

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-74949; File No. SR-EDGX-2015-18)

May 13, 2015

Self-Regulatory Organizations; EDGX Exchange, Inc.; Notice of Filing of Proposed Rule Change to Establish Rules Governing the Trading of Options on the EDGX Options Exchange

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 April 30, 2015, EDGX Exchange, Inc. (the “Exchange” or “EDGX”) filed with the Securities and Exchange Commission (“SEC” or “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 filed a proposal to adopt rules to govern the trading of options on the Exchange (referred to herein as “EDGX Options Exchange” or “EDGX Options”). As described more fully below, the EDGX Options Exchange will operate a fully automated, Customer priority/pro rata allocation model. The fundamental premise of the proposal is that the Exchange will operate its options market in a similar manner to the options exchange operated by the Exchange’s affiliate, BATS Exchange, Inc. (“BZX Options”), with the exception of the proposed priority model and certain other limited differences.

The text of the proposed rule change is available at the Exchange’s website at [www.batstrading.com](http://www.batstrading.com), at the principal office of the Exchange, and at the Commission’s Public Reference Room.

---

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

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

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts 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 is proposing to adopt a series of rules in connection with EDGX Options, which will be a facility of the Exchange. EDGX Options will operate an electronic trading system developed to trade options (“System”) that will provide for the electronic display and execution of orders, as described below. All Exchange Members will be eligible to participate in EDGX Options provided that the Exchange specifically authorizes them to trade in the System. The System will provide a routing service for orders when trading interest is not present on EDGX Options, and will comply with the obligations of the Options Order Protection and Locked/Crossed Market Plan.

**EDGX Options Members**

The Exchange will authorize any Exchange Member who meets certain enumerated qualification requirements to obtain access to EDGX Options (any such Member, an “Options Member”).

There will be two basic types of Options Members, Options Order Entry Firms (“OEFs”) and Options Market Makers. Options Market Makers, in turn, will be eligible to participate as

Directed Market Makers, Primary Market Makers and Market Makers. OEFs will be those Options Members representing orders as agent on EDGX Options and non-market maker participants conducting proprietary trading as principal. Options Market Makers are Options Members registered with the Exchange as Options Market Makers.

To become an Options Market Maker, an Options Member is required to register by filing a written application with the Exchange, and then must register to make markets in individual series of options. Pursuant to proposed Rule 22.2, the Exchange may appoint one Primary Market Maker per option class. Market Makers may select from among any option issues traded on the Exchange to request appointment as a Primary Market Maker, subject to the approval of the Exchange. In considering the approval of the appointment of a Primary Market Maker in each security, the Exchange will consider: the Market Maker's preference; the financial resources available to the Market Maker; the Market Maker's experience, expertise and past performance in making markets, including the Market Maker's performance in other securities; the Market Makers [sic] operational capability; and the maintenance and enhancement of competition among Market Makers in each security in which they are registered, including pursuant to the performance standards set forth in proposed Rule 22.2(i).<sup>3</sup>

An unlimited number of Market Makers may be registered in each class unless the number of Market Makers registered to make a market in a particular option class should be limited whenever, in the Exchange's judgment, quotation system capacity in an option class or classes is not sufficient to support additional Market Makers in such class or classes. The Exchange will not restrict access in any particular option class until such time as the Exchange has submitted objective standards for restricting access to the SEC for its review and approval.

---

<sup>3</sup> The Exchange notes that proposed Rule 22.2 is based in part on BZX Options Rule 22.2 (paragraphs (a) and (b)) and in part on Amex Rule 923NY (paragraphs (c) through (i)).

EDGX Options Market Makers will be required to electronically engage in a course of dealing to enhance liquidity available on EDGX Options and to assist in the maintenance of fair and orderly markets. Among other things, an Options Market Maker would have to satisfy the following responsibilities and duties during trading: (1) on a daily basis maintain a two-sided market on a continuous basis in at least 75% of the individual options series in which it is registered; (2) engage, to a reasonable degree under the existing circumstances, in dealings for their own accounts when there exists, or it is reasonably anticipated that there will exist, a lack of price continuity, a temporary disparity between the supply of (or demand for) a particular option contract, or a temporary distortion of the price relationships between option contracts of the same class; (3) compete with other Market Makers in all series in which the Market Maker is registered to trade; and (4) maintain minimum net capital in accordance with Commission and the Exchange rules. The Exchange proposes to specify numerically the meaning of “continuous” with respect to Market Makers’ obligation to maintain continuous, two-sided quotes. For the purposes of Rule 22.6, the Exchange will consider the continuous quoting requirement fulfilled if a Market Maker provides two-sided quotes for 90% of the time the Market Maker is required to provide quotes in an appointed options series on a given trading day, or such higher percentage as the Exchange may announce in advance. Substantial or continued failure by an Options Market Maker to meet any of its obligations and duties, will subject the Options Market Maker to disciplinary action, suspension, or revocation of the Options Market Maker’s registration in one or more options series.

Options Market Makers receive certain benefits for carrying out their duties. For example, a Market Maker may be designated by the Exchange as a Primary Market Maker or may have orders directed to it in its capacity as a Directed Market Maker, in each case receiving

a priority advantage over other non-Customer orders to the extent applicable priority overlays have been implemented, as described below. In addition, a lender may extend credit to a broker-dealer without regard to the restrictions in Regulation T of the Board of Governors of the Federal Reserve System if the credit is to be used to finance the broker-dealer's activities as a specialist or market maker on a national securities exchange. Thus, an Options Market Maker has a corresponding obligation to hold itself out as willing to buy and sell options for its own account on a regular or continuous basis to justify this favorable treatment. The Exchange believes that the proposed 90% continuous quoting requirement for all Market Makers is consistent with that typically required of Primary Market Makers and market makers of similar status.

Every Options Member shall at all times maintain membership in another registered options exchange that is not registered solely under Section 6(g) of the Securities Exchange Act of 1934 or in FINRA. OEF's that transact business with customers must at all times be members of FINRA. Pursuant to proposed EDGX Rule 17.2(g), every Options Member will be required to have at least one registered Options Principal who satisfies the criteria of that Rule, including the satisfaction of a proper qualification examination. An OEF may only transact business with Public Customers if such Options Member also is an Options Member of another registered national securities exchange or association with which the Exchange has entered into an agreement under Rule 17d-2 under the Exchange Act pursuant to which such other exchange or association shall be the designated options examining authority for the OEF.

As provided in EDGX Rule 16.2, existing Exchange Rules applicable to the EDGX equity market contained in Chapters I through XV of the Exchange Rules will apply to Options Members unless a specific Exchange Rule applicable to the options market (Chapters XVI through XXIX of the Exchange Rules) governs or unless the context otherwise requires. Options

Members can therefore provide sponsored access to the EDGX Options Exchange to a nonmember (“Sponsored Participant”) pursuant to Rule 11.3 of the Exchange Rules.

### **Execution System**

The Exchange’s options trading system will leverage the Exchange’s current state of the art technology, including its customer connectivity, messaging protocols, quotation and execution engine, order router, data feeds, and network infrastructure. This approach minimizes the technical effort required for existing Exchange Members to begin trading options on the EDGX Options Exchange. The EDGX Options Exchange will closely resemble the Exchange’s affiliate, BZX Options, but will differ in that EDGX Options will maintain a pro rata allocation model with execution priority dependent on the capacity of an order (e.g., Customer or non-Customer) as well as status as a Primary Market Maker or Directed Market Maker, as applicable. The proposed model for EDGX Options is similar to other options exchanges such as NYSE Amex Options (“Amex”), the MIAX Options Exchange (“MIAX”), and other exchanges, which are sometimes referred to as “classic” exchanges.

Like the Exchange system for equities, all trading interest entered into the System will be automatically executable. Orders entered into the System will be displayed either with attribution or anonymously. The Exchange will become an exchange member of the Options Clearing Corporation (“OCC”). The System will be linked to OCC for the Exchange to transmit locked-in trades for clearance and settlement.

