

# SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-102977; File No. SR-Phlx-2025-20]

## Self-Regulatory Organizations; Nasdaq PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Phlx's FLEX Floor Trading

May 2, 2025

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 22, 2025, Nasdaq PHLX LLC ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Options 8, Section 34, FLEX Trading.<sup>3</sup>

The text of the proposed rule change is available on the Exchange's Website at <https://listingcenter.nasdaq.com/rulebook/phlx/rulefilings>, at the principal office of the Exchange, and at the Commission's Public Reference Room.

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

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

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

<sup>3</sup> Phlx Options 8, Section 34 rule text was previously amended by two rule changes which are effective, but not yet operative. See Securities Exchange Act Release Nos. 97658 (June 7, 2023), 88 FR 38562 (June 13, 2023) (SR-Phlx-2023-22); and 100321 (June 12, 2024), 89 FR 51580 (June 18, 2024) (SR-Phlx-2024-24). Phlx further delayed the implementation so that it could implement SR-Phlx-2023-22 while also completing an OCC industry rule change prior. These two prior rule changes will be implemented at the same time as the rule changes proposed herein.

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 aspects of such statements.

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

1. Purpose

The Exchange proposes to amend Options 8, Section 34, FLEX Trading. The Exchange also proposes a technical amendment to Options 8, Section 33, Accommodation Transactions.

FLEX Options are customized equity, index, and currency contracts that allow investors to tailor contract terms for exchange-listed equity and index options. By way of background, in 2023, the Exchange filed a rule change to amend the manner in which FLEX Options are transacted on Phlx’s Trading Floor.<sup>4</sup> Thereafter, the Exchange filed to delay the implementation of SR-Phlx-2023-22 to on or before August 30, 2024.<sup>5</sup> Finally, in 2024, Phlx filed a rule change

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<sup>4</sup> See Securities Exchange Act Release No. 97658 (June 7, 2023), 88 FR 38562 (June 13, 2023) (SR-Phlx-2023-22) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Various Options 8 Rules) (“SR-Phlx-2023-22”). SR-Phlx-2023-22 amended FLEX Orders in 3 ways. First, the Exchange amended the rules to require FLEX Orders to be reported into Phlx’s Options Floor Based Management System or “FBMS,” thereby further automating the execution and reporting of FLEX Options. All executed FLEX contracts will be reported to OPRA and sent to the OCC for clearing, similar to all other equity, equity index and U.S. dollar-settled foreign currency options orders executed on the Exchange’s trading floor. Second, the Exchange removed its RFQ process including the BBO Improvement Interval Process, with the rule change. Third, the Exchange reorganized Options 8, Section 34 to restructure the rule to include additional information which describes current FLEX trading on Phlx. With respect to Cabinet Orders, SR-Phlx-2023-22 amended Options 8, Section 33 to require Cabinet Orders to be reported into FBMS. With this change, members and member organizations will be required to record all Cabinet Orders represented in the trading crowd into FBMS. All executed contracts will be reported to OPRA and sent to OCC for clearing similar to all other equity, equity index and U.S. dollar-settled foreign currency options orders executed on the Exchange’s trading floor.

<sup>5</sup> See Securities Exchange Act Release No. 98919 (November 13, 2023), 88 FR 80363 (November 13, 2023) (SR-Phlx-2023-48) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Delay the Implementation of the FLEX and Cabinet Automation).

to amend FLEX Options rules at Options 8, Section 34(b) and further delay the implementation of SR-Phlx-2023-22 to the end of Q4 2025.<sup>6</sup> At this time, the Exchange proposes to further amend the rules proposed in SR-Phlx-2023-22 and SR-Phx-2024-24, which are immediately effective, but not yet operative. The Exchange proposes to implement the amendments in Phlx-2023-22 and SR-Phx-2024-24 at the same time as the proposed amendments.

Specifically, the Exchange proposes to (1) clarify the Options 8, Section 34 functionality that will be available with the implementation of SR-Phlx-2023-22 and SR-Phx-2024-24; (2) list p.m.-settled FLEX Index Options that expire on or within two business days of a third Friday-of-the-month expiration day for a non-FLEX Option; and (3) permit FLEX Options on certain Exchange-Traded Funds (“ETFs”) to be settled by delivery in cash if the underlying security meets prescribed criteria. Each change will be described below.

