April 26, 2021

VIA ELECTRONIC DELIVERY

Ms. Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Securities Exchange Act Release No. 91257 (March 4, 2021), 86 FR 13769 (March 10, 2021) (SR-CBOE-2020-106)

Dear Ms. Countryman,

Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") appreciates the opportunity to respond to the questions the Securities and Exchange Commission (the "Commission") raised in the above-referenced Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as Modified by Amendment No. 1, to Amend Its Rules Regarding the Minimum Increments for Electronic Bids and Offers and Exercise Prices of Certain FLEX Options and Clarify in the Rules How the System Ranks FLEX Option Bids and Offers for Allocation Purposes (the "Order"). Specifically, the Exchange proposes to permit minimum increments and exercise prices in FLEX options submitted for electronic execution to be expressed in three decimals (if expressed in dollars) or four decimals (if expressed in percentages, which would be rounded to three decimals following the close of trading to determine the dollar amount), as well as to codify and clarify certain other provisions regarding FLEX trading (the "Proposal"):

The Exchange reiterates that it believes the Proposal is consistent with the Securities Exchange Act of 1934 (the "Act"), as it will provide investors with the ability to obtain more precise premiums and exercise prices for FLEX Options in electronic FLEX trading. Given the various trading and hedging strategies employed by investors and the importance of every penny, particularly with larger orders and orders in classes with significant notional values, this additional precision may provide them with more control over the prices at which their FLEX Orders trade and are exercised. The Proposal will also benefit investors by adding transparency regarding FLEX trading to the Rules.

Allowing Nearly Economically Equivalent FLEX Options and Non-FLEX Options

The Commission first questions whether the Proposal is consistent with the Act because it could allow FLEX Options, with decimal exercise price differences that, for all practical purposes, are insignificant as compared to the exercise price of a non-FLEX option, to gain priority over economically equivalent non-FLEX option customer orders on the book and/or trade through the

NBBO.[1] Additionally, the Commission states that the Exchange did not address the Proposal's impact on customers and market quality in the Exchange's non-FLEX options market, and thus the Proposal raises questions as to whether any potential benefit of order flow migrating from the over-the-counter ("OTC") market to the Exchange would outweigh the potential costs of orders moving from the non-FLEX options market to the less transparent FLEX options market and the impact on market quality and customer orders in the non-FLEX options market.[2]

The Exchange does not believe the Proposal raises any price protection concerns due to the possibility of having nearly economically equivalent options listed in the FLEX and non-FLEX markets. Under current Cboe Options Rules (which were previously approved by the Commission and thus deemed consistent with the Act), it is already possible for FLEX Options to be listed with exercises prices that, for all practical purposes, are nearly the same as the exercise prices of non-FLEX options (and, thus, the potential differences between the exercise prices of FLEX and non-FLEX options could be deemed "insignificant"). Specifically, exercise prices of FLEX Options may already be in penny increments,[3] while exercise prices of non-FLEX Options are generally limited to be in increments of anywhere from $0.50 to $10, depending on the underlying and premium.[4] For example, a market participant could trade a FLEX SPX Aug 3300.01 call even though a non-FLEX SPX Aug 3300 call is listed on the Exchange. Additionally, the Exchange is permitted to list options overlying the same index or an ETF tracking the same index in both the FLEX and non-FLEX markets that would be nearly economically equivalent. A market participant could trade a FLEX Aug XSP 330 call (as long as not listed as a non-FLEX option series) if the Exchange lists a non-FLEX Aug SPX 3300 call, which are economically equivalent options. In the non-FLEX market, a market participant could purchase the XSP call at a price that is through the market of the SPX option, which is economically equivalent. Further, a customer could trade a non-FLEX XSP AUG 330 option at a price that does not respect the NBBO or customers resting in the book for the SPX AUG 3300 option. Similarly, an Aug SPY 330 call may trade at a price through the market of the Aug XSP 330 call, which is economically equivalent.[5]

The Exchange, however, has observed no trading activity that indicates market participants may be trading in FLEX products as a reason to trade-through the market of, or gain priority over customers on the book in, economically equivalent (or nearly economically equivalent) non-FLEX products. For example, the Exchange compiled a dataset of all SPX FLEX series listed on the Exchange from October 14, 2019 through October 9, 2020 that matched non-FLEX series on the same expiration date, put/call, and exercise-style (a.m. v. p.m.), but had different strikes. The Exchange analyzed the difference in strike prices between FLEX and non-FLEX series to show that the risk of trading FLEX options as a substitute to avoid trading in the non-FLEX market is