**Hours of Operation.** The Exchange will begin accepting orders at 8:00 a.m. Eastern Time, as described below. The options trading system will operate between the hours of 9:30 a.m. Eastern Time and 4:00 p.m. Eastern Time, with all orders being available for execution during that timeframe.

**Minimum Quotation and Trading Increments.** The Exchange is proposing to apply the following quotation increments: (1) if the options series is trading at less than \$3.00, five (5) cents; (2) if the options series is trading at \$3.00 or higher, ten (10) cents; and (3) if the options series is trading pursuant to the Penny Pilot program one (1) cent if the options series is trading at less than \$3.00, five (5) cents if the options series is trading at \$3.00 or higher, except for QQQQ, SPY, or IWM where the minimum quoting increment will be one cent for all series. In addition, the Exchange is proposing that the minimum trading increment for options contracts traded on EDGX Options will be one (1) cent for all series. The Exchange also proposes to offer trading of Mini Options, and that the minimum trading increment for Mini Options shall be the same as the minimum trading increment permitted for standard options on the same underlying security.

**Penny Pilot Program.** Upon initial operation of EDGX Options the Exchange proposes to commence trading, pursuant to the Penny Pilot Program (the “Penny Pilot”), all classes that are, on that date, traded by other options exchanges pursuant to the Penny Pilot, which is currently scheduled to expire on June 30, 2015, unless extended.

The Exchange represents that it has the necessary system capacity to support any additional series listed as part of the Penny Pilot.

The Exchange agrees to submit semi-annual reports to the Commission that will include sample data and written analysis of information collected from April 1 through September 30, and from October 1 through March 31, for each year, for the ten most active and twenty least active option classes added to the Penny Pilot. In addition, for comparison purposes, the reports include data from a control group consisting of the ten least active option classes from the initial group of 63 option classes in the program. This report will include, but is not limited to: (1) data

and written analysis on the number of quotations generated for options included in the report; (2) an assessment of the quotation spreads for the options included in the report; (3) an assessment of the impact of the Penny Pilot on the capacity of the Exchange's automated systems; (4) data reflecting the size and depth of markets; and (5) any capacity problems or other problems that arose related to the operation of the Penny Pilot and how the Exchange addressed them.

Additionally, the Exchange proposes that any Penny Pilot issues that have been delisted may be replaced on a semi-annual basis by the next most actively traded multiply listed options classes that are not yet included in the Penny Pilot, based on trading activity in the previous six months. The replacement issues, as applicable, would be added to the Penny Pilot Program on the second trading day following January 1 and July 1 of each year. The Exchange will employ the same parameters to prospective replacement issues as approved and applicable under the Penny Pilot Program, including excluding high-priced underlying securities. The replacement issues will be announced in Information Circulars distributed to Members.

**Order Types.** The proposed System will make available to Options Members the following order types: Limit Orders, Minimum Quantity Orders, Market Orders, Price Improving Orders, Book Only Orders, Post Only Orders, and Intermarket Sweep Orders, with characteristics and functionality similar to what is currently approved for use on BZX Options. Each of the proposed rules regarding the order types and order type modifiers described below is substantively identical to the applicable rule for a corresponding order type or order type modifier offered by BZX Options with the exception of the Post Only Order, to which the Exchange has proposed some substantive modification. The Exchange has also proposed minor corrections and improvements to the descriptions of the IOC and FOK time-in-force and Price Improving Orders, as compared to the corresponding BZX Options Rules. The Exchange notes

that it has not proposed initially to adopt all of the order types and order type modifiers currently offered by BZX Options.<sup>4</sup> The Exchange has not proposed to adopt any new order types or order type modifiers that are not currently offered by BZX Options.

“Limit Orders” are orders to buy or sell an option at a specified price or better. A limit order is marketable when, for a limit order to buy, at the time it is entered into the System, the order is priced at the current inside offer or higher, or for a limit order to sell, at the time it is entered into the System, the order is priced at the inside bid or lower.

“Minimum Quantity Orders” are orders that require that a specified minimum quantity of contracts be obtained, or the order is cancelled. Minimum Quantity Orders will only execute against multiple, aggregated orders if such execution would occur simultaneously. The Exchange will only honor a specified minimum quantity on a Book Only Order entered with a time-in-force designation of Immediate or Cancel and will disregard a minimum quantity on any other order.

“Market Orders” are orders to buy or sell at the best price available at the time of execution. Market Orders to buy or sell an option traded on EDGX Options will be rejected if they are received when the underlying security is subject to a “Limit State” or “Straddle State” as defined in the Plan to Address Extraordinary Market Volatility Pursuant to Rule 608 of Regulation NMS under the Act (the “Limit Up-Limit Down Plan”).<sup>5</sup> Any portion of a Market Order that would execute at a price more than \$0.50 or 5 percent worse than the national best bid and offer (“NBBO”) at the time the order initially reaches EDGX Options, whichever is greater,

---

<sup>4</sup> The Exchange has not proposed to adopt stop orders or stop limit orders, reserve orders, partial post only at limit orders or the WAIT time-in-force, each of which is offered by BZX Options.

<sup>5</sup> Securities Exchange Act Release No. 67091 (May 31, 2012), 77 FR 33498 (June 6, 2012) (order approving the Plan on a pilot basis).

will be cancelled.

“Price Improving Orders” are orders to buy or sell an option at a specified price at an increment smaller than the minimum price variation in the security. Price Improving Orders may be entered in increments as small as (1) one cent. Price Improving Orders shall be displayed at the minimum price variation in that security and shall be rounded up for sell orders and rounded down for buy orders. Unless a User<sup>6</sup> has entered instructions not to do so, Price Improving Orders will be subject to the “display-price sliding process,” as described below. The display-price sliding process is contained in proposed Rule 21.1(h).

“Book Only Orders” are orders that are to be ranked and executed on the Exchange pursuant to Rule 21.8 (Order Display and Book Processing) or cancelled, as appropriate, without routing away to another options exchange. A Book Only Order will be subject to the display-price sliding process unless a User has entered instructions not to use the display-price sliding process.

“Post Only Orders” are orders that are to be ranked and executed on the Exchange pursuant to proposed Rule 21.8 or cancelled, as appropriate, without routing away to another options exchange except that the order will not remove liquidity from the EDGX Options Book. A Post Only Order cannot be designated with instructions to use the display-price sliding process, and any such order will be rejected. A Post Only Order that is not subject to the Price Adjust process, as described below, that would lock or cross a Protected Quotation of another options exchange or the Exchange will be cancelled. The Exchange notes that Post Only Orders on BZX Options are permitted to remove liquidity under certain circumstances and can be

---

<sup>6</sup> As proposed in Rule 16.1(a)(63), the term “User” means any Options Member or Sponsored Participant who is authorized to obtain access to the System pursuant to Rule 11.3 (Access).

designated for the display-price sliding process under BZX Options Rules. The Exchange has not proposed to adopt these features.

“Intermarket Sweep Orders” or “ISOs” are orders that shall have the meaning provided in proposed Rule 27.1, which relates to intermarket trading. Such orders may be executed at one or multiple price levels in the System without regard to Protected Quotations at other options exchanges (i.e., may trade through such quotations). The Exchange relies on the marking of an order by a User as an ISO order when handling such order, and thus, it is the entering Options Member’s responsibility, not the Exchange’s responsibility, to comply with the requirements relating to ISOs. ISOs are not eligible for routing pursuant to Rule 21.9.

**Time in Force Designations.** Options Members entering orders into the System may designate such orders to remain in force and available for display and/or potential execution for varying periods of time. Unless cancelled earlier, once these time periods expire, the order (or the unexecuted portion thereof) is returned to the entering party.

“Good Til Day” or “GTD” shall mean, for orders so designated, that if after entry into the System, the order is not fully executed, the order (or the unexecuted portion thereof) shall remain available for potential display and/or execution for the amount of time during such trading day specified by the entering User unless canceled by the entering party.

