CBOE EXECUTE SUCCESS℠

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March 18, 2016

Via Electronic Mail
Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609
rule-comments@sec.gov

Re: Response to Comment Letters Received by the Securities and Exchange Commission Regarding File No. SR-CBOE-2016-005

Dear Mr. Fields:

Chicago Board Options Exchange, Incorporated ("CBOE" or "Exchange") respectfully submits this letter in response to comments submitted to the U.S. Securities and Exchange Commission ("SEC" or "Commission") by SpiderRock EXS, LLC and SpiderRock Advisors, LLC (collectively "SpiderRock")[1] on the above-referenced rule filing.[2] For the reasons articulated in its rule filing and those that follow, CBOE believes that its proposal is consistent with the Securities Exchange Act of 1934 ("Act")[3] and that it should be approved by the Commission.

Summary of Professional Rules and Proposed Rule Change

As described in CBOE's rule filing, the U.S. options exchanges have adopted materially similar definitions of the term "Professional," which commonly refers to a person or entity that is not a broker or dealer in securities and places more than 390 orders in listed options per day on average during a calendar month for their own beneficial account(s). Whereas non-Professional "public customers" are generally exempt from transaction fees and certain surcharges and receive allocation and execution priority above equally priced competing interests of Market-Makers, broker-dealers, and other market participants, Professionals are treated akin to brokers and dealers of securities on the various exchanges with respect to the fees they pay and execution priority they receive. Similar to other U.S. options exchanges, CBOE affords certain fee- and

1 See Comments on CBOE Rulemaking from SpiderRock EXS, LLC and SpiderRock Advisors, LLC on Notice of Filing of a Proposed Rule Change Relating to Professionals (Release No. 34-77049; File No. SR-CBOE-2016-005) (February 22, 2016); available at http://www.sec.gov/comments/sr-cboe-2016-005/cboe2016005.shtml.

2 See Securities Exchange Act Release No. 77049 (February 4, 2016), 81 FR 7173 (February 10, 2016) (Notice of Filing of a Proposed Rule Change Relating to Professionals) (SR-CBOE-2016-005).

3 15 U.S.C. 78f(b).

priority-related marketplace advantages to public customers based on various business- and regulatory-related objectives, including, for example, to attract retail order flow to the Exchange and to provide competitive pricing. As the Commission has noted, fairly distinguishing among market participants to attract order flow or create more competitive markets is consistent with the Act.[4]

In its filing, the Exchange proposes to adopt new Interpretation and Policy .01 to its Professional rule relating to the counting of "orders" for Professional order counting purposes. Specifically, the Exchange seeks to make changes to the way that orders are counted for Professional order counting purposes to realign the way the Exchange distinguishes public customers from Professionals. CBOE believes that the proposed rule change will better promote the underlying objectives of it Professional rule, including, but not limited to the business-related objectives cited above.

Summary of Comment Letter Received by the SEC and Discussion

SpiderRock has submitted a comment letter to the SEC opposing the Exchange's proposed rule change in SR-CBOE-2016-005. In its comment letter, SpiderRock contests that if adopted, the Exchange's proposed rule change would restrict brokerage customers' use of certain execution strategies and eliminate priority for numbers of market participants that should be afforded execution priority above other market participants on the Exchange.[5] For the reasons that follow, the Exchange respectfully disagrees with SpiderRock's position.

Contrary to SpiderRock's view that the proposed rule change would restrict its clients from using certain types of order execution strategies, the proposed rule change would not place any additional restrictions on any market participant's ability to enter any type of order on the Exchange that is otherwise permissible under the Exchange's rules.[6] One of SpiderRock's primary objections to the Exchange's proposal is that the proposed rule change would not permit its customers to continue using "conditional basket execution techniques."[7] Throughout its comment letter, SpiderRock states numerous times that the proposed rule change would

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4 See Securities Exchange Act Release No. 59287 (January 23, 2009), 74 FR 5694, 5698-99 (January 30, 2009) (Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of the Proposed Rule Change, as Modified by Amendment Nos. 1 and 2 Thereto, Relating to Professional Account Holders) (SR-ISE-2006-026).

5 In addition to discussing the Exchange's proposal and aspects of the Exchange's Professional designation, SpiderRock deliberates on a variety of competitive and market structure-related issues in its comment letter, including, but not limited to, order flow consolidation and internalization, transaction facilitation via auction mechanisms, and the merits of customer priority in general. See, e.g., note 1 supra at pages 1-4, 8-9. With respect to the final topic of customer priority in general, SpiderRock even goes so far as to "recommend that the Commission revisit the concept of customer priority and eliminate it." See id. at page 9. To the extent that SpiderRock's comments concern overarching market structure- and market dynamics-related issues, the Exchange believes that SpiderRock's comments tread far beyond the scope of the Exchange's proposal. Accordingly, SpiderRock's arguments on these issues are not addressed in this response. Suffice it to say that the Exchange believes that further comment on these topics is inappropriate in the context of the rule filing at issue and that it respectfully disagrees with characterizations of the U.S. options markets in SpiderRock's comment letter.

