX options positions (and concomitant RWA), which helps to protect investors and the public interest by enabling Market-Makers to continue to provide liquidity that is critical to the SPX options markets. Although the Exchange is seeking to limit RWA transactions to those initiated by Cboe Options Market-Makers, the proposal is not designed to permit discrimination between customers, issuers, brokers, or dealers; rather, the proposal seeks to alleviate the negative impact of bank capital requirements on the primary liquidity providers in the listed options market (*i.e.*, Market-Makers), who are disproportionately impacted by bank capital requirements governing bank-affiliated clearing firms. The Exchange believes the ability for Market-Makers to efficiently and effectively reduce open positions across numerous options series in one large transaction will help to reduce the risk of market dislocation, especially during periods of increased volume and volatility. Market-Makers will be able to continue providing liquidity during such times (increasing the RWA attributed to the Market-

Makers) because they will know that they can subsequently reduce their open positions (and concomitant RWA) across numerous options series in one large transaction.

Furthermore, the Rule 6.57 is patterned on Rule 6.49A, which sets forth similar procedures for on-floor transfers. In addition, generally, Rule 6.57 is an exception to various Exchange trading rules because RWA Packages are designed to carry out the important purpose of reducing RWA, and the construction and procedures set forth in Rule 6.57 are necessary to carry out that purpose. RWA Packages are large in size (at least 10,000 options) and broad in construction (at least 50 separate options series) and must be closing transactions because the purpose of RWA Packages is to significantly reduce RWA associated with Market-Maker positions to enable Market-Makers to continue to provide critical liquidity to SPX options. In order to functionally execute such a large portfolio of SPX options the Exchange believes it is necessary for the procedures to deviate from certain current exchange trading rules. The Exchange believes the narrow scope of the proposed rule change and the limited, beneficial purpose of RWA Packages make allowing RWA Packages to execute without interacting with pre-existing interest on the electronic book appropriate and important to support the provision of liquidity in the SPX market.<sup>17</sup> Specifically, the Exchange believes it is necessary and proper for interpretation and policy .01 to specify that Rules 6.9(a) through (d) and (f), 6.41, 6.44, 6.45, 6.47, and 6.74 are either supersede [sic] by, or do not apply to, Rule 6.57.

As previously noted above, the proposed procedure for RWA Packages sets forth the specific manner in which RWA Packages and any solicited orders must be represented, and thus the situations described in Rule 6.9(a) through (d) and (f) would never occur. The proposed rule makes clear that these provisions are superseded by the proposed rule.

In addition, Rule 6.41 is inapplicable to RWA Packages because Rule 6.41 is inapplicable to index options such as SPX options. Thus, an RWA Package, which by definition can only contain SPX options, will not be subject to Rule 6.41. Furthermore, Rule 6.44 sets forth the meaning of bids and offers for one contract where RWA Packages must be for more than one contract; thus, Rule

existing interest on the electronic book. See Rule 6.53B(c).

<sup>14</sup> 15 U.S.C. 78f(b).

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

<sup>16</sup> *Id.*

<sup>17</sup> S&P 500 Option Variance Basket Trades, a particular basket of SPX options with a limited purpose, may execute without interacting with pre-existing interest on the electronic book. See Rule 6.53B(c).

6.44 is similarly inapplicable to RWA Packages. The Exchange believes it is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to explicitly provide that Rule 6.57 supersedes Ruls [sic] 6.41 and 6.44 to avoid any possible confusion regarding the applicability of Rules 6.41 and 6.44 to RWA Package execution.

In particular, the Exchange believes it is critical that RWA Packages be executed without regard to the specific priority set forth in Rule 6.45, 6.47, or 6.74 because the size of the RWA Packages (at least 50 SPX options series, 10 options per series, and at least 10,000 options) makes it functionally impossible for RWA Packages to interact with the electronic book as orders on the electronic book (complex order book or simple order book) do not have the necessary size and depth across a large portfolio of options to satisfy the terms of an RWA Package. Thus, requiring RWA Packages to follow the priority in Rule 6.45, 6.47, or 6.74 would prevent RWA Packages from being executed. Given the limited purpose and significant size and complexity of RWA Packages, the Exchange believes it is consistent with Exchange Act and helps remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest to permit RWA transactions to deviate from existing priority rules. This will permit [sic] because doing so will allow RWA Packages to be executed in an efficient manner, which, in turn, will help reduce the RWA associated with a Market-Maker's SPX positions, and, in turn, will reduce the risk of market dislocation, especially during periods of increased volume and volatility.

