been sent. The identity of the sender and recipients will not be known to any party, and the Exchange will not disclose a list of BX Participants that have opted-in to receive Requests for PRISM.

It would be deemed conduct inconsistent with just and equitable principles of trade and a violation of Options 9, Section 1, and other Exchange Rules, to utilize non-public information in connection with a Request for PRISM to a BX Participant’s economic advantage. The Exchange intends to begin implementation of the proposed rule change by June 30, 2021. The Exchange will issue an Options Trader Alert to BX Participants with the date of implementation.

III. Discussion and Commission Findings

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange. In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act, which requires that the rules of an exchange be designed, among other things, 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 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, and not be designed to permit unfair discrimination between customers, issuers, brokers or dealers. The Commission also finds that the proposed rule change is consistent with Section 6(b)(8) of the Act, which requires that the rules of a national securities exchange not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

The proposed rule change appears reasonably designed to offer Participants an efficient process to solicit an Initiating Order among other BX Participants for entry into the PRISM auction. The Commission believes that by permitting BX Participants to use FIX to send a Request for PRISM (with a PRISM Order) simultaneously to all BX Participants that have opted-in, the proposed Request for PRISM process would provide BX Participants with another means of soliciting interest for a PRISM auction from a potentially broader group of market participants, potentially providing price improvement to the PRISM Order. The Commission further notes that the proposal would not amend the manner in which PRISM auction operates. Any paired order entered into PRISM must comply with the eligibility requirements of BX Options 3, Section 13(i) to commence the auction and the auction process will operate as it does today.

The Commission also believes that the proposal appears to be designed to provide an objective process for the selection of the contra-side to the PRISM Order. Any BX Participant may choose to opt-in, and those who opt-in would receive any Request for PRISM sent from BX Participants. Further, any BX Participant that chooses to opt-in may subsequently opt-out. In addition, the Exchange has proposed that the identity of the sender and recipients would not be known to any party and that it would not disclose a list of the BX Participants that opted-in to receive a Request for PRISM. Thus, the decision of which Participant is chosen to provide the Initiating Order will be based solely on which recipient responded first to the Request for PRISM.

The Commission also believes that the proposed rule change appears designed to prevent the misuse of information related to the proposed Request for PRISM and create an audit trail for surveilling Requests for PRISM. The Exchange represents that it will employ surveillances to prevent misuse of non-public information related to a Request for PRISM similar to how it employs surveillances today to ensure that information available in auctions is not misused. The Exchange also represents that the communications that would occur, through FIX, would be available to and maintained by the Exchange, and that it would be able to monitor entries into both the order book and the PRISM auction. Further, the Exchange proposes in Options 3, Section 13 that it would be deemed conduct inconsistent with just and equitable principles of trade and a violation of Options 9, Section 1, and other Exchange Rules for BX Participants receiving Requests for PRISM to utilize the information to a BX Participant’s economic advantage. In addition, a Request for PRISM would be subject to the restrictions set forth in BX Options 3, Section 22 (Limitations on Order Entry), and any paired order resulting from a Request for PRISM would be subject to the PRISM auction requirements in BX Options 3, Section 13.

For the reasons set forth above, the Commission believes that the proposed rule changes are consistent with the requirements of the Act.

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (SR–BX–2020–033) hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.37

Jill M. Peterson,
Assistant Secretary.

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SECURITIES AND EXCHANGE COMMISSION


Self-Regulatory Organizations; Cboe Exchange, Inc.; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, To Amend Rules 5.37, 5.38, and 5.73 Related to Auction Notification Messages and Index Combo Orders in SPX in the Complex Automated Improvement Mechanism, and FLEX Automated Improvement Mechanism

February 12, 2021.

I. Introduction

On June 3, 2020, Cboe Exchange, Inc. (“Exchange” or “Cboe”) filed with the Securities and Exchange Commission

35 Notice, supra note 5, at 73098.
36 See id.
("Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")1 and Rule 19b-4 thereunder,2 a proposed rule change to amend Rules 5.37, 5.38, and 5.73 to (1) allow the Exchange to determine to disseminate the stop price in auction notification messages for Automated Improvement Mechanism ("AIM"), Complex Automated Improvement Mechanism ("C–AIM"), and FLEX AIM auctions in S&P 500® Index options ("SPX"); and (2) modify the minimum increment for C–AIM and FLEX AIM auction responses to Index Combo Orders in SPX. The proposed rule change was published for comment in the Federal Register on June 18, 2020.3