---

1 See Order at 13770.

2 See id.

3 See Cboe Options Rule 4.21(b)(6).

4 See Cboe Options Rules 4.5 and 4.13.

5 The Exchange notes there are no price protections for economically equivalent options listed for trading. Trade-throughs are only prohibited for identical series, not economically equivalent series. Ultimately, while these options may be economically equivalent (or nearly economically equivalent), they are different products, and market participants price them to incorporate not only the economic and notional value, but also trading costs, which may differ for each product.

minimal, if any, because there are rarely instances in which a FLEX series has terms "almost identical" to a non-FLEX listed series. The Exchange found that 99.90% of all SPX and SPXW FLEX series created were over $1.00 away from the matching SPX/SPXW listed series strikes, and that 90.10% of these were over $100.00 away from the matching listed series strikes. The Exchange notes that the SPX/SPXW FLEX series created comprise 99.7% of all FLEX index series created. Additionally, of the negligible portion of all other FLEX index series created, approximately half were over $1.00 away from the matching listed index series strikes. The Exchange also found that 97.61% of all equity and ETP FLEX series created were over $1.00 away from the matching listed series strikes, and that 83% of these were over $10.00 away from the matching listed series strikes and 44.97% of these were over $100.00 away from the matching listed series strikes. The Exchange believes this data supports the Exchange's position that the Commission's concern that allowing FLEX Options that are nearly economically equivalent to non-FLEX Options will cause market participants to move orders from the non-FLEX market to the FLEX market is only an academic and not practical concern. Instead, the Exchange believes the data supports the Exchange's position that there is minimal (if any) risk that market participants desire or attempt to use the FLEX market as a substitute to the non-FLEX market for the purpose of gaining priority over economically equivalent non-FLEX option customer orders on the book and/or trading through the NBBO. The Exchange has no concerns that permitting exercise prices of FLEX Options to be in more discrete increments, as permitted by the Proposal, will increase the likelihood of such behavior going forward.

The Exchange believes market participants that can achieve their trading objectives in the non-FLEX market do not attempt to trade economically equivalent FLEX Options to gain priority over customers in the non-FLEX Book because there is little, if any benefit, of doing so for several reasons.

- First, the Exchange believes attempting to execute an order in the FLEX market as a substitute for the non-FLEX market may reduce execution opportunities for that order due to the smaller number of market participants that trade in the FLEX market compared to the non-FLEX market, which may make it more difficult to locate counterparties. Additionally, since there is no book in the FLEX market, there is no resting liquidity against which market participants may execute their orders. Therefore, moving orders from the non-FLEX market to the FLEX market may introduce inefficiency, as well as price and execution risk, to market participants' trading strategies given the reduced liquidity, participation, and price discovery in the FLEX market compared to the non-FLEX market.[6]

- Second, the Exchange understands that the same liquidity providers (primarily Market-Makers) that trade with market participants in the FLEX market are generally the same liquidity providers that quote and often set market prices in the non-FLEX market. A significant portion of FLEX trades are submitted to the Exchange as crossing transactions. As a result, a broker seeking execution for a FLEX order generally contacts liquidity providers that trade FLEX Options to get their best bids or offers, as applicable, for the

[6] See Sections VII and X of the ODD regarding risks associated with FLEX Options.

proposed order. Those liquidity providers, who as noted above are generally setting the non-FLEX market for the same underlying, use the same pricing tools they use in the non-FLEX market when giving their best prices to the broker for the FLEX order. Therefore, liquidity providers would generally be willing to pay or receive, as applicable, a substantially similar (if not the same) amount for a FLEX Option and an economically equivalent non-FLEX Option. This ultimately creates competition for prices in the FLEX market. The Exchange believes this process provides orders with a measure of price protection within the FLEX market and makes it unlikely a market participant could achieve better pricing for a FLEX Option that is economically equivalent (or nearly economically equivalent) to a non-FLEX Option.