### **Options 8, Section 34**

First, the Exchange proposes to capitalize certain terms uniformly throughout Options 8, Section 34. The Exchange proposes to capitalize the following terms: “FLEX Options,” “FLEX Equity Options,” “FLEX Index Options,” and “FLEX Currency Options.” The Exchange proposes to amend Options 8, Section 34(f)(4) to define FLEX U. S. dollar-settled foreign currency options as “FLEX Currency Options.” The Exchange is also underlying [sic] certain text in Options 8, Section 34(k)(2) that appeared deleted in SR-Phlx-2023-22 due to a missing bracket after the (h).

Second, the Exchange proposes to relocate the exclusion of iShares Bitcoin Trust ETF

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<sup>6</sup> See Securities Exchange Act Release No. 100321 (June 12, 2024), 89 FR 51580 (June 18, 2024) (SR-Phlx-2024-24) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Delay Implementation of Certain Exchange Options 8 Rules and Amend Options 8, Section 34(b)). Phlx further delayed the implementation so that it could implement SR-Phlx-2023-22 while also completing an OCC industry rule change prior.

(“IBIT”), the Fidelity Wise Origin Bitcoin Fund; the ARK21Shares Bitcoin ETF, the Grayscale Bitcoin Trust (BTC), the Grayscale Bitcoin Mini Trust BTC, and the Bitwise Bitcoin ETF from trading as a FLEX Options from Options 8, Section 34(a) to Options 8, Section 34(e). The language in Options 8, Section 34(a) currently states, “The Exchange will not authorize for trading a FLEX Option on iShares Bitcoin Trust ETF, the Fidelity Wise Origin Bitcoin Fund; the ARK21Shares Bitcoin ETF, the Grayscale Bitcoin Trust (BTC), the Grayscale Bitcoin Mini Trust BTC, and the Bitwise Bitcoin ETF.” This non-substantive amendment is intended to place the exception in the Permissible Series paragraph for ease of locating any exceptions.

Third, the Exchange proposes to relocate current Options 8, Section 34(f)(1)(B) to (f)(1)(A) and state, “an underlying equity security or index, as applicable (the index multiplier for FLEX Index Options is 100);”. This proposed rule text reflects the current characteristics of underlying interest for FLEX Option. The proposed rule text brings greater clarity to the Rule.

Fourth, the Exchange proposes to amend the language in Options 8, Section 34(f)(3) which was initially amended to state, “The Exchange may determine the smallest increment for exercise prices of FLEX Options not to exceed two decimal places.” While not substantively amending the exercise price, the Exchange proposes to amend this sentence to state, “The Exchange may determine the smallest increment for exercise prices of FLEX Options on a class-by-class basis without going lower than the \$0.01.” The Exchange believes that the proposed rule text brings greater clarity to Phlx’s rule text and is consistent with rule text in Cboe Rule 5.3(e)(3).<sup>7</sup> Also, this rule text is identical to ISE Options 3A, Section 3(c)(6).<sup>8</sup>

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<sup>7</sup> Of note, the Exchange is not proposing to provide for Micro FLEX Index Options or to allow prices to be expressed as a percentage value, similar to Cboe, because the Exchange does not offer these features today.

<sup>8</sup> ISE received approval to trade FLEX on November 22, 2024. See also Securities Exchange Release Act No. 101720 (November 22, 2024), 89 FR 94986 (November 29, 2024) (SR-ISE-2024-12).