To the extent Cboe Market-Makers cannot reduce options positions in an efficient and effective manner their ability to continue to provide liquidity may be impaired. As noted, the procedures set forth in Rule 6.57 are similar to the procedures set forth in Rule 6.49A. The Exchange believes the procedures set forth in Rule 6.57 improve on the procedures set forth in Rule 6.49A as Rule 6.57, among other things, provides for the publication of RWA Packages in an electronic format, which allows for a fair process by which TPHs may review, price, and bid/offer for an RWA Package.

In addition, the Exchange believes proposed Interpretation and Policy .02, which provides that nothing in paragraph (a) of Rule 6.57 prevents a Market-Maker from executing

transactions (opening or closing) during the RFQ period in the normal operation of the Market-Maker's business, is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest by helping to ensure Market-Makers continue to perform their affirmative obligations during the trading day.

Finally, the Exchange believes proposed Interpretation and Policy .03, which indicates that Rule 6.57 is to be adopted for a limited term ending two years from the approval date of this rule filing, is consistent with Exchange Act and helps to remove impediments to and perfect the mechanism of a free and open market and, in general, helps protect investors and the public interest by allowing the Exchange to evaluate at the end of the two-year period whether Rule 6.57 continues to be a useful tool to reduce RWA associated with SPX options positions.

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

Cboe Options 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. Although the Exchange is seeking to limit RWA transactions to those initiated by Cboe Options Market-Makers, the Exchange does not believe the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act because the proposal seeks to alleviate the negative impact of bank capital requirements on the primary liquidity providers in the listed options market (*i.e.*, Market-Makers), who are disproportionately impacted by bank capital requirements governing bank-affiliated clearing firms. Use of the proposed process is voluntary, and all Market-Makers with SPX positions may engage in RWA transactions. The proposed rule change proposes a process that may be carried out only [sic] the Exchange's trading floor in a product that trades solely on the Exchange. RWA Transactions have a limited purpose, which is to reduce RWA attributable to Market-Makers' SPX open positions in order to free up capital and enable Market-Makers to continue to provide the liquidity to the SPX market, which liquidity benefits all market participants. This is not intended to be a competitive trading tool.

#### *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-2018-056 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-2018-056. 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 (<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-CBOE-2018-056 and should be submitted on or before September 7, 2018.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>18</sup>

**Eduardo A. Aleman,**  
Assistant Secretary.

[FR Doc. 2018-18158 Filed 8-22-18; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-83882; File No. SR-FINRA-2018-032]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change To Amend FINRA Rule 6710 To Modify the Dissemination Protocols for Agency Debt Securities

August 17, 2018.

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> notice is hereby given that on August 16, 2018, the Financial Industry Regulatory Authority, Inc. ("FINRA") 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 FINRA. 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

FINRA is proposing to amend FINRA Rule 6710 to modify the dissemination

protocols with respect to Agency Debt Securities.

The text of the proposed rule change is available on FINRA's website at <http://www.finra.org>, at the principal office of FINRA 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, FINRA 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. FINRA 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 the Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

FINRA requires members to report to the Trade Reporting and Compliance Engine ("TRACE") transactions in TRACE-Eligible Securities,<sup>3</sup> including securities that meet the definition of "Agency Debt Security."<sup>4</sup> FINRA disseminates transaction information on Agency Debt Securities and displays either the actual size (volume) of the transaction or a capped amount, depending on whether the security is rated as Investment Grade,<sup>5</sup> Non-