- Third, if a FLEX Option with an exercise price "insignificantly different" from the exercise price of a non-FLEX Option traded through the book of that non-FLEX Option, while that would be a better price for one transaction participant, it would be a worse price for the participant on the opposite side, and thus it may be more difficult for the initiating participant to obtain an execution. For example, suppose the market for a non-FLEX Aug ABC 800 call is 10.20 – 11.00. If a market participant submitted a FLEX Order to buy an Aug ABC 800.01 call with a bid of 10.00, it is unlikely another market participant would sell at that price, given that participant could sell the practically economically equivalent non-FLEX Option series at 10.20, which would be a better price for that seller. Similarly, a participant wishing to buy the FLEX option from a liquidity provider would not necessarily be willing to pay a price above the offer of the economically equivalent non-FLEX option. The Exchange has not observed market participants attempting to trade in the FLEX market rather than the non-FLEX market for this purpose in classes in which this is possible today.

- Fourth, the Exchange believes the fees that market participants must pay in connection with their trade activity would offset any such benefit and make it financially unviable to do so. The Exchange charges a FLEX Surcharge fee for several products (including SPX, which is by far the most traded FLEX Option product on the Exchange), thus making trading in FLEX Options more expensive than in non-FLEX Options.[7] Therefore, it would make little financial sense for a market participant to trade in the FLEX market if it can trade a nearly economically equivalent product in the non-FLEX market. Rather than cause market participants to move volume from the non-FLEX market to the FLEX market, the Exchange believes the Proposal will move volume currently being executed in the OTC market to the Exchange, as the terms available in OTC are similar to the precision Cboe is seeking in the Proposal.

FLEX products are inherently different than non-FLEX products and appeal to different investor bases, as they ultimately service different products. The Exchange believes the Proposal may provide an additional trading and hedging tool to institutional investors to individual tailor certain terms of options to address their investment needs. The Exchange believes the benefits of this

[7] See Cboe Options Fees Schedule.

additional tool in the listed options market outweigh the de minimis (if any) cost of market participants using FLEX Options to trade through the markets of any nearly economically equivalent non-FLEX options. The Exchange is not aware of any negative impact on execution prices as a result of the listing of economically equivalent (or nearly economically equivalent) options on the Exchange today, nor is the Exchange aware of any data or analysis suggesting that the FLEX has been used as a substitute for the non-FLEX market as a result of the ability to list FLEX Options that are economically equivalent (or nearly economically equivalent) to standardized non-FLEX Options listed for trading on the Exchange.

By permitting FLEX Options to trade with the same exercise prices and in the same increments currently available to customized options in the OTC market, the Exchange believes the Proposal will remove impediments to and perfects the mechanism of a free and open market and a national market system by further improving a comparable alternative to the OTC market in customized options. By enhancing our FLEX trading platform to provide additional flexible terms available in the OTC market but not currently available in the listed options market, the Exchange believes it may be a more attractive alternative to the OTC market. The Exchange believes market participants benefit from being able to trade customized options in an exchange environment in several ways, including but not limited to the following: (1) enhanced efficiency in initiating and closing out positions; (2) increased market transparency; and (3) heightened contra-party creditworthiness due to the role of the OCC as issuer and guarantor of FLEX Options.

Ultimately, the Exchange believes the additional sophistication and high-touch requirements necessary to trade in the FLEX market and longer timeframe[8] to receive execution in the FLEX market compared to the non-FLEX market would minimize/eliminate any potential benefit a market participant was attempting to gain by attempting to trade FLEX Options if a non-FLEX Option was listed for trading. Additionally, as noted above, the Exchange believes the likelihood of a market participant achieving any price benefit by trading through the NBBO in the listed market is minimal (or non-existent). For these reasons, the Exchange believes the potential for a market participant to obtain any financial benefit by effecting a trade in a FLEX Option that has a practically economically equivalent non-FLEX Option listed is de minimis or non-existent. Therefore, the Exchange believes the risk of market participants using FLEX Options with slightly different strike prices (compared to the strike prices of listed non-FLEX Options) to trade through the prices available in the non-FLEX market or to bypass customer orders resting in the book is incredibly low (as noted above, data supports this assertion). As a result, the Exchange believes any potential benefits of the Proposal significantly outweigh the costs of order flow moving from the non-FLEX market to the FLEX market, as the Exchange believes any such costs to be negligible. As discussed in the Proposal, rather than cause market participants to change their order flow from non-FLEX to FLEX, the Exchange believes the Proposal will draw new volume to the Exchange from the opaque OTC market and, thus, will not cause any market fragmentation.