“Immediate Or Cancel” or “IOC” shall mean, for an order so designated, a limit order that is to be executed in whole or in part as soon as such order is received. The portion not so executed immediately on the Exchange or another options exchange is cancelled and is not posted to the EDGX Options Book. IOC limit orders that are not designated as Book Only Orders and that cannot be executed in accordance with Rule 21.8 on the System when reaching the Exchange will be eligible for routing away pursuant to Rule 21.9.

“DAY” shall mean, for an order so designated, a limit order to buy or sell which, if not executed expires at market close.

“Fill-or-Kill” or “FOK” shall mean, for an order so designated, a limit order that is to be executed in its entirety as soon as it is received and, if not so executed, cancelled. A limit order designated as FOK is not eligible for routing away pursuant to Rule 21.9.

**One Second Exposure Period.** Proposed Rule 22.12 would prohibit Options Members from executing as principal on EDGX Options orders they represent as agent unless (i) agency orders are first exposed on EDGX Options for at least one (1) second or (ii) the Options Member has been bidding or offering on EDGX Options for at least one (1) second prior to receiving an agency order that is executable against such bid or offer. As noted above, proposed Rule 22.12 would require Options Members to expose their customers’ orders on the Exchange for at least one second under certain circumstances. During this one second exposure period, other Options Members will be able to enter orders to trade against the exposed order. In adopting a one-second order exposure period, the Exchange is proposing a requirement that is consistent with the Rules of other options exchanges, including BZX Options.<sup>7</sup> Thus, the exposure period will allow Options Members that are members of other options exchanges to comply with Rule 22.12 without programming separate time parameters into their systems for order entry or compliance purposes. The Exchange believes that market participants are sufficiently automated that a one second exposure period allows an adequate time for market participants to electronically respond to an order. Also, it is possible that market participants might wait until the end of the exposure period, no matter how long, before responding. Thus, the Exchange believes that any longer

---

<sup>7</sup> See, e.g., Chicago Board Options Exchange (“CBOE”) Rules 6.45A, 6.45B, 6.74A and 6.74B; International Securities Exchange (“ISE”) Rule 717(d); NOM Chapter VII, Sec. 12.

than one second would not further the protection of investors or market participants, but rather, would potentially increase market risk to investors and other market participants by creating a longer period of time for the exposed order to be subject to market risk.

The technology for the Exchange's trading system for EDGX Options will be comparable to the technology used for the trading system currently used for equities trading on the Exchange today. The Exchange has had ample experience with that trading system to believe that one second is an adequate exposure period. Further, the Exchange believes that many of its current Members will be Options Members and that such current Members have demonstrated an ability to respond to orders in a timely fashion.

**Match Trade Prevention Modifiers.** As is true for BZX Options, the Exchange will allow Options Members to use Match Trade Prevention ("MTP") Modifiers. Any incoming order designated with an MTP modifier will be prevented from executing against a resting opposite side order also designated with an MTP modifier and originating from the same market participant identifier ("MPID"), Exchange Member identifier, trading group identifier, or Exchange Sponsored Participant identifier.

**Re-Pricing Mechanisms.** The Exchange, like BZX Options, proposes to offer two re-pricing mechanisms for Users of EDGX Options, the display-price sliding process and the Price Adjust process. In turn, under each type of price sliding, Users will be able to select between either single price sliding or multiple price sliding. The Exchange will offer display-price sliding (including multiple display-price sliding) and Price Adjust (including multiple Price Adjust) to ensure compliance with locked and crossed market rules relevant to participation on EDGX Options. The proposed display-price sliding functionality for EDGX Options is identical to functionality for BZX Options, with the exception of language related to Post Only Order

functionality, which is not applicable. Specifically, as noted above, the Exchange omitted language regarding Post Only Orders contained in the BZX Options description of display-price sliding because the Exchange has proposed to reject orders that are designated as Post Only Orders and subject to display-price sliding. Similarly, because the Exchange has not proposed to adopt functionality that results in executions of Post Only Orders against resting liquidity under certain circumstances, the Exchange has omitted from the Exchange's proposed Price Adjust rule certain language contained in the corresponding BZX Options rule regarding such circumstances.

**Market Opening Procedures.** The System shall open options, other than index options, for trading after 9:30 a.m. Eastern Time as described below. With respect to index options, the System shall open such options for trading at 9:30 a.m. Eastern Time.

As proposed, the Exchange will accept market and limit orders and quotes for inclusion in the opening process (the "Opening Process") beginning at 8:00 am Eastern Time or immediately upon trading being halted in an option series due to the primary listing market for the applicable underlying security declaring a regulatory trading halt, suspension, or pause with respect to such security (a "Regulatory Halt") and will continue to accept market and limit orders and quotes until such time as the Opening Process is initiated in that option series (the "Order Entry Period"), other than index options. The Exchange will not accept IOC or FOK orders for queuing prior to the completion of the Opening Process. The Exchange will convert all ISOs entered for queuing prior to the completion of the Opening Process into non-ISOs.

After the first transaction on the primary listing market after 9:30 a.m. Eastern Time in the securities underlying the options as reported on the first print disseminated pursuant to an effective national market system plan ("First Listing Market Transaction") or the Regulatory Halt has been lifted, the related option series will be opened automatically as described below.

The System will determine a single price at which a particular option series will be opened (the “Opening Price”) as calculated by the System within 30 seconds of the First Listing Market Transaction or the Regulatory Halt being lifted. Where there are no contracts in a particular series that would execute at any price, the System shall open such options for trading without determining an Opening Price. After establishing an Opening Price that is also a Valid Price,<sup>8</sup> orders and quotes in the System that are priced equal to or more aggressively than the Opening Price will be matched based on the Exchange’s proposed priority rule, Rule 21.8. Matches will occur until there is no remaining volume or there is an imbalance of orders. All orders and quotes or portions thereof that are matched pursuant to the Opening Process will be executed at the Opening Price. An imbalance of orders on the buy side or sell side may result in orders that are not executed in whole or in part. Such orders will be handled in time sequence, beginning with the order with the oldest time stamp and may, in whole or in part, be placed on the EDGX Options Book, cancelled, executed, or routed in accordance with proposed Rule 21.9.

**Order Display/Matching System.** Other than the differences with respect to the market model described below, the System will be based upon technology and functionality currently approved for use in the Exchange’s equities trading system and the Exchange’s affiliate, BZX Options. Specifically, the System will allow Options Members to enter market orders and priced limit orders to buy and sell options listed on EDGX Options. The orders will be designated for display (price and size) in the order display service of the System.

**Book Processing/Priority.** After the opening, trades on the Exchange will occur when a buy order/quote and a sell order/quote match on the Exchange’s order book. The System shall execute trading interest within the System in price priority, meaning it will execute all trading

---

<sup>8</sup> Valid Price is defined in proposed Rule 21.7(a)(2).

interest at the best price level within the System before executing trading interest at the next best price. Pursuant to proposed Rule 21.8(c), after considering price priority, all orders are matched according to pro-rata priority. In addition, Customer, Primary Market Maker and/or Directed Market Maker priority overlays are also available at the Exchange's discretion on a class-by-class basis pursuant to proposed Rule 21.8(d). For example, (i) the Customer Overlay provides Customers with priority over all non-Customer interest at the same price; (ii) the Directed Market Maker overlay (which may only be in effect if the Customer Overlay is also in effect) provides the Directed Market Maker with priority over other Market Makers for a certain percentage of contracts allocated at the same price (60% or 40% depending upon the number of other Market Makers at the NBBO) and for small size orders; and (iii) the Primary Market Maker overlay (which may only be in effect if the Customer Overlay is also in effect) provides Primary Market Makers with priority over other Market Makers for a certain percentage of contracts allocated at the same price (60% or 40% depending upon the number of other Market Makers at the NBBO) and for small size orders.

After executions resulting from the Priority Overlays described above, Orders and Quotes within the System for the accounts of non-Customers, including Professional Customers, have next priority. If there is more than one highest bid or more than one lowest offer in the Consolidated Book for the account of a non-Customer, then such bids or offers will be afforded priority on a "size pro rata" basis.