Investment Grade,<sup>6</sup> or is unrated. For transactions in Agency Debt Securities that are either Investment Grade or unrated, FINRA disseminates the actual size of the trade for transactions less than or equal to \$5 million in par value traded, thus providing actual transaction size up to \$5 million, and disseminates "\$5MM+" for trades exceeding \$5 million in par value traded.<sup>7</sup> For transactions in Agency Debt Securities that are Non-Investment Grade, FINRA disseminates the actual size of the trade for transactions less than or equal to \$1 million in par value, and disseminates "1MM+" for trades exceeding \$1 million in par value traded.<sup>8</sup>

FINRA is proposing to apply a \$5 million dissemination cap to all Agency Debt Securities, regardless of the rating assigned to the security. When adopting the original dissemination caps for Agency Debt Securities, FINRA believed that unrated Agency Debt Securities should default to the \$5 million dissemination cap due to factors such as that they trade more consistently with Investment Grade securities that are subject to the \$5 million dissemination cap. While Non-Investment Grade Agency Debt Securities have been disseminated with the \$1 million dissemination cap, FINRA is not aware of the existence of any Non-Investment Grade Agency Debt Securities other than credit risk transfer securities ("CRTs"), a type of Agency Debt Security issued by Fannie Mae ("Fannie") and Freddie Mac ("Freddie"). Based on experience gained with CRTs and in consultation with Fannie and Freddie, FINRA

<sup>3</sup> Rule 6710 generally defines a "TRACE-Eligible Security" as: A debt security that is United States ("U.S.") dollar-denominated and is: (1) Issued by a U.S. or foreign private issuer, and, if a "restricted security" as defined in Securities Act Rule 144(a)(3), sold pursuant to Securities Act Rule 144A; (2) issued or guaranteed by an Agency as defined in Rule 6710(k) or a Government-Sponsored Enterprise as defined in Rule 6710(n); or (3) a U.S. Treasury Security as defined in Rule 6710(p). "TRACE-Eligible Security" does not include a debt security that is issued by a foreign sovereign or a Money Market Instrument as defined in Rule 6710(o).

<sup>4</sup> "Agency Debt Security" generally includes a debt security (i) issued or guaranteed by an Agency as defined in Rule 6710(k); (ii) issued or guaranteed by a Government-Sponsored Enterprise ("GSE") as defined in Rule 6710(n); or (iii) issued by a trust or other entity that was established or sponsored by a GSE for the purpose of issuing debt securities, where such enterprise provides collateral to the trust or other entity or retains a material net economic interest in the reference tranches associated with the securities issued by the trust or other entity. Rule 6710(n) provides that "Government-Sponsored Enterprise" has the same meaning as defined in 2 U.S.C. 622(8).

<sup>5</sup> Rule 6710 provides that "Investment Grade" means "a TRACE-Eligible Security that, if rated by only one nationally recognized statistical rating organization ("NRSRO"), is rated in one of the four

highest generic rating categories; or if rated by more than one NRSRO, is rated in one of the four highest generic rating categories by all or a majority of such NRSROs; provided that if the NRSROs assign ratings that are evenly divided between (i) the four highest generic ratings and (ii) ratings lower than the four highest generic ratings, FINRA will classify the TRACE-Eligible Security as Non-Investment Grade for purposes of TRACE. If a TRACE-Eligible Security is unrated, for purposes of TRACE, FINRA may classify the TRACE-Eligible Security as an Investment Grade security. FINRA will classify an unrated Agency Debt Security as defined in [Rule 6710(l)] as an Investment Grade security for purposes of the dissemination of transaction volume." See FINRA Rule 6710(h).

<sup>6</sup> Rule 6710 provides that "Non-Investment Grade" means "a TRACE-Eligible Security that, if rated by only one NRSRO, is rated lower than one of the four highest generic rating categories; or if rated by more than one NRSRO, is rated lower than one of the four highest generic rating categories by all or a majority of such NRSROs. Except as provided in paragraph (h), if a TRACE-Eligible Security is unrated, FINRA may classify the TRACE-Eligible Security as a Non-Investment Grade security." See FINRA Rule 6710(i).

<sup>7</sup> See Securities Exchange Act Release No. 59733 (April 8, 2009), 74 FR 17709 (April 16, 2009) (Notice of Filing of File No. SR-FINRA-2009-010).

<sup>8</sup> See *supra* note 7.

<sup>18</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.