---

[8] In addition to it potentially taking more time to locate a counterparty to trade in FLEX, because FLEX Auctions expose orders for a minimum of three seconds, FLEX executions may take more time than non-FLEX executions (which require exposure of only one second, or less in certain auctions, including crossing auctions), which would not be practical for executions for which speed of execution is a priority.

The Exchange's surveillance program will incorporate all FLEX Options that trade with premiums and exercise prices as set forth in the Proposal. If the Exchange identifies FLEX Orders that appear to be attempts to use FLEX Options to trade through or gain priority over customers in the non-FLEX market, the Exchange may determine those orders to be inconsistent with just and equitable principles of trading in violation of Cboe Options Rule 8.1. Broker-dealers are also subject to due diligence and best execution obligations, which obligations may require broker-dealers to consider the prices of economically equivalent options when executing customer orders. The Exchange notes that market participants may currently, and currently do, execute orders (including on behalf of customers) in the premium and exercise price increments in the unregulated, opaque OTC market, where neither the Exchange nor the Commission has oversight over market participants that may be purposely trading at prices through the listed market. The Proposal may encourage these orders to be submitted to the Exchange, which could bring these orders into a regulated, transparent market and be subject to surveillance and oversight to which they are currently not subject with respect to execution of these option orders.

The Exchange notes the Commission approved a proposed rule change of NYSE American LLC ("NYSE American") to allow FLEX Options on certain ETFs to be cash-settled.[9] NYSE American is not authorized under its Rules to list non-FLEX Options on ETFs with cash-settlement – those options are all physically settled. NYSE American noted that cash-settled FLEX Options may broaden the base of investors that use FLEX Options to manage their trading and investment risk, including investors that currently trade in the OTC markets for customized options, where settlement restrictions do not apply. NYSE American further stated that cash-settled FLEX Options may encourage market makers to shift liquidity from the OTC market onto an exchange to enhance the process of price discovery.[10] The NYSE American rule change allowed cash-settled FLEX Options on certain ETFs to have the exact same expiration and exercise price as non-FLEX options on the same ETFs with physical settlement, and thus permits economically equivalent FLEX and non-FLEX Options to be listed. As a result, that proposed rule change presented the same issues related to price protection that the Proposal theoretically presents. Specifically, permitting two options – one cash-settled and one physically settled – on the same underlying ETF could have the effect of allowing cash-settled FLEX ETF options gain priority over customer orders on the book for the similar physically settled non-FLEX ETF options and also allow bypassing or trading through the NBBO. Yet, in its proposed rule change, and in the Commission approval order of that change, there was no discussion of why NYSE American's proposed rule change did not raise such a price protection issue. NYSE American merely stated that it did not believe its proposed rule change would cause fragmentation of liquidity.[11] NYSE American further stated: "[NYSE American] believes that offering innovative products flows to the benefit of the investing public. A robust and competitive market requires that exchanges respond to members' evolving needs by constantly improving their offerings. Such efforts would be stymied if exchanges were prohibited from offering

---

[9] See Securities Exchange Act Release No. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAMER-2019-38) ("NYSE American Approval Order").

[10] See Securities Exchange Act Release No. 87444 (November 1, 2019), 84 FR 60120, 60124 (November 7, 2019) (SR-NYSEAMER-2019-38). As discussed above, this is substantially similar to the purpose of the Proposal.

[11] See NYSE American Approval Order at 60123.

innovative products for reasons that are generally debated in academic literature. [NYSE American] believes that introducing cash-settled FLEX Equity Options would further broaden the base of investors that use FLEX Options to manage their trading and investment risk, including investors that currently trade in the OTC markets for customized options, where settlement restrictions do not apply."[12]

The Exchange similarly believes the Proposal will not cause a fragmentation of liquidity. The Exchange has listed FLEX Options for trading for nearly 30 years. Any such price protection and fragmentation issues would have existed since the commencement of FLEX Options trading, as discussed above. Yet, the Exchange has observed no market fragmentation or investor attempts to trade FLEX Options with the same or similar terms to gain priority over customers in the book or trade through the NBBO in the non-FLEX market. As discussed above, the Exchange believes any such risk is de minimis, as the Exchange believes there is little, if any, benefit for investors to attempt to trade in the FLEX market if economically equivalent options are otherwise available in the more liquid non-FLEX market, as it would be far more difficult to find counterparties for executions, particularly at a price outside of the non-FLEX market price. The Exchange believes any such price protection issues are academic and theoretical, as they have not manifested in nearly 30 years of FLEX trading, and should not hinder innovation efforts to address real investor demand, which may result in tangible benefits of FLEX Options to increase price transparency and discovery of options that are currently only available in the OTC market.