Fifth, the Exchange proposes to amend the language in Options 8, Section 34(f)(5) to provide, “The expiration date may be any business day (specified to the day, month, and year) no more than 15 years from the date on which an executed FLEX equity and index option is submitted to the System and no more than 3 years from the date on which an executed FLEX currency option is submitted to the System with exercise settlement value on the expiration date determined by reference to the reported level of the index as derived from the opening prices of the component securities (“a.m. settlement”) or closing prices (“p.m. settlement”).”<sup>9</sup> This amendment aligns the rule text related to settlement style required for a complex FLEX Order leg with rule text in Cboe 4.21(b)(4) and ISE Options 3A, Section 3(c). The Exchange notes that Cboe received approval of its pilot program that permitted it to list p.m.-settled FLEX Index Options that expire on or within two business days of a third Friday-of-the-month expiration day for a non-FLEX Option (“FLEX PM Third Friday Options”).<sup>10</sup> Consistent with the Commission’s approval of Cboe’s proposal, the Exchange is proposing to allow the listing of FLEX PM Third Friday Options on Phlx as well, and will align with Cboe Rule 4.21(b)(5)(B)(ii).<sup>11</sup>

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<sup>9</sup> The Exchange would remove the rule text in current Options 8, Section 34 (f)(5) that provides, “except that (i) a FLEX index option that expires on or within two business days prior or subsequent to a third Friday-of-the-month expiration day for a non-FLEX option (except quarterly expiring index options) or underlying currency may only have an.”

<sup>10</sup> See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) (“FLEX Settlement Pilot Approval”). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission’s Division of Economic and Risk Analysis (“DERA”) staff. See FLEX Settlement Pilot Approval, notes 18 and 35.

<sup>11</sup> The only broad-based indexes option that would be able to list as a FLEX PM Third Friday Option is the Nasdaq-100 Index option (“NDX” or “NDX options”) and options based on 1/100 the value of the Nasdaq-100 (“XND” or “XND options”). The Exchange notes that Cboe lists both NDX and XND electronic FLEX options today pursuant to a license agreement with Nasdaq. Phlx received approval to permit the listing of a third-Friday-of-the-month p.m. expiration on NDX and XND options its standardized market. See Securities Exchange Act Release No. 98950 (November 15, 2023), 88 FR 81172 (November 21, 2023) (SR-Phlx-2023-45) (Order Approving a Proposed Rule Change To Permit the Listing and Trading of P.M.-Settled Nasdaq-100 Index Options With a Third-Friday-of-the-Month Expiration).

Sixth, the Exchange proposes to re-style Options 8, Section 34(f)(6) to change the title from “Settlement” to “Settlement type.” The Exchange also proposes to add a title at (A), “FLEX Equity Options.” At proposed Options 8, Section 34(f)(6)(A)(1) the Exchange proposes to add rule text to state, “FLEX Equity Options, other than as permitted in subparagraph (2) below, are settled with physical delivery of the underlying security.” The Exchange proposes to also introduce FLEX Equity Options that are cash-settled in proposed Options 8, Section 34(f)(6)(A)(2). The Exchange will discuss cash-settled FLEX Equity Options in greater detail below.

The Exchange proposes to amend Options 8, Section 34(f)(6)(B) to add a title for FLEX Index Options at (B) and change the current rule text<sup>12</sup> to instead provide that the settlement value for FLEX Index Options may be specified based on the index value reported at the:

(1) close with exercise settlement value determined by reference to the reported level of the index derived from the reported closing prices of the component securities (“P.M.-settled”);

(2) opening of trading on the Exchange with exercise settlement value determined by reference to the reported level of the index derived from the reported opening prices of the component securities (“A.M.-settled”).

While not substantively amending the rule text, the Exchange believes that the proposed text adds clarity by noting how the exercise value is determined depending on whether the option is a.m.-settled or p.m.-settled. The Exchange proposes to add a title “FLEX Currency Options” to new Options 8, Section 34(f)(6)(C). The Exchange also proposes a technical amendment to underline “Market Maker” in Options 8, Section 34(g)(3). SR-Phlx-2023-22 inadvertently did

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<sup>12</sup> Initially, the Exchange stated at Options 8, Section 34(f)(6)(A) that “respecting FLEX index options, the settlement value may be specified as the index value reported at the: (i) close (P.M.-settled); and (ii) opening (A.M.-settled) of trading on the Exchange. American style index options exercised prior to the expiration date can only settle based on the closing value on the exercise date. FLEX index options are settled in U.S. dollars.”

not underline that text, thereby designating it as new text. The Exchange proposes to remove the following rule text currently in Options 8, Section 34(f)(6)(B), “American style index options exercised prior to the expiration date can only settle based on the closing value on the exercise date.” This language is not necessary as American Style Options are defined in Options 1, Section 1(b)(3) to mean an option contract that may be exercised at any time from its commencement until its expiration. The definition is not needed in this rule. The Exchange also relocated the rule text in Options 8, Section 34(f)(6)(B) that stated, “FLEX index options are settled in U.S. dollar” to the beginning of that section.