On July 22, 2020, the Exchange submitted Amendment No. 1 to the proposed rule change, which replaced and superseded the proposed rule change in its entirety.4 On July 27, 2020, pursuant to Section 19(b)(2) of the Act,5 the Commission designated a longer period within which to approve or disapprove the proposed rule change, as modified by Amendment No. 1.6 This order approves the proposed rule change, as modified by Amendment No. 1.7

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

A. Background

The AIM, C–AIM, and FLEX AIM are electronic auctions intended to provide an agency order with the opportunity to receive price improvement (over the National Best Bid or Offer in AIM, or the synthetic best bid or offer on the Exchange in C–AIM).8 Upon submitting an agency order into one of these auctions, the Initiating Trading Permit Holder must also submit a contra-side second order for the same size as the agency order. The contra-side order guarantees that the agency order will receive an execution. Upon commencement of an auction, market participants submit responses to trade against the agency order. At the conclusion of the auction, depending on the contra-side interest available, the contra-side order may be allocated a certain percentage of the agency order.9

On March 16, 2020, the Exchange activated the AIM and C–AIM in SPX and FLEX AIM options, so that trading in SPX could continue while the trading floor was closed.10 Once the trading floor re-opened on June 15, 2020, the Exchange disengaged AIM and C–AIM for SPX. Prior to the trading floor closure, the Exchange had not activated C–AIM (or AIM) in SPX and thus all non-FLEX crossing transactions in SPX were previously only able to occur on the trading floor.11

B. Minimum Increment for Index Combo Orders in SPX

The Exchange proposes to amend Rules 5.38 and 5.73 to modify the minimum increment for C–AIM and FLEX AIM auction responses, respectively, in which the agency order complex strategy is comprised of an Index Combo Order (as defined in Rule 5.33(b) in SPX).12 When submitting an agency order into a C–AIM auction, the initiating member must also submit principal or solicited contra-side complex order(s) for the same size as the agency order, which guarantees that the agency order will receive an execution.13 Upon commencement of a C–AIM auction, market participants submit responses to trade against the agency order and at the conclusion of an auction, depending on the contra-side interest available, the contra order may be allocated a certain percentage of the agency order.14

Rules 5.38(c)(5)(A) and 5.38(a)(4) currently provide that the minimum price increment for C–AIM responses and agency and initiating orders, respectively, must be in an increment the Exchange determines on a class basis, which is $0.05 in SPX options.15 The corresponding FLEX AIM Rules 5.73(c)(5)(A) and 5.73(a)(4) provide the same treatment for FLEX AIM auctions. Thus, under current rules market participant responses in the C–AIM and FLEX AIM auctions must improve the net package price (i.e., each strategy unit) based on then-current leg markets by at least the minimum increment of $0.05.16 Because of the differences between the quoting practices on floor and the quoting practices in the C–AIM and FLEX AIM auctions with respect to Index Combo Orders in SPX,17 however,