The Proposal is consistent with the initial purpose for which the Exchange initially proposed to adopt FLEX Options, previously approved and deemed consistent with the Act by the Commission, which is to provide investors with the benefits of trading options on a listed market versus the OTC market.[13] The Proposal seeks to expand the availability of FLEX Options in a manner consistent with that purpose. Specifically, the Proposal seeks to meet the demands of investors that currently may only obtain more precise hedging as described above through the OTC markets. The primary purpose of FLEX Options has been since their inception, and continues to be, to permit trading in options that were otherwise permissible in the OTC market to be permissible on a listed exchange, and the Proposal is consistent with that purpose. Options may currently trade in more precise prices and strikes in the OTC market than they can in the listed market. The Exchange believes it benefits the investing public to continue to enhance product offerings to evolve to constantly changing needs of investors. The Exchange believes the Proposal is an appropriate expansion of FLEX trading that will bring the same benefits to investors.

Displayed Auction Price in SAM Auctions

The Commission states the Exchange did not address whether the Proposal would increase the risk that traders participating in FLEX SAM Auctions could step ahead of other traders by amounts that are economically insignificant or its consistency with Section 6(b)(5) of the Exchange Act,

---

12 See id. at 60124.

13 See [insert cite to first FLEX approval order.]

including investor protection.[14] The Exchange does not believe the Proposal will significantly risk (if at all) the possibility that FLEX Auctions will result in economically insignificant price improvement. SAM Auctions (including FLEX SAM Auctions) may result in a 100% cross of large orders (at least 500 contracts) if there is no price improvement for the entire size of the order during the auction. Given the beneficial allocation of the cross to the initiating contra order, the Exchange believes SAM Auctions (including FLEX SAM Auctions) as structured provides adequate incentive for the initiator to provide its best price to the agency-side customer, regardless of the granularity of the price increment.

Further, because a FLEX Trader would not know the prices of other responses, the FLEX Trader could not submit a response with the purpose of increasing the prices of other responses by an economically insignificant amount. While the proposed subincrements in FLEX SAM are smaller (subpenny) than those currently available, the Exchange believes any increased potential risk the Proposal may create is outweighed by the benefits of increased opportunities for price improvement for large orders. Therefore, the Exchange believes it is beneficial to disseminate the auction price to provide market participants with a heightened opportunity to compete for the customer order and thus increase the possibility that the auction will result in price improvement.

SAM Auctions (FLEX and non-FLEX) currently permit auction prices and responses to be in subincrements compared to the standard minimum increment for the vast majority of classes (which are non-penny classes) that trade on the Exchange, and thus permit subincrement price improvement for those classes. Therefore, the risk noted by the Commission currently exists, but only for responses with respect to the auction price (and not responses with respect to each other), because the Exchange currently disseminates the auction price in SAM Auctions (FLEX and non-FLEX). In SAM and FLEX SAM Auctions, it is possible for responses to be submitted at prices only a small amount greater than the auction price. However, responses may only trade with the auctioned order if there is sufficient size at an improved price to trade with the entire order. Additionally, if a market participant responds with a price that is only slightly better than the auction price, that participant risks being allocated no part of the auctioned order since other market participants may be responding with better prices. As a result, the Exchange believes market participants will continue to respond with their most aggressive prices to maximize their chances of participating in the trade at the end of the auction.

As discussed in the Proposal, while it is possible that a FLEX Trader's response in an electronic FLEX SAM Auction may lose execution priority if the response of another FLEX Trader is better by a small amount, it is just as possible the FLEX Trader may gain execution priority by a small amount. The purpose of not displaying auction responses of other auction participants is to encourage all FLEX Traders to submit their best-priced responses.[15] With respect to larger orders, as demonstrated in the Proposal, even small price changes can create a significant price difference. The Exchange does not believe the Proposal will discourage FLEX Traders from providing liquidity to electronic FLEX SAM Auctions, because the prices of their responses will continue to not be available to other FLEX Traders to use to step ahead by a small amount (and thus

---

[14] See Order at 13771.