Seventh, the Exchange proposes to amend Position Limits in Options 8, Section 34(i) to add a new paragraph stating that,

There shall be no position limits for FLEX Equity Options, other than as set forth in this paragraph and (4) below. Position limits for FLEX Equity Options where the underlying security is an ETF that is settled in cash pursuant to subparagraph (f)(6)(A) shall be subject to the position limits set forth in Options 9, Section 13, and subject to the exercise limits set forth in Options 9, Section 15. Positions in such cash-settled FLEX Options shall be aggregated with positions in physically-settled non-FLEX options on the same underlying ETF for the purpose of calculating the position limits set forth in Options 9, Section 13, and the exercise limits set forth in Options 9, Section 15.

The Exchange will describe position limits for cash-settled FLEX Equity Options on an ETF below with the description of its proposal to permit a cash-settled ETF.

The Exchange proposes to remove certain numbering as unnecessary in proposed Options 8, Section 34(i)(2), which is currently Options 8, Section 34(i)(1). The Exchange would create a new Options 8, Section 34(i)(2) and title it “Reports.” The Exchange would remove “However” from this new paragraph and start the paragraph with “Each.”

The Exchange proposes to add the title “Additional Margin Requirements” to proposed Options 8, Section 34(i)(3).

The Exchange proposes to amend proposed Options 8, Section 34(i)(3), current Options

8, Section 34(i)(3), by renumbering it to “(4)” and adding a title “Aggregation of FLEX Positions.” Further, the Exchange proposes to note that, “For purposes of the position limits and reporting requirements set forth in this Rule, FLEX Option positions shall not be aggregated with positions in non-FLEX Options other than as noted in this subparagraphs (i)(1) and (i)(4)(a)-(c), and positions in FLEX Index Options on a given index shall not be aggregated with options on any stocks included in the index or with FLEX Index Option positions on another index.”<sup>13</sup>

Pursuant to proposed Options 8, Section 34(i)(4)(a), commencing at the close of trading two business days prior to the last trading day of the calendar quarter, positions in P.M.-settled FLEX Index Options (i.e., the settlement value for FLEX Index Options is derived from closing prices on the expiration date)<sup>14</sup> shall be aggregated with positions in Quarterly Options Series on the same index with the same expiration and shall be subject to the position limits set forth in Options 4A, Section 6.<sup>15</sup> Pursuant to proposed Options 8, Section 34(i)(4)(b), commencing at the close of trading two business days prior to the last trading day of the week, positions in FLEX Index Options that are cash settled<sup>16</sup> shall be aggregated with positions in Short Term Option Series on the same underlying (e.g., same underlying index as a FLEX Index Option) with the same means for determining exercise settlement value (e.g., opening or closing prices of the underlying index) and same expiration, and shall be subject to the position limits set forth in

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<sup>13</sup> The Exchange also proposes to change “shall” to “will” in two places in this paragraph.

<sup>14</sup> The Exchange is amending this provision to reflect the current practice with respect to p.m.-settled Index Options, including FLEX Index Options. Phlx Options 4A, Section 12(a)(6) provides that P.M.-settled standard index options have an exercise settlement value that is derived from closing prices on the expiration day. The Exchange notes that a similar amendment will be made to ISE Options 3A, Section 18(c)(1) in a separate rule change.

<sup>15</sup> See Cboe Rule 8.35(d)(1) for materially identical provisions. See also ISE Options 3A, Section 18(c)(1) for identical rule text.

<sup>16</sup> The Exchange notes that all FLEX Index Options will be cash settled. Cash-settled FLEX Equity Options ETFs will be described later in this proposal.