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4 In Amendment No. 1, the Exchange amended the proposal to: (1) To add that, when the proposed stop price dissemination in auction notification messages is enabled for AIM, C–AIM, or FLEX AIM auctions in SPX, it would apply to all such AIM, C–AIM, or FLEX AIM auctions; (2) to specify that the proposed minimum increment modification would apply to Index Combo Orders in SPX, and to correct an internal cross-reference in the proposed rules; (3) to provide additional detail to the description and example of the proposed modification to the minimum increment for Index Combo Orders in SPX; and (4) to provide additional justification and support for the proposed rule change. The full text of Amendment No. 1 is available on the Commission's website at: https://www.sec.gov/comments/sr-cboe-2020-052/srcboe2020052-744403-221166.pdf.
6 See Securities Exchange Act Release No. 89400, 85 FR 46202 (July 31, 2020). The Commission designated September 16, 2020 as the date by which the Commission shall approve or disapprove, or institute proceedings to determine whether to disapprove, the proposed rule change.
8 See Securities Exchange Act Release No. 89505, 85 FR 80863 (December 14, 2020). The Commission designated February 13, 2021 as the date by which the Commission shall approve or disapprove, or institute proceedings to determine whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1.9 This order approves the proposed rule change, as modified by Amendment No. 1.
9 See Securities Exchange Act Release No. 90592, 85 FR 80863 (December 14, 2020). The Commission designated September 16, 2020 as the date by which the Commission shall approve or disapprove, or institute proceedings to determine whether to disapprove, the proposed rule change.
11 See Rules 5.38 (AIM), 5.38 (C–AIM), and 5.73 (FLEX AIM).
12 See Rules 5.37(e), 5.38(e), and 5.73(e).
13 The Exchange had activated C–AIM and AIM in SPX for the first time as a result of the March 16, 2020 trading floor suspension to help prevent the spread of COVID–19. According to the Exchange, FLEX AIM in SPX had been activated prior to March 16, 2020.
14 An Index Combo Order is an order to purchase or sell one or more index option series and the offsetting number of Index Combinations defined by the delta. For purposes of an Index Combo order, the following terms have the following meanings: (1) An "Index Combination" (8.00) is the price (negative) number of Index Combinations that must be sold (purchased) to establish a market neutral hedge with one or more series of the same index option; and (3) An Index Combo order may not have a ratio greater than eight options to one Index Combination (8.00), and will be subject to all provisions applicable to complex orders (excluding the one-to-three/three-to-one ratio) in the Rules. See Rule 5.33(b).
15 See Rule 5.38.
16 See generally Rule 5.38(e). The same process applies to the FLEX AIM auction pursuant to the FR Rules. See generally Rule 5.73(e).
17 The System rejects a C–AIM response or agency or initiating order that is not in the applicable minimum increment.
18 Although members of the trading crowd on the trading floor are permitted to improve the net package price (based on then-current leg markets) by the minimum increment of $0.05, the Exchange states that this is not the common practice. See Amendment No. 1, supra note 4, at 9.
19 An Index Combo Order in SPX is a complex order that includes one or more SPX legs, hedged by an SPX combo, or synthetic future, defined by the delta. The Exchange notes that Index Combo Orders in SPX comprise a significant portion of crosses in SPX and that a significant amount of SPX volume was executed through C–AIM when the...
applying the $0.05 minimum increment to auction responses in both floor trading and the electronic C–AIM and FLEX AIM auctions could result in a significant difference in the price improvement that an order receives depending on whether the Index Combo Order in SPX is traded in the electronic auctions or on the trading floor.\footnote{See id. at 9–11, for examples of these pricing distinctions in practice.} A floor broker seeking to cross SPX complex orders on the trading floor generally identifies the legs of the complex order and their relative sizes to each other with a net package price.\footnote{See id. at 7.} The trading crowd then generally provides a market based on the strategy’s theoretical value, rather than on the value of the net package (which equals the strategy times the ratio), particularly when the complex order represented is a delta neutral order that includes a combo.\footnote{See id. at 7.} In open outcry trading, the trading crowd generally prices the combo hedge portion separately from the non-combo portion of the order.\footnote{See id. at 10 (stating that in April 2020, Index Combo Orders in SPX comprised 60.5% of crossed trading, the trading crowd generally identifies the legs of the complex order and their relative sizes to each other with a net package price.) If the crowd improves the price of the non-combo leg of the order by a minimum increment, or greater, that price is given on each contract.\footnote{See id. at 10 (stating that in April 2020, Index Combo Orders in SPX comprised 60.5% of crossed trading, the trading crowd generally identifies the legs of the complex order and their relative sizes to each other with a net package price.) The proposed changes are intended to provide for substantially the same price improvement opportunities at meaningful increments for Index Combo Orders in SPX, whether they are submitted to the C–AIM or FLEX AIM electronic auctions or executed on the trading floor.\footnote{See id. at 10.} Accordingly, to better align the C–AIM and FLEX AIM electronic auction crossing processes and the open outcry crossing process for Index Combo Orders in SPX, the Exchange proposes to amend Rule 5.37(c)(5)(A) to revise the FLEX AIM process for Index Combo Orders in SPX in the same manner.\footnote{See amended Rule 5.37(c)(5)(A).} The Exchange also proposes to amend Rule 5.73(c)(5)(A) to revise the FLEX AIM process for Index Combo Orders in SPX in the same manner.\footnote{See amended Rule 5.73(c)(5)(A).} C. Auction Stop Price Dissemination in SPX