6 See Rule 6.53 (Certain Types of Orders Defined).

7 See note 1 supra at page 7.

"restrict," "disallow," or "ban" the use of these types of basket-style order management strategies. The Exchange believes that these statements are misleading and simply untrue. Notably, the proposed rule change would not restrict, disallow, or ban any type of market activity or order execution strategy. Rather, the proposed rule change would change the priority status of certain market participants (in option classes in which the selected Exchange matching algorithm applies customer priority) and require payment of certain fees. Public customers and Professionals alike are free to employ these strategies on the Exchange as they see fit, the only difference being that, unlike a public customer, a Professional may not receive execution priority over broker-dealer orders and Market-Maker quotes at the same price and may incur transaction fees. Although SpiderRock customers may choose not to use conditional basket execution strategies anymore if the proposed rule change is adopted because such strategies may achieve lower percentage leg fill rates due to increased competition with broker-deal orders and Market-Maker quotes at the top of the book or because such strategies may become less profitable (due to additional transaction fees), the decision not to use conditional basket execution strategies would be a business choice of each individual customer, not an Exchange-imposed restriction. The fact that the proposed rule change may result in decreased fill rates (with respect to the percentage of legs in the basket that may fill within the desired parameters of the strategy) or increased costs (causing decreased profitability) for SpiderRock customers does not mean that SpiderRock's customers' use of conditional basket execution strategies on the Exchange would be in any way restricted, prohibited, or banned.

SpiderRock's anti-competitive arguments are similarly unfounded and have been refuted previously by the Commission in the same context. SpiderRock claims in its comment letter that the proposed rule change would strip priority from certain customers solely "by virtue of having hired a more sophisticated advisor" than other market participants.[8] Essentially, SpiderRock argues that the proposed rule change would prejudice its customers simply because they have chosen to use certain trading technologies, which are available to all market participants. The Exchange disagrees with SpiderRock's characterization of its proposal; the Exchange is not proposing to distinguish public customers from Professionals based whether they use certain trading technologies, but rather on whether they place more than 390 orders in listed options on average per day. Notably, opponents of the International Securities Exchange's ("ISE's") original Professional proposal made similar arguments in their comments to the Commission on SR-ISE-2009-026.[9] As the Commission stated in response to comments on ISE's proposal at the time, the Exchange's proposal does not limit, prohibit, or proscribe the type of technology any customer uses.[10] SpiderRock's customers could still use sophisticated technology to trade options and would not be considered Professionals so long as they place 390 orders or fewer per day on average during a calendar month for their own beneficial account(s). Under the Exchange's proposal, customers who place fewer orders than this limit may continue to receive

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8 See id. at page 7; see also id. at page 3-4.

9 See, e.g., Comments on ISE Rulemaking from Andrew Carr on Notice of Filing of Proposed Rule Change, as Modified by Amendment No. 1 Thereto, Relating to Professional Account Holders (Release No. 34-57254; File No. SR-ISE-2006-26) (March 4, 2008); available at http://www.sec.gov/comments/sr-ise-2006-26/ise200626.shtml.

10 See note 4 supra at 5700.

priority over non-customer orders and Market-Maker quotes at the same price even if they have access to sophisticated options trading technology.

SpiderRock also claims in its comment letter that the proposed rule change should not be approved because it would likely result in numbers of non-broker-dealer market participants having to compete with broker-dealers and Market-Makers without priority, which it views as unfair and anti-competitive. Whereas SpiderRock views such a result as unfair and anti-competitive, the Exchange views it just the opposite. The Exchange believes that non-broker-dealer market participants that place orders on the scale set forth under the Exchange's Professional rule, using the order counting regime in the Exchange's proposal, possess a level of sophistication that enables them to effectively compete with broker-dealer orders and Market-Maker quotes for execution opportunities.[11] For example, the Exchange does not necessarily believe that SpiderRock customers (which according to SpiderRock include "a variety of . . . hedge funds, proprietary trading firms, large bank trading desks, institutional advisors, wealth management firms, and other brokers and dealers")[12] that employ sophisticated trading algorithms to generate an average of more than one order per minute of each trading day during an entire calendar month should receive the same marketplace advantages over broker-dealers and Market-Makers that are afforded to more traditional retail investors on the Exchange. Accordingly, the Exchange disagrees with SpiderRock that its proposal is unfair or anti-competitive and, rather, believes that the proposed rule change would enhance the competitive balance of its market.

The Exchange also believes that it is within its discretion to set the parameters of its Professional rule where it sees fit based on its economic and business judgement. The Commission has recognized that order priority rules have been adopted largely as part of the exchanges' trading and business models in order to attract order flow and "create more competitive markets."[13] Moreover, the Commission has stated that decisions to grant priority and waive transaction fees for certain market participants do not necessarily place an inappropriate burden on competition and "should most reasonably be viewed as within the discretion of the Exchange, so long as the[y] . . . do not unfairly discriminate among participants."[14] Contrary to SpiderRock's position that the Exchange's proposal is unfair and anti-competitive, the Exchange believes that the proposed rule change would foster a more competitive marketplace and restore the distinction between public customers and Professionals to a place that more appropriately furthers the underlying objectives of the Exchange's Professional rule.

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11 See also note 4 supra at 5699.
12 See note 1 supra at page 1.
13 See note 4 supra at 5698.
14 See id. at 5699.

CBOE appreciates the opportunity to provide these comments. For the reasons set forth above as well as those articulated in CBOE's rule filing submission, the Exchange believes that the Commission should approve the proposed rule change as filed.

Sincerely,

William P. Wallenstein

cc: Richard Holley III (SEC)
Ronesha Butler (SEC)
Benjamin Kalish (SEC)