[15] FLEX Traders are permitted to submit multiple responses at multiple prices.

"piggyback" off of pricing done by other investors) in order to gain execution priority. The Commission itself acknowledged the difference between use of a sub-increment in the context of an auction and in the context of displayed liquidity in the book. Specifically, in response to a commenter arguing that the Commission should prohibit the Boston Options Exchange ("BOX") from using "sub-increment" pricing in its price improvement period ("PIP") auction,[16] the Commission states that it did "not believe that the PIP raise[d] the same problems caused by sub-penny quotations of non-option securities . . ." because the use of the sub-increment was in an auction rather than public quotations.[17] The Exchange notes that BOX disseminates the starting price of a PIP Auction, which is the auction with respect to which the Commission made that statement.[18]

The goal of auctions is to create price competition among those responding to auctions. Because responses will continue to not be visible to FLEX Traders that compete to trade against the order submitted into a FLEX SAM Auction, the Exchange believes the Proposal will not impact price competition in FLEX SAM Auctions.

Complexity of the Proposal

The Commission further states that the Exchange did not explain how it will ensure that bids and offers will be improved at increments that are meaningful to market participants under the Proposal and that the increased complexity created by the proposed pricing increments could have the effect of reducing participation in FLEX auctions, leading to less competitive prices.[19] The Exchange cannot ensure that bids and offers will be improved at all. It is possible for orders submitted to the Exchange, including into price improvement auctions, to receive no price improvement. Rather, the Exchange implements functionality that it believes may result in price improvement that market participants find meaningful. We believe the Proposal will continue to encourage participants to provide price improvement in a competitive manner.

FLEX participants are institutional, highly sophisticated investors, and the Exchange does not believe the Proposal will create complexity that will discourage participation in FLEX auctions. These investors already trade in these smaller increments in OTC. Additionally, most products on the Exchange trade in different increments, including FLEX Options that may compete in dollars

---

[16] BOX was permitting penny increments in this price improvement auction despite the standard increments for options being $0.05 and $0.10. See Securities Exchange Act Release No. 49068 (January 13, 2004), 69 FR 2775 (January 13, 2004) (SR-BSE-2002-15) (order approving PIP auctions that permit orders and responses be submitted into the auctions in penny increments).

[17] See Securities Exchange Act Release No. 50870, 69 FR 77423, 77459 (December 27, 2004) (proposed rules and amendments to joint industry plans). The Exchange acknowledges that it submitted a comment arguing for prohibition of the use of sub-increment pricing in BOX's PIP auction. However, the Commission approved it as being consistent with the Exchange Act (and the Exchange itself has similar price improvement auctions that permit penny pricing in options with minimum increments of $0.05 and $0.10), and the Commission disagreed with the Exchange's argument.

[18] See BOX Rule 7150(f).

[19] See Order at 13771.

or percentages. The Proposal merely permits these investors to compete with more discrete dollar or percentage amounts.

The Commission notes that the Exchange itself has acknowledged in a different context in another proposal that de minimis price improvement may discourage market participants from providing contra-side interest at the best prices and liquidity providers from joining or improving at meaningful increments.[20] The proposal to which the Commission references permitted the Exchange to modify the minimum increment in Automated Improvement Mechanism ("AIM") auctions for one single type of strategy (combo orders) in one class (SPX).[21] The Exchange intended, in that proposal, to address the fact that AIM (which historically was not available during regular trading hours for SPX) could impact market quality for combos specifically on the trading floor, where a significant number of combos are regularly represented for crossing and priced by Market-Makers on the floor in a certain manner. SPX has significant volume executed on the trading floor. As discussed in the proposal, the Exchange was concerned that permitting SPX combos to be submitted into AIM auctions with increments much smaller than the increments in which those orders generally trade on the trading floor would diminish liquidity on the trading floor given the significant number of combos that generally execute in that setting. To encourage the continued provision of liquidity on the trading floor, that proposal required AIM pricing for those combos in SPX to be the same as the pricing used on the trading floor for those combos to maintain floor liquidity. Such proposal was consistent with the initial purpose of AIM, which was to create an electronic crossing auction to handle an order in a similar manner to how such an order is handled in an open outcry crossing auction.