Options 4A, Section 6.<sup>17</sup> Pursuant to proposed Options 8, Section 34(i)(4)(c), as long as the options positions remain open, positions in FLEX Options that expire on a third Friday-of-the-month expiration day shall be aggregated with positions in non-FLEX Options on the same underlying, and shall be subject to the position limits set forth in Options 4A, Section 6, or Options 9, Section 13, as applicable, and the exercise limits set forth in Options 9, Section 15, as applicable.<sup>18</sup>

Eighth, the Exchange proposes to amend Exercise Limits in Options 8, Section 34(j) to provide further detail and rearrange the rule text. The Exchange proposes to relocate the rule text in Options 8, Section 34(j)(1) that provides, “Positions in FLEX options shall not be taken into account when calculating exercise limits for non-FLEX options, except as provided in paragraph (d) above. The minimum exercise size shall be the lesser of \$1 million underlying equivalent value for FLEX index options, and 25 contracts for FLEX equity and currency options, or the remaining size of the position.” Instead, the Exchange proposes to provide at Options 8, Section 34(j)(1)(a) that, “The minimum value size for FLEX Equity Options and FLEX Currency Options exercises shall be 25 contracts or the remaining size of the position, whichever is less.” Proposed Options 8, Section 34(j)(1)(b) will require that the minimum value size for FLEX Index Options exercises be \$1 million Underlying Equivalent Value (as defined below) or the remaining Underlying Equivalent Value of the position, whichever is less.<sup>19</sup> Proposed Options 8, Section 34(j)(1)(c) will stipulate that except as provided in proposed

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<sup>17</sup> This is based on Cboe Rule 8.35(d)(2), except the Exchange does not currently list Credit Default Options and will therefore not incorporate the applicable portion into its proposed rule. See also ISE Options 3A, Section 18(c)(2) for identical text.

<sup>18</sup> See Cboe Rule 8.35(d)(3) for materially identical provisions. See also ISE Options 3A, Section 18(c)(3) for identical text.

<sup>19</sup> See Cboe Rule 8.42(g)(2) for materially identical provisions. See also ISE Options 34A, Section 19(a)(2) for identical text.

subparagraph (i) and (i)(4) above,<sup>20</sup> FLEX Options shall not be taken into account when calculating exercise limits for non-FLEX Option contracts.<sup>21</sup> Proposed Options 8, Section 34(j)(1)(d) will set forth the definition of Underlying Equivalent Value as the aggregate value of a FLEX Index Option (index multiplier times the current index value) multiplied by the number of FLEX Index Options.<sup>22</sup> Finally, the Exchange proposes to add a sentence to the end of Options 8, Section 34(j) that provides, “There shall be no exercise limits for broad-based FLEX Index Options (including reduced value option contracts) on the broad-based indexes listed in Options 4A, Section 6(a).”

### **Options 8, Section 33**

The Exchange also proposes to make a technical amendment to Options 8, Section 33, Accommodation Transactions, at paragraph (e) to remove correct improperly placed parentheticals from SR-Phlx-2024-22.

### **Cash-Settled FLEX Equity Options on Exchange Traded Funds (“ETFs”)**

Generally, FLEX Equity Options will be settled by physical delivery of the underlying security,<sup>23</sup> while all FLEX Index Options will be settled by delivery in cash.<sup>24</sup> The Exchange proposes to allow FLEX Equity Options where the underlying security is an ETF to be settled by delivery in cash if the underlying security meets prescribed criteria. The Exchange notes that

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<sup>20</sup> As described above, proposed Options 8, Section 34(i)(4) will govern the aggregation of FLEX positions generally, while proposed Options 8, Section 34(i)(1) will govern the aggregation of cash-settled FLEX Equity Options specifically and that positions in such cash-settled FLEX Equity Options will be aggregated with positions in physically settled options on the same underlying ETF. Cash-settled FLEX Equity Options will be discussed later in this filing.

<sup>21</sup> See Cboe Rule 8.42(g)(3) for materially identical provisions. See also ISE Options 3A, Section 19(a)(3) for identical text.

<sup>22</sup> See Phlx Options 8, Section 34(b)(8)(D) for materially identical provisions.

<sup>23</sup> See proposed Options 8, Section 34(f)(6)(A)(1).