In allocating the participation entitlements set forth in proposed Rule 21.8 to the Directed Market Maker and the Primary Market Maker, the following shall apply. In a class of options where both the Primary Market Maker and the Directed Market Maker participation entitlements are in effect and an Options Member has directed an order to a Directed Market

Maker: (a) if the Directed Market Maker's priority quote is at the NBBO, the Directed Market Maker's participation entitlement will supersede the Primary Market Maker's participation entitlements for an order directed to such Directed Market Maker; (b) if the Directed Market Maker's priority quote is not at the NBBO, the Primary Market Maker's participation entitlement will apply to that order, provided the Primary Market Maker's priority quote is at the NBBO; and (c) if neither the Directed Market Maker's nor the Primary Market Maker's priority quote is at the NBBO then executed contracts will be allocated in accordance with the pro-rata allocation methodology as described in paragraphs (c) and (e) above without regard to any participation entitlement. If an incoming order has not been directed to a Directed Market Maker by an Options Member, however, then the Primary Market Maker's participation entitlement will apply to that order, provided the Primary Market Maker's priority quote is at the NBBO.

As proposed and as noted above, the participation entitlements of proposed Rule 21.8 shall not be in effect unless the Customer Overlay is also in effect and the participation entitlements shall only apply to any remaining balance after Customer orders have been satisfied.

Neither the Primary Market Maker nor the Directed Market Maker may be allocated a total quantity greater than the quantity they are quoting at the execution price. If the Primary Market Maker's or the Directed Market Maker's allocation of an order pursuant to its participation entitlement is greater than its pro-rata share of priority quotes at the best price at the time that the participation entitlement is granted, neither the Primary Market Maker nor the Directed Market Maker shall receive any further allocation of that order.

In establishing the counterparties to a particular trade, the participation entitlements

must first be counted against the Primary Market Maker's highest priority bids and offers or the Directed Market Maker's highest priority bids or offers.

The proposed participation entitlements only apply to the allocation of executions among competing Market Maker priority quotes existing on the EDGX Options Book at the time the order is received by the Exchange. No market participant is allocated any portion of an execution unless it has an existing interest at the execution price. Moreover, no market participant can execute a greater number of contracts than is associated with its interest at a given price. Accordingly, the Primary Market Maker and the Directed Market Maker participation entitlements contained in the proposed Rule are not guarantees.

The Exchange believes that proposed Rule 21.8 governing priority on the Exchange is consistent with other options exchanges that have similar market models, including Amex and MIAX.<sup>9</sup>

**Routing.** The EDGX Options Exchange will support orders that are designated to be routed to the NBBO as well as orders that will execute only within EDGX Options. Orders that are designated to execute at the NBBO will be routed to other options markets to be executed when the Exchange is not at the NBBO consistent with the Options Order Protection and Locked/Crossed Market Plan. Subject to the exceptions contained in proposed Rule 27.2(b), the System will ensure that an order will not be executed at a price that trades through another options exchange. An order that is designated by an Options Member as routable will be routed in compliance with applicable Trade-Through restrictions. Any order entered with a price that would lock or cross a Protected Quotation that is not eligible for either routing, or the display-price sliding process or the Price Adjust process will be cancelled.

---

<sup>9</sup> See, e.g., Amex Rule 964NY; MIAX Rule 514.

EDGX Options shall route orders in options via BATS Trading, Inc. (“BATS Trading”), which serves as the Outbound Router of the Exchange, as defined in current Rule 2.11. The function of the Outbound Router will be to route orders in options listed and open for trading on EDGX Options to other options exchanges pursuant to EDGX Options rules solely on behalf of EDGX Options. The Outbound Router is subject to regulation as a facility of the Exchange, including the requirement to file proposed rule changes under Section 19 of the Act. Use of BATS Trading or Routing Services (as described below) to route orders to other market centers is optional. Parties that do not desire to use BATS Trading or other Routing Services provided by the Exchange must designate orders as not available for routing.

In the event the Exchange is not able to provide order routing services through its affiliated broker-dealer, the Exchange will route orders to other options exchanges in conjunction with one or more routing brokers that are not affiliated with the Exchange (“Routing Services”).

EDGX Options will offer a variety of routing options that will be identical to the routing options offered by BZX Options. Routing options may be combined with all available order types and times-in-force, with the exception of order types and times-in-force whose terms are inconsistent with the terms of a particular routing option. The System will consider the quotations only of accessible markets. The term “System routing table” refers to the proprietary process for determining the specific options exchanges to which the System routes orders and the order in which it routes them. The Exchange reserves the right to maintain a different System routing table for different routing options and to modify the System routing table at any time without notice. The proposed System routing options are Parallel D, Parallel 2D, Destination Specific and Directed ISO. The Exchange notes that Destination Specific and Directed ISO are both offered by BZX Options but that such options are currently listed in both the routing section

and the order description section. The Exchange believes that these options are more appropriately listed as routing strategies, and thus has proposed to include them in Rule 21.9.

The Exchange also proposes to offer two optional Re-Route instructions, Aggressive Re-Route and Super Aggressive Re-Route, either of which can be assigned to routable orders. Pursuant to the Aggressive Re-Route instruction, to the extent the unfilled balance of a routable order has been posted to the EDGX Options Book, should the order subsequently be crossed by another accessible options exchange, the System shall route the order to the crossing options exchange. Pursuant to the Super Aggressive Re-Route instruction, to the extent the unfilled balance of a routable order has been posted to the EDGX Options Book, should the order subsequently be locked or crossed by another accessible options exchange, the System shall route the order to the locking or crossing options Exchange.

**Data Feed; Anonymity.** The System will include a proprietary data feed, Multicast PITCH, which will display depth of book quotations and execution information based on orders received by EDGX Options using the minimum price variation applicable to that security. The Exchange will make available to all market participants through the Options Price Reporting Authority (“OPRA”) an indication that there is Customer interest included in the best bid and offer disseminated by the Exchange. The Exchange will also identify Customer orders and trades as such on messages disseminated by the Exchange through its Multicast PITCH data feed. To the extent a User has submitted an Attributable Order, which is the default property for all orders entered into the System, the Multicast PITCH data feed will indicate the User’s MPID along with the price and size of their order or quote.

The intra-day transaction reports produced by the System will indicate the details of the transactions, and will not reveal contra party identities. However, the Exchange does anticipate

generating daily, weekly and/or monthly reports containing aggregate information regarding Market Maker and Customer executions, and thus, has proposed to make clear in Rule 21.10 that such identifying information will be made available. The Exchange believes that this practice is common on other options exchanges that operate market models similar to that proposed by the Exchange.

**Risk Monitor Mechanism.** The Exchange also proposes to offer to all Users of EDGX Options the ability to establish certain risk control parameters via the Exchange's Risk Monitor Mechanism. The proposed Risk Monitor Mechanism is identical to that offered by BZX Options pursuant to Rule 21.16. The Risk Monitor Mechanism provides protection from the risk of multiple executions across multiple series of an option or across multiple options. The risk to Users is not limited to a single series in an option or even to all series of an option; Users that quote in multiple series of multiple options have significant exposure, requiring them to offset or hedge their overall positions.

In particular, the Risk Monitor Mechanism will be useful for EDGX Options Market Makers, who are required to continuously quote in assigned options. Quoting across many series in an option creates the possibility of "rapid fire" executions that can create large, unintended principal positions that expose the Market Maker to unnecessary market risk. The Risk Monitor Mechanism is intended to assist such Users in managing their market risk.

Though the Risk Monitor Mechanism will be most useful to Market Makers, the Exchange proposes to offer the functionality to all participant types. There may be other firms that trade on a proprietary basis and provide liquidity to the Exchange; these firms could potentially benefit, similarly to Market Makers, from the Risk Monitor Mechanism. The Exchange believes that the Risk Monitor Mechanism should help liquidity providers generally,

market makers and other participants alike, in managing risk and providing deep and liquid markets to investors.