The Exchange submitted the Proposal within a completely different context than the prior proposal referenced by the Commission. The FLEX Option market is less liquid than the SPX market. Additionally, the Exchange has permitted FLEX Options to execute in AIM Auctions (in subincrements compared to the non-FLEX minimum increment for most classes) unlike non-FLEX SPX (until recently). Therefore, the Exchange does not believe the Proposal creates the same risk that the Exchange believed its activation of AIM for SPX Options would create. A combo order is a specific and common type of strategy that market participants price in a different manner than other orders, as discussed in that proposal. Permitting SPX AIM combo orders to trade in a significantly different increment than SPX combo orders represented on the trading floor would have created a disparity that may have impacted floor liquidity given the prevalence of combo orders. Given the nature of liquidity in the FLEX market, the Exchange does not believe the Proposal would have the same result. Therefore, the Exchange does not believe the increased pricing options could have the potential to make it harder for market participants to anticipate auction prices, which could affect market quality and decrease FLEX Options market participation. As noted above, FLEX Traders are generally institutional, highly sophisticated investors and currently execute options trades in the OTC market using the same precision pricing the Exchange is proposing to adopt for FLEX Options. As a result, the Exchange believes FLEX Traders have sufficient knowledge of the pricing of FLEX Options and, therefore, believes those market

---

[20] See Order at 13771.

[21] See Securities Exchange Act Release No. 89638 (August 21, 2020), 85 FR 53045 (August 21, 2020) (SR-CBOE-2020-052) at 36925

participants will have sufficient knowledge regarding the prices at which to submit responses to FLEX Auctions. The Proposal is intended to increase FLEX participation and liquidity and bring transparency to more options trades. By not disseminating prices of responses, the Exchange believes market participants will continue to be encouraged to submit their best-priced responses (regardless of the permissible increment).

Ranking Percentage Exercise Prices Prior to Conversion to Dollar Amounts

Finally, the Commission states the Exchange must address why it believes ranking, as proposed to be codified, is consistent with the Act.[22] The Exchange believes ranking percentage-priced premiums at the time of the auction rather than after the close of trading (when the dollar amount of the price is determined) will promote just and equitable principles of trade because it is consistent with the ranking of dollar-priced premiums. FLEX Traders are competing in auctions based on the percentage amount of their bids and offers (in the same manner they do with dollar bids and offers) and thus should be ranked based on that amount, as they do not know at the time of submitting those bids and offers to what final price they will be rounded. Like bids and offers in dollar amounts, the Exchange believes a FLEX Trader willing to pay more (or receive less) at the time of a FLEX Auction should receive priority. As long as it is possible that different percentage bids and offers could differ after the close of trading, the Exchange believes a more aggressive auction response bares the risk that the adjusted price may also be more aggressive, and the responder should be rewarded for taking on that risk by receiving a higher ranking. The Exchange believes consistency in ranking of bids and offers submitted in all FLEX Auctions (and non-FLEX Auctions) will benefit investors, and providing FLEX Traders that submit more aggressive responses with priority will encourage FLEX Traders to submit competitive responses, which ultimately benefits investors as well.

* * * * *

By permitting FLEX Options to trade with precision similar to that currently available for customized options in the OTC market, the Exchange believes the Proposal will further improve a comparable alternative to the OTC market in customized options. By enhancing our FLEX trading platform to provide additional terms available in the OTC market but not currently available in the listed options market, the Exchange believes it may be a more attractive alternative to the OTC market. The Exchange believes market participants benefit from being able to trade customized options in an exchange environment in several ways, including but not limited to the following: (1) enhanced efficiency in initiating and closing out positions; (2) increased market transparency; and (3) heightened contra-party creditworthiness due to the role of the OCC as issuer and guarantor of FLEX Options. The Exchange believes the Proposal will expand the pool of option trades that can receive these benefits with no impact on the non-FLEX market.

---

[22] See Order at 13771.

The Exchange appreciates the opportunity to respond to questions raised in the Order and urges the Commission to approve it in a timely manner. Please feel free to contact myself at [redacted] or [redacted] if you have any questions related to this matter.

Respectfully submitted,

/s/ Laura G. Dickman

Laura G. Dickman
Vice President, Associate General Counsel
Cboe Global Markets, Inc.