<sup>24</sup> See proposed Options 8, Section 34(f)(6)(A)(2). As discussed below, cash settlement is also permitted in the OTC market.

cash-settled FLEX ETF Options will be subject to the same trading rules and procedures described in Options 8, Section 34 that will govern the trading of other FLEX Options on the Exchange. Today, NYSE American Rule 903G,<sup>25</sup> Cboe Rule 4.21(b)(5)(A)<sup>26</sup> and ISE Options 3A, Section 3(c)(5)(A)<sup>27</sup> allow for cash-settled FLEX ETF Options as well. The Exchange's proposed rule changes for cash-settled ETF Options will be based on NYSE American Rule 903G, Cboe Rule 4.21(b)(5)(A) and ISE Options 3A, Section 3(c)(5)(A).

The Exchange proposes rule text in Options 8, Section 34(f)(6)(A)(2) to provide that for FLEX Equity Options with an underlying security that is an ETF that has an average daily notional value of \$500 million or more and a national average daily volume of at least 4,680,000 shares,<sup>28</sup> measured over the prior 6-month period,<sup>29</sup> settlement may be settled by physical delivery of the underlying security or by delivery in cash.

The Exchange also proposes in Options 8, Section 34(f) that a FLEX Equity Option overlying an ETF (cash- or physically-settled) may not be the same type (put or call) and may not have the same exercise style, expiration date, and exercise price as a non-FLEX Equity

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<sup>25</sup> See Securities Exchange Act Release No. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAmer-2019-38) (Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Allow Certain Flexible Equity Options To Be Cash Settled).

<sup>26</sup> Cboe also filed an immediately effective rule change to allow certain FLEX Options to be cash settled. See Securities Exchange Act Release No. 98044 (August 2, 2023), 88 FR 53548 (August 8, 2023) (SR-Cboe-2023-036) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Allow Certain Flexible Exchange Equity Options To Be Cash Settled).

<sup>27</sup> See also Securities Exchange Release Act No. 101720 (November 22, 2024), 89 FR 94986 (November 29, 2024) (SR-ISE-2024-12) (Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Adopt Rules To List and Trade FLEX Options).

<sup>28</sup> See Cboe Rule 4.21(b)(5)(A)(ii) for materially identical provisions.

<sup>29</sup> As noted below, the Exchange plans to conduct the bi-annual review on January 1 and July 1 of each year. As such, the six-month periods will be from January to June, and from July to December each year.

Option overlying the same ETF.<sup>30</sup> In other words, regardless of whether a FLEX Equity Option overlying an ETF is cash or physically settled, at least one of the exercise style (i.e., American-style or European-style), expiration date, and exercise price of that FLEX Option must differ from those terms of a non-FLEX Option overlying the same ETF in order to list such a FLEX Equity Option. For example, suppose a non-FLEX SPY option (which is physically settled, p.m.-settled and American-style) with a specific September expiration and exercise price of 475 is listed for trading. A FLEX Trader could not submit an order to trade a FLEX SPY option that is cash-settled (or physically settled) and American-style with the same September expiration and exercise price of 475.

In addition, the Exchange proposes new Options 8, Section 34(f)(6)(A)(2)(a), which would provide that the Exchange will determine bi-annually the underlying ETFs that satisfy the notional value and trading volume requirements in subparagraph (2) by using trading statistics for the previous six-month period.<sup>31</sup> The Exchange will permit cash settlement as a contract term on no more than 50 underlying ETFs that meet the criteria in subparagraph (2). If more than 50 ETFs satisfy the notional value and trading volume requirements, the Exchange will select the top 50 ETFs that have the highest average daily volume.<sup>32</sup>

Proposed new Options 8, Section 34(f)(6)(A)(2)(b) would further provide that if the

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<sup>30</sup> See introductory paragraph of Cboe Rule 4.21(b) for materially identical provisions. All non-FLEX Equity Options (including on ETFs) are physically settled. Note all FLEX and non-FLEX Equity Options (including ETFs) are p.m.-settled.