### **Options Order Protection and Locked/Crossed Market Plan Rules**

The Exchange will participate in the approved Options Order Protection and Locked/Crossed Market Plan (“Plan”), and therefore will be required to comply with the obligations of Participants under the Plan. The Exchange proposes to adopt rules relating to the Plan that are substantially similar to the rules in place on all of the options exchanges that are Participants to the Plan.

The Plan replaced the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (“Old Plan”). The Old Plan required its participant exchanges to operate a stand-alone system or “Linkage” for sending order-flow between exchanges to limit trade-throughs, and the Linkage was operated by the Options Clearing Corporation (“OCC”). The Plan essentially applies the Regulation NMS price-protection provisions to the options markets. Similar to Regulation NMS, the Plan requires the Plan Participants to adopt rules “reasonably designed to prevent Trade-Throughs,” while exempting Intermarket Sweep Orders (“ISOs”) from that prohibition. The Plan’s definition of an ISO is essentially the same as under Regulation NMS. The remaining exceptions to the trade-through prohibition, discussed more specifically below, either track those under Regulation NMS or correspond to unique aspects of the options market, or both.

The Rules in proposed Chapter XXVII conform to the requirements of the Plan. Rule 27.1 sets forth the defined terms for use under the Plan. Rule 27.2 prohibits trade-throughs and exempts ISOs from that prohibition. Rule 27.2 also contains additional exceptions to the trade-through prohibition that track the exceptions under Regulation NMS or correspond to unique

aspects of the EDGX Options Exchange, or both.

Proposed Rule 27.3 sets forth the general prohibition against locking/crossing other eligible exchanges as well as several exceptions that permit locked markets in limited circumstances; such exceptions have been approved by the Commission for inclusion in the rules of other options exchanges. Specifically, the exceptions to the general prohibition on locking and crossing occur when (1) the locking or crossing quotation was displayed at a time when the Exchange was experiencing a failure, material delay, or malfunction of its systems or equipment; (2) the locking or crossing quotation was displayed at a time when there is a Crossed Market; or (3) the Member simultaneously routed an ISO to execute against the full displayed size of any locked or crossed Protected Bid or Protected Offer.

### **Securities Traded on EDGX Options**

**General Listing Standards.** The Exchange proposes to adopt listing standards for Options traded on EDGX Options (Chapter XIX) as well as for Index Options (Chapter XXIX) that are identical to the approved rules of BZX Options.<sup>10</sup> The Exchange will join the Options Listings Procedures Plan and will list and trade options already listed on other options exchanges. The Exchange will gradually phase-in its trading of options, beginning with a selection of actively traded options. At least initially, the Exchange does not plan to develop new options products or listing standards.

**\$1 Strike Program.** Pursuant to proposed Rule 19.6, Supplementary Material .02, the interval between strike prices of series of options on individual stocks may be \$1.00 or greater (“\$1 Strike Prices”) provided the strike price is \$50 or less, but not less than \$1. The listing of \$1 strike prices shall be limited to option classes overlying no more than one hundred fifty (150)

---

<sup>10</sup> See Rules of BZX Options, Chapters XIX and XXIX.

individual stocks (the “\$1 Strike Price Program”) as specifically designated by EDGX Options. As proposed, EDGX Options may list \$1 Strike Prices on any other option classes if those classes are specifically designated by other national securities exchanges that employ a similar \$1 Strike Price Program under their respective rules.

To be eligible for inclusion into the \$1 Strike Price Program, an underlying security must close below \$50 in the primary market on the previous trading day. After a security is added to the \$1 Strike Price Program, EDGX Options may list \$1 Strike Prices from \$1 to \$50 that are no more than \$5 from the closing price of the underlying on the preceding day. For example, if the underlying security closes at \$13, EDGX Options may list strike prices from \$8 to \$18. EDGX Options may not list series with \$1 intervals within \$0.50 of an existing strike price in the same series, except that strike prices of \$2, \$3, \$4, \$5 and \$6 shall be permitted within \$0.50 of an existing strike price for classes also selected to participate in the \$0.50 Strike Program. Additionally, for an option class selected for the \$1 Strike Price Program, EDGX Options may not list \$1 Strike Prices on any series having greater than nine (9) months until expiration. A security shall remain in the \$1 Strike Price Program until otherwise designated by EDGX Options.

For options classes selected to participate in the \$1 Strike Program, the Exchange will, on a monthly basis, review series that were originally listed under the \$1 Strike Program with strike prices that are more than \$5 from the current value of an options class and delist those series with no open interest in both the put and the call series having a: (1) strike higher than the highest strike price with open interest in the put and/or call series for a given expiration month; and (2) strike lower than the lowest strike price with open interest in the put and/or call series for a given expiration month. If the Exchange identifies series for delisting pursuant to this policy, the

Exchange shall notify other options exchanges with similar delisting policies regarding the eligible series for delisting, and shall work jointly with such other exchanges to develop a uniform list of series to be delisted so as to ensure uniform series delisting of multiply listed options classes.

Notwithstanding the above delisting policy, the Exchange may grant member requests to add strikes and/or maintain strikes in series of options classes traded pursuant to the \$1 Strike Program that are eligible for delisting.

In addition to \$1 strikes as proposed above, the Exchange proposes to offer options trading on series of options with \$0.50, \$2.50 and \$5.00 strike price intervals, consistent with other options exchanges, including BZX Options.

With regard to the impact on system capacity, the Exchange has analyzed its capacity and represents that it and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the listing and trading of option series that may be listed and traded in the strike price intervals described above, including \$0.50, \$1, \$2.50 and \$5.00 strikes.

**Mini Options.** After an option class on a stock, Exchange-Traded Fund Share, Trust Issued Receipt, Exchange Traded Note, and other Index Linked Security with a 100 share deliverable has been approved for listing and trading on the Exchange, the Exchange proposes to permit listing of series of option contracts with a 10 share deliverable on that stock, Exchange-Traded Fund Share, Trust Issued Receipt, Exchange Traded Note, and other Index Linked Security for all expirations opened for trading on the Exchange. Pursuant to proposed Interpretation and Policy .07 to Rule 19.6, Mini Option contracts could be listed on SPDR S&P 500 (“SPY”), Apple Inc. (“AAPL”), SPDR Gold Trust (“GLD”), Google Inc. (“GOOG”), and

Amazon.com Inc. (“AMZN”). Strike prices for Mini Options shall be set at the same level as for regular options. For example, a call series strike price to deliver 10 shares of stock at \$125 per share has a total deliverable value of \$1250 and the strike price will be set at 125. No additional series of Mini Options may be added if the underlying security is trading at \$90 or less. The underlying security must trade above \$90 for five consecutive days prior to listing Mini Options contracts in an additional expiration month.

**Quarterly Options Series Program.** Pursuant to proposed Rule 19.6, Interpretation and Policy .04 and proposed Rule 29.11(g) the Exchange may list and trade options series that expire at the close of business on the last business day of a calendar quarter (“Quarterly Options Series”). As proposed, the Exchange may list Quarterly Options Series for up to five (5) currently listed options classes that are either options on exchange traded funds (“ETF”) or index options. In addition, the Exchange may also list Quarterly Options Series on any options classes that are selected by other securities exchanges that employ a similar program under their respective rules.

The Exchange may list series that expire at the end of the next consecutive four (4) calendar quarters, as well as the fourth quarter of the next calendar year. For example, if the Exchange is trading Quarterly Options Series in the month of May 2016, it may list series that expire at the end of the second, third, and fourth quarters of 2016, as well as the first and fourth quarters of 2017. Following the second quarter 2016 expiration, the Exchange could add series that expire at the end of the second quarter of 2017.

For each class of ETF options selected for the Quarterly Options Series program, the Exchange may list strike prices within \$5 from the previous day’s closing price of the underlying security at the time of initial listing. Subsequently, the Exchange may list up to 60 additional

strike prices that are within thirty percent (30%) of the previous day's close, or more than 30% away from the previous day's close provided demonstrated customer interest exists for such series.