Current Rules 5.37(c)(2), 5.38(c)(2), and 5.73(c)(2) provide that the system initiates the AIM, C–AIM, and FLEX AIM auction processes, respectively, by sending an auction notification message detailing the side, size, auction ID, and options series and, for C–AIM auctions, complex strategy, or, for FLEX AIM auctions, length of the auction period and options series or complex strategy, as applicable) of the agency order to all users that elect to receive AIM, C–AIM, or FLEX AIM auction notification messages.\footnote{See id. at 12–13.} Because AIM, C–AIM, and FLEX AIM auction notification messages are not included in the disseminated BBO (in connection with AIM auctions) or OPRA, the Exchange does not currently include the stop price of an agency order in auction notification messages.\footnote{See id. at 12–13.} To better align the AIM and C–AIM pricing process in SPX with the open outcry process, the Exchange proposes to amend Rules 5.37(c)(2) and 5.38(c)(2) to provide that the Exchange may also determine to include the stop price in SPX AIM and C–AIM auction notification messages.\footnote{See id. at 12–13.} As with all other information disseminated in an AIM and C–AIM auction notification message, the disseminated stop price for SPX auctions will be available to all users that elect to receive auction notification messages.\footnote{See id. at 12–13.} Because the FLEX AIM rules are similar to the AIM and C–AIM rules, the Exchange also proposes to maintain this consistency by amending Rule 5.73(c)(2) to similarly provide that the Exchange may determine to include the stop price in FLEX AIM auction notification messages for all FLEX AIM auctions in SPX.\footnote{See amended Rule 5.73(c)(2).}

3210 Combos, using a delta of 12.5, the System would calculate the minimum increment by multiplying the ratio of the non-combo leg of the order (800) to the number of combos (100) by the minimum increment of $0.05. Therefore, $0.80 × 0.05 = $0.40 as the resulting point for price improvement during the C–AIM or FLEX C–AIM auction. See id.\footnote{See id. at 6.} The Exchange represents that it will notify its trading permit holders of a determination to include the stop price in auction notification messages, pursuant to Rule 1.5, via a specification, notice, or regulatory circular with appropriate advanced notice, which will be posted on the Exchange’s website, electronic message, or other communication method as provided in the Rules. See id. at 12 n.18.\footnote{See id. at 12 n.18.} The Exchange represents that it will notify its trading permit holders of a determination to include the stop price in auction notification messages, pursuant to Rule 1.5, via a specification, notice, or regulatory circular with appropriate advanced notice, which will be posted on the Exchange’s website, electronic message, or other communication method as provided in the Rules. See id. at 12 n.18.\footnote{See id. at 12 n.18.}

The Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.\footnote{See id. at 12–13.} In particular, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with Section 6(b)(5) of the Act,\footnote{See id. at 12–13.} which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to 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. The Commission also finds that the proposed rule change, as modified by Amendment No. 1, is consistent with Section 6(b)(8) of the Act,\footnote{See id. at 12–13.} which requires that the rules of a national securities exchange do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

As discussed above, the Exchange proposes to publish the stop price of SPX AIM auctions. As previously noted, according to the Exchange, orders in SPX generally take on greater risk, have a higher notional value, trade in much larger size, and effect increasingly more complex strategies than options in other classes.\footnote{See id. at 12–13.} Therefore, the Exchange believes that this proposed change may address any uncertainties market participants may have when pricing SPX responses.\footnote{See id. at 12–13.} The Exchange further states that, for SPX orders crossed on the trading floor in open outcry, market makers generally have more confidence in the pricing of their responses as the crosses start with a request for market and the trading crowd then provides a “ballpark” of the prices at which they are willing to trade, which the market maker may then use to more confidently price its responses.\footnote{See id. at 12–13.} The Exchange believes that its proposal, therefore, has been designed to incentivize continued, competitive responses to SPX electronic auctions in substantially the same manner in which responses may be
is consistent with the Act. As described above, providing potential auction responders with more information about an upcoming SPX AIM auction may encourage market participants to submit more competitive responses, particularly given the large and complex nature of orders in SPX. Accordingly, the Commission believes the Exchange’s proposal may result in increased liquidity in AIM auctions and therefore increased price improvement opportunities for SPX agency orders in the AIM auctions.

The Commission is also aware that other options exchanges currently disseminate the stop price of an agency order in similar auction mechanisms and does not believe this aspect of the proposed rule change raises any novel regulatory issues. The Commission believes that providing similar additional information in its electronic price improvement auction notification messages should make the Cboe electronic price improvement auction notification competitive with other options exchanges and encourage the submission of more responses to these auctions. For this reason, the Commission believes that the proposed rule change is also consistent with Section 6(b)(8) of the Act.

Accordingly, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change, as modified by Amendment No. 1 (SR–CBOE–2020–052), be, and hereby is, approved.

Jill M. Peterson,
Assistant Secretary.