The Exchange has also proposed a delisting policy with respect to Quarterly Options Series in ETF options. On a monthly basis, the Exchange will review series that are outside of a range of five (5) strikes above and five (5) strikes below the current price of the ETF, and delist series with no open interest in both the call and the put series having a (1) strike higher than the highest price with open interest in the put and/or call series for a given expiration month; and (2) strike lower than the lowest strike price with open interest in the put and/or the call series for a given expiration month. Notwithstanding the delisting policy, customer requests to add strikes and/or maintain strikes in Quarterly Options Series eligible for delisting shall be granted.

The Exchange also may list Quarterly Option Series based on an underlying index pursuant to similar provisions in Rule 29.11. There are two noteworthy distinctions between the rules for listing Quarterly Options Series based on an ETF versus Quarterly Options Series based on an index. First, whereas the initial listing of Quarterly Options Series based on an underlying ETF is restricted to strike prices within \$5 from the previous day's closing price of the underlying security, the initial listing of strikes for Quarterly Options Series based on an underlying index is restricted to: (i) a price that is within thirty percent (30%) of the current index value, and (ii) no more than five strikes above and five strikes below the value of the underlying index. Second, whereas the Exchange may list up to 60 additional strike prices for each Quarterly Options Series based on an ETF, there is no firm cap on the additional listing of strikes for Quarterly Options Series based on an underlying index; rather, additional strike prices may be listed provided the new listings do not result in more than five strike prices on the same

side of the underlying index value as the new listings.

The interval between strike prices on Quarterly Options Series shall be the same as the interval for strike prices for series in that same options class that expire in accordance with the normal monthly expiration cycle.

With regard to the impact on system capacity, the Exchange has analyzed its capacity and represents that it and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the listing and trading of options series pursuant to the above-described Quarterly Options Series program.

**Short Term Option Series Program.** The Exchange plans to operate a Short-Term Options Series Program similar to other Short Term Options Programs, including that of BZX Options. Pursuant to proposed Rule 19.6, Interpretation and Policy .05 for equity options and Rule 29.11(h) for index options in, the Exchange intends to open for trading on any Thursday or Friday that is a business day (“Short Term Option Opening Date”) series of options on that class that expire on each of the next five (5) Fridays that are business days and are not Fridays in which monthly options series or Quarterly Options Series expire (“Short Term Option Expiration Dates”). As proposed, the Exchange may have no more than a total of five Short Term Option Expiration Dates. If EDGX Options is not open for business on the respective Thursday or Friday, the Short Term Option Opening Date will be the first business day immediately prior to that respective Thursday or Friday. Similarly, if EDGX Options is not open for business on the Friday that the options are set to expire, the Short Term Option Expiration Date will be the first business day immediately prior to that Friday.

As proposed, the Exchange may select up to fifty (50) option classes in which Short Term Option Series may be traded. In addition to those fifty option classes the Exchange may also list

Short Term Option Series on any option classes that are selected by other securities exchanges that employ a similar program. For each option class eligible for participation in the Short Term Option Series Program, the Exchange may open up to thirty (30) Short Term Option Series for each expiration date in that class. The Exchange may also open Short Term Option Series that are opened by other securities exchanges in option classes selected by such exchanges under their respective short term option rules.

As noted above, the remaining parameters of the proposed Short Term Options Program are identical to those of BZX Options and similar to those operated by other options exchanges.

With regard to the impact on system capacity, the Exchange has analyzed its capacity and represents that it and the Options Price Reporting Authority have the necessary systems capacity to handle the additional traffic associated with the listing and trading of option series pursuant to the Short Term Option Series Program.

#### **Conduct and Operational Rules for Options Members**

EDGX proposes to adopt rules that are nearly identical to the approved rules of other options exchanges, including BZX Options. Thus, EDGX proposes to adopt rules that are based on the rules of BZX Options regarding: Business Conduct Rules (Chapter XVIII); exercises and deliveries (Chapter XXIII); records, reports and audits (Chapter XXIV); minor rule violations (Chapter XXV); doing business with the public (Chapter XXVI); and margin (Chapter XXVIII).

The Exchange notes that certain requirements that will be applicable to Options Members are contained in other sections of the Exchange's existing Rules. For example, the Exchange has included applicable rules requiring options principal registration into proposed EDGX Rule 17.2(g) but also proposes to include reference to applicable registration requirements that are already contained in EDGX Rule 2.5. The Exchange also proposes to expand EDGX Rule 2.5 to

clearly include options principal registration. The Exchange intends to require Authorized Traders of Options Members to comply with existing Exchange registration requirements applicable to all Authorized Traders.<sup>11</sup> Accordingly, the Exchange has not proposed specific rules applicable to registration of representatives other than options principals.

As is true for BZX Options, with respect to Position Limits (Rule 18.7) and Exercise Limits (Rule 18.9), the Exchange is proposing to apply the limits established pursuant to the rules of the CBOE, although the Exchange will establish such limits for products not traded on the CBOE. By expressly incorporating an already-approved limit, the Exchange will ensure that an appropriate limit is in place at all times without the need to continually adjust its rule manually or to disrupt the operations of its Members.

### **National Market System**

The EDGX Options Exchange will operate as a full and equal participant in the national market system for options trading established under Section 11A of the Exchange Act, just as its equities market participates today. The EDGX Options Exchange will become a member of OPRA, the Options Linkage Authority (“OLA”), the Options Regulatory Surveillance Authority (“ORSA”), and the Options Listing Procedures Plan (“OLPP”).

The Exchange expects to participate in those plans on the same terms currently applicable to current members of those plans, and it expects little or no plan impact due to the fact that the Exchange’s market will operate in a manner similar to several other existing options exchanges.

### **Regulation**

The Exchange will leverage many of the structures it established to operate a national securities exchange in compliance with Section 6 of the Exchange Act. As described in more

---

<sup>11</sup> See Exchange Rule 2.5, Interpretation and Policy .01 and Exchange Rule 11.4.

detail below, there will be three elements of that regulation: (1) the Exchange will join the existing options industry agreements pursuant to Section 17(d) of the Exchange Act, as it has with respect to its equities market, (2) the Exchange's Regulatory Services Agreement ("RSA") with FINRA will govern many aspects of the regulation and discipline of Members that participate in options trading, just as it does for equities market regulation, and (3) the Exchange will perform options listing regulation, as well as authorize Options Members to trade on EDGX Options, and conduct surveillance of options trading as it does today for equities.

Section 17(d) of the Exchange Act and the related Exchange Act rules permit SROs to allocate certain regulatory responsibilities to avoid duplicative oversight and regulation. Under Exchange Act Rule 17d-1, the SEC designates one SRO to be the Designated Examining Authority, or DEA, for each broker-dealer that is a member of more than one SRO. The DEA is responsible for the financial aspects of that broker-dealer's regulatory oversight. Because EDGX Options Members also must be members of at least one other SRO, the Exchange would generally not be designated as the DEA for any of its members.

Rule 17d-2 under the Act permits SROs to file with the Commission plans under which the SROs allocate among each other the responsibility to receive regulatory reports from, and examine and enforce compliance with specified provisions of the Act and rules thereunder and SRO rules by, firms that are members of more than one SRO ("common members"). If such a plan is declared effective by the Commission, an SRO that is a party to the plan is relieved of regulatory responsibility as to any common member for whom responsibility is allocated under the plan to another SRO.

All of the options exchanges and FINRA have entered into the Options Sales Practices Agreement, a Rule 17d-2 agreement. Under this Agreement, the examining SROs will examine

firms that are common members of the Exchange and the particular examining SRO for compliance with certain provisions of the Act, certain of the rules and regulations adopted thereunder, certain examining SRO rules, and certain EDGX Options Rules. In addition, EDGX Options Rules contemplate participation in this Agreement by requiring that any Options Member also be a member of at least one of the examining SROs.

For those regulatory responsibilities that fall outside the scope of any Rule 17d-2 agreements, the Exchange will retain full regulatory responsibility under the Exchange Act. However, as noted above, the Exchange has entered into an RSA with FINRA, pursuant to which FINRA personnel operate as agents for the Exchange in performing certain of these functions. As is the case with the EDGX equities market, the Exchange will supervise FINRA and continue to bear ultimate regulatory responsibility for the EDGX Options Exchange. The Exchange intends to amend the existing RSA in order to capture certain aspects of regulation specifically applicable to EDGX Options and the regulation and discipline of Options Members.

As a member of the Intermarket Surveillance Group, the Exchange will comply with the specifications of the Consolidated Options Audit Trail System (“COATS”) in submitting data for purposes of creating a consolidated audit trail. The Exchange will also receive COATS data for purposes of its surveillance operations.

Consistent with the Exchange’s existing regulatory structure, the Exchange’s Chief Regulatory Officer shall have general supervision of the regulatory operations of EDGX Options, including responsibility for overseeing the surveillance, examination, and enforcement functions and for administering all regulatory services agreements applicable to EDGX Options. Similarly, the Exchange’s existing Regulatory Oversight Committee will be responsible for overseeing the adequacy and effectiveness of Exchange’s regulatory and self-regulatory

organization responsibilities, including those applicable to EDGX Options.

Finally, as is true with respect to equities, the Exchange, and FINRA pursuant to the RSA referenced above, will perform automated surveillance of trading on EDGX Options for the purpose of maintaining a fair and orderly market at all times. Specifically, EDGX Options will be monitored to identify unusual trading patterns and determine whether particular trading activity requires further regulatory investigation by FINRA.

In addition, the Exchange will oversee the process for determining and implementing trade halts, identifying and responding to unusual market conditions, and administering the Exchange's process for identifying and remediating "obvious errors" by and among its Options Members. EDGX proposed rules (Chapter XX) regarding halts, unusual market conditions, extraordinary market volatility, obvious errors, and audit trail are identical to the approved rules of BZX Options.<sup>12</sup>

The Exchange notes that the obvious error rule of BZX Options was recently approved<sup>13</sup> and that other options exchanges are in the process of implementing similar rules. The Exchange has not proposed any changes as compared to the recently approved obvious error rule of BZX Options. Thus, in addition to the general provisions for reviewing and handling transactions that potentially qualify for adjustment or nullification as Obvious Errors or Catastrophic Errors, the Exchange proposes to adopt Interpretation and Policy .01 to provide for how the Exchange will treat Obvious and Catastrophic Errors in response to the Limit Up-Limit Down Plan, which is applicable to all NMS stocks, as defined in Regulation NMS Rule 600(b)(47).<sup>14</sup> As proposed,

---

<sup>12</sup> See BZX Options Rules Chapter XX; see also Rules of NOM, Chapter V, and BOX, Chapter V.

<sup>13</sup> See Securities Exchange Act Release No. 74556 (March 20, 2015), 80 FR 16031 (March 26, 2015) (SR-BATS-2014-067).

<sup>14</sup> 17 CFR 242.600(b)(47).

during a pilot period to coincide with the pilot period for the Plan, including any extensions to the pilot period for the Plan, an execution will not be subject to review as an Obvious Error or Catastrophic Error pursuant to paragraph (c) or (d) of the Proposed Rule if it occurred while the underlying security was in a “Limit State” or “Straddle State,” as defined in the Plan. During a Limit or Straddle State, options prices may deviate substantially from those available immediately prior to or following such States. Thus, determining a Theoretical Price in such situations would often be very subjective, creating unnecessary uncertainty and confusion for investors. Because of this uncertainty, the Exchange is proposing to provide in Rule 20.6 that the Exchange will not review transactions as Obvious Errors or Catastrophic Errors when the underlying security is in a Limit or Straddle State.

The Exchange represents that it will conduct its own analysis concerning the elimination of the Obvious Error and Catastrophic Error provisions during Limit and Straddle States and agrees to provide the Commission with relevant data to assess the impact of this proposed rule change. As part of its analysis, the Exchange will evaluate (1) the options market quality during Limit and Straddle States, (2) assess the character of incoming order flow and transactions during Limit and Straddle States, and (3) review any complaints from Members and their customers concerning executions during Limit and Straddle States. The Exchange also agrees to provide to the Commission data requested to evaluate the impact of the inapplicability of the Obvious Error and Catastrophic Error provisions, including data relevant to assessing the various analyses noted above.

In connection with this proposal, the Exchange will provide to the Commission and the public a dataset containing the data for each Straddle State and Limit State in NMS Stocks underlying options traded on the Exchange beginning in the month during which the proposal is

approved, limited to those option classes that have at least one (1) trade on the Exchange during a Straddle State or Limit State. For each of those option classes affected, each data record will contain the following information:

- Stock symbol, option symbol, time at the start of the Straddle or Limit State, an indicator for whether it is a Straddle or Limit State.
- For activity on the Exchange:
  - executed volume, time-weighted quoted bid-ask spread, time-weighted average quoted depth at the bid, time-weighted average quoted depth at the offer;
  - high execution price, low execution price;
  - number of trades for which a request for review for error was received during Straddle and Limit States;
  - an indicator variable for whether those options outlined above have a price change exceeding 30% during the underlying stock's Limit or Straddle State compared to the last available option price as reported by OPRA before the start of the Limit or Straddle State (1 if observe 30% and 0 otherwise). Another indicator variable for whether the option price within five minutes of the underlying stock leaving the Limit or Straddle state (or halt if applicable) is 30% away from the price before the start of the Limit or Straddle State.

In addition, the Exchange shall provide to the Commission and the public assessments relating to the impact of the operation of the Obvious Error rules during Limit and Straddle States as follows: (1) Evaluate the statistical and economic impact of Limit and Straddle States

on liquidity and market quality in the options markets; and (2) Assess whether the lack of Obvious Error rules in effect during the Straddle and Limit States are problematic. The timing of this submission would coordinate with Participants' proposed time frame to submit to the Commission assessments as required under Appendix B of the Plan. The Exchange notes that the pilot program is intended to run concurrent with the pilot period of the Plan, which currently expires to October 23, 2015. The Exchange proposes to reflect this date in the Proposed Rule.

### **Minor Rule Violation Plan**

The Exchange's disciplinary rules, including Exchange Rules applicable to "minor rule violations," are set forth in Chapter VIII of the Exchange's current Rules. Such disciplinary rules will apply to Options Members and their associated persons.

The Commission approved the EDGX Exchange's Minor Rule Violation Plan ("MRVP") in 2010.<sup>15</sup> The Exchange's MRVP specifies those uncontested minor rule violations with sanctions not exceeding \$2,500 that would not be subject to the provisions of Rule 19d-1(c)(1) under the Act<sup>16</sup> requiring that an SRO promptly file notice with the Commission of any final disciplinary action taken with respect to any person or organization.<sup>17</sup> The Exchange's MRVP includes the policies and procedures included in Exchange Rule 8.15 (Imposition of Fines for

---

<sup>15</sup> See Release No. 34-62036 (May 5, 2010), 75 FR 26822 (May 12, 2010) (File No. 4-594) ("MRVP Order").

<sup>16</sup> 17 CFR 240.19d-1(c)(1).

<sup>17</sup> The Commission adopted amendments to paragraph (c) of Rule 19d-1 to allow SROs to submit for Commission approval plans for the abbreviated reporting of minor disciplinary infractions. See Release No. 34-21013 (June 1, 1984), 49 FR 23828 (June 8, 1984). Any disciplinary action taken by an SRO against any person for violation of a rule of the SRO which has been designated as a minor rule violation pursuant to such a plan filed with and declared effective by the Commission will not be considered "final" for purposes of Section 19(d)(1) of the Act if the sanction imposed consists of a fine not exceeding \$2,500 and the sanctioned person has not sought an adjudication, including a hearing, or otherwise exhausted his administrative remedies.

Minor Violation(s) of Rules) and in Rule 8.15, Interpretation and Policy .01.

The Exchange proposes to amend its MRVP and Rule 8.15, Interpretation and Policy .01 to include proposed Rule 25.3 (Penalty for Minor Rule Violations).<sup>18</sup> The rules included in proposed Rule 25.3 as appropriate for disposition under the Exchange's MRVP are: violations of applicable Position Limit and Exercise Limit rules; order entry violations regarding restrictions on orders entered by Market Makers; violations of Market Maker continuous bid and offer rules; violations of rules applicable to expiring exercise declarations; and violations of Exchange requirements to provide trade data. The rules included in Rule 25.3 are the same as the rules included in the MRVPs of BZX Options and other options exchanges.<sup>19</sup>

Upon implementation of this proposal, the Exchange will include the enumerated options trading rule violations in the Exchange's standard quarterly report of actions taken on minor rule violations under the MRVP. The quarterly report includes: the Exchange's internal file number for the case, the name of the individual and/or organization, the nature of the violation, the specific rule provision violated, the sanction imposed, the number of times the rule violation has occurred, and the date of disposition.

Although the Exchange has not proposed fees for EDGX Options in connection with this proposal, the Exchange does anticipate filing a separate proposal prior to the launch of EDGX Options to establish applicable fees. The Exchange notes that pursuant to both the Act and existing Exchange Rule 15.1, the Exchange has the authority to prescribe dues, fees, assessments and other charges (collectively, "Fees") so long as such Fees are equitably allocated, reasonable

---

<sup>18</sup> In the MRVP Order, the Commission noted that the Exchange proposed that any amendments to Rule 8.15.01 made pursuant to a rule filing submitted under Rule 19b-4 of the Act would automatically be deemed a request by the Exchange for Commission approval of a modification to its MRVP. See MRVP Order, *supra* note 15, at note 5.

<sup>19</sup> See BZX Options Rule 25.3; see also, NOM, Chapter X, Section 7, and BOX, Chapter X, Section 2.

and not unreasonably discriminatory.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with the provisions of the Act,<sup>20</sup> in general and with Section 6(b)(5) of the Act,<sup>21</sup> in particular, in that it is designed 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

As described above, the fundamental premise of the proposal is that the Exchange will operate its options market in a similar manner to its affiliated options exchange, BZX Options, with the exception of the priority model and certain other limited differences. The Exchange believes that EDGX Options will benefit individual investors, options trading firms, and the options market generally. The entry of an innovative, low-cost competitor such as EDGX Options will promote competition, spurring existing markets to improve their own execution systems and reduce trading costs.

The basis for the majority of the rules of EDGX Options are [sic] the approved rules of BZX Options, which have already been found to be consistent with the Act. For instance, the Exchange does not believe that any of the proposed order types or order type functionality raise any new or novel issues that have not previously been considered. Thus, the Exchange further believes that the functionality that it proposes to offer is consistent with Section 6(b)(5) of the

---

<sup>20</sup> 15 U.S.C. 78a et seq.

<sup>21</sup> 15 U.S.C. 78f(b)(5).

Act,<sup>22</sup> because the System is designed to be efficient and its operation transparent, thereby facilitating transactions in securities, removing impediments to and perfecting the mechanism of a free and open market and a national market system. As noted above, the Exchange will participate in the approved Options Order Protection and Locked/Crossed Market Plan, and therefore will be required to comply with the obligations of Participants under the Plan.

Similarly, the Exchange proposes to adopt initial and continued listing standards for equity and index options that are substantially similar to the listing standards adopted by BZX Options and other options exchanges. The Exchange has also proposed to adopt rules that are substantially similar to those of BZX Options with respect to the Penny Pilot Program and various other strike price programs, including the program regarding the listing of \$0.50, \$1, \$2.50 and \$5.00 strikes, the Quarterly Options Series Program and the Short Term Options Series program. The Exchange believes that general consistency amongst options exchanges with respect to the series of options available for listings and trading is consistent with Section 6(b)(5) of the Act,<sup>23</sup> in particular, in that it is designed 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 by avoiding unnecessary confusion.

The Exchange believes that the rules of EDGX Options as well as the proposed method of monitoring for compliance with and enforcing such rules is also consistent with the Act, particularly Sections 6(b)(1), 6(b)(5) and 6(b)(6) of the Act, which require, in part, that an

---

<sup>22</sup> 15 U.S.C. 78f(b)(5).

<sup>23</sup> 15 U.S.C. 78f(b)(5).

exchange have the capacity to enforce compliance with, and provide appropriate discipline for, violations of the rules of the Commission and of the exchange.<sup>24</sup> The Exchange has proposed to adopt rules necessary to regulation Options Members that are nearly identical to the approved Rules of BZX Options as well as numerous other options exchanges. The Exchange proposes to regulate activity on EDGX Options in the same way it regulates activity on its equities market, specifically through various Exchange specific functions, an RSA with FINRA, as well as participation in industry plans, including plans pursuant to Rule 17d-2 under the Exchange Act.

More specifically, the Exchange's MRVP, as proposed to be amended, is also consistent with Sections 6(b)(1), 6(b)(5) and 6(b)(6) of the Act, which require, in part, that an exchange have the capacity to enforce compliance with, and provide appropriate discipline for, violations of the rules of the Commission and of the exchange.<sup>25</sup> In addition, because amended Rule 8.15 will offer procedural rights to a person sanctioned for a violation listed in proposed Rule 25.3, the Exchange will provide a fair procedure for the disciplining of members and associated persons, consistent with Section 6(b)(7) of the Act.<sup>26</sup> The proposal to include the rules listed in proposed Rule 25.3 in the Exchange's MRVP is also consistent with the public interest, the protection of investors, or otherwise in furtherance of the purposes of the Act, as required by Rule 19d-1(c)(2) under the Act,<sup>27</sup> because it should strengthen the Exchange's ability to carry out its oversight and enforcement responsibilities as an SRO in cases where full disciplinary proceedings are unsuitable in view of the minor nature of the particular violation.

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

---

<sup>24</sup> 15 U.S.C. 78f(b)(1), 78f(b)(5) and 78f(b)(6).

<sup>25</sup> 15 U.S.C. 78f(b)(1), 78f(b)(5) and 78f(b)(6).

<sup>26</sup> 15 U.S.C. 78f(b)(7).

<sup>27</sup> 17 CFR 240.19d-1(c)(2).

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange operates in an intensely competitive global marketplace for transaction services. Relying on its array of services and benefits, the Exchange competes for the privilege of providing market services to broker-dealers. The Exchange's ability to compete in this environment is based in large part on the quality of its trading systems, the overall quality of its market and its attractiveness to the largest number of investors, as measured by speed, likelihood and cost of executions, as well as spreads, fairness, and transparency.

The Exchange notes that most U.S. options exchanges are owned and operated by companies that operate more than one options exchange.<sup>28</sup> The primary reason to operate multiple options exchanges, as is true with respect to the proposed launch of EDGX Options, is that it allows an exchange operator to offer multiple market models, including a price-time market and a pro rata market, often with Customer priority as a critical component of the latter. Accordingly, the proposed rule change is intended to enhance competition by allowing the Exchange to compete with existing options exchanges that operate models based on Customer priority and pro rata allocations.

The proposed rule change will reduce overall trading costs and increase price competition, both pro-competitive developments, and will promote further initiative and innovation among market centers and market participants.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

---

<sup>28</sup> The IntercontinentalExchange Group, Inc. ("ICE") operates two options exchanges, Amex and Arca; NASDAQ OMX Group, Inc. operates three options exchanges, NOM, Phlx and NASDAQ OMX BX; International Securities Exchange Holding, Inc. operates two options exchanges, ISE and ISE Gemini; and CBOE Holdings operates two options exchanges, CBOE and C2 Options Exchange.

Written comments were neither solicited nor received.

### 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 e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-EDGX-2015-18 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-EDGX-2015-18. This file number should be included on the subject line if e-mail 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; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-EDGX-2015-18 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>29</sup>

Robert W. Errett  
Deputy Secretary

---

<sup>29</sup> 17 CFR 200.30-3(a)(12).