<sup>31</sup> See proposed Options 8, Section 34(f)(6)(A)(2)(b), which is based on Cboe Rule 4.21(b)(5)(A)(ii)(a). The Exchange plans to conduct the bi-annual review on January 1 and July 1 of each year. As such, the six-month periods will be from January to June, and from July to December each year. The results of the bi-annual review will be announced via an Options Trader Alert and any new securities that qualify would be permitted to have cash settlement as a contract term beginning on February 1 and August 1 of each year. If the Exchange initially begins listing cash-settled FLEX Equity Options on a different date (e.g., September 1), it would initially list securities that qualified as of the last bi-annual review (e.g., the one conducted on July 1).

<sup>32</sup> See proposed Options 8, Section 34(f)(6)(A)(2)(a), which is based on Cboe Rule 4.21(b)(5)(A)(ii)(a).

Exchange determines pursuant to the review conducted under paragraph (2)(a) of this Rule that an underlying ETF ceases to satisfy the criteria in subparagraph (2)(a) of this Rule, any new position overlying such ETF entered into will be required to have exercise settlement by physical delivery and any open cash-settled FLEX ETF Option positions may be traded only to close the position.<sup>33</sup>

The Exchange believes it is appropriate to introduce cash settlement as an alternative contract term to the select group of ETFs because they are among the most highly liquid and actively traded ETF securities. As described more fully below, the Exchange believes that the deep liquidity and robust trading activity in the ETFs identified by the Exchange as meeting the criteria mitigate against historic concerns regarding susceptibility to manipulation.

#### *Characteristics of ETFs*

ETFs are funds that have their value derived from assets owned. The net asset value (“NAV”) of an ETF is a daily calculation that is based off the most recent closing prices of the assets in the fund and an actual accounting of the total cash in the fund at the time of calculation. The NAV of an ETF is calculated by taking the sum of the assets in the fund, including any securities and cash, subtracting out any liabilities, and dividing that by the number of shares outstanding.

Additionally, each ETF is subject to a creation and redemption mechanism to ensure the price of the ETF does not fluctuate too far away from its NAV -- which mechanisms the Exchange believes reduce the potential for manipulative activity. Each business day, ETFs are required to make publicly available a portfolio composition file that describes the makeup of

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<sup>33</sup> See proposed Options 8, Section 34(f)(6)(A)(2)(b), which is based on Cboe Rule 4.21(b)(5)(A)(ii)(b). If a listing is closing only, pursuant to Options 4, Section 4(a), opening transactions by Market Makers executed to accommodate closing transactions of other market participants are permitted.

their creation and redemption “baskets” (i.e., a specific list of names and quantities of securities or other assets designed to track the performance of the portfolio as a whole). ETF shares are created when an Authorized Participant,<sup>34</sup> typically a market maker or other large institutional investor, deposits the daily creation basket or cash with the ETF issuer. In return for the creation basket or cash (or both), the ETF issues to the Authorized Participant a “creation unit” that consists of a specified number of ETF shares. For instance, IWM is designed to track the performance of the Russell 2000 Index. An Authorized Participant will purchase all the Russell 2000 constituent securities in the exact same weight as the index prescribes, then deliver those shares to the ETF issuer. In exchange, the ETF issuer gives the Authorized Participant a block of equally valued ETF shares, on a one-for-one fair value basis. This process can also work in reverse. A redemption is achieved when the Authorized Participant accumulates a sufficient number of shares of the ETF to constitute a creation unit and then exchanges these ETF shares with the ETF issuer, thereby decreasing the supply of ETF shares in the market.

The principal, and perhaps most important, feature of ETFs is their reliance on an “arbitrage function” performed by market participants that influences the supply and demand of ETF shares and, thus, trading prices relative to NAV. As noted above, new ETF shares can be created and existing shares redeemed based on investor demand; thus, ETF supply is open-ended. This arbitrage function helps to keep an ETF’s price in line with the value of its underlying portfolio, i.e., it minimizes deviation from NAV. Generally, in the Exchange’s view, the higher the liquidity and trading volume of an ETF, the more likely the price of the ETF will not deviate from the value of its underlying portfolio, making such ETFs less susceptible to price

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<sup>34</sup> “Authorized Participant” means a member or participant of a clearing agency registered with the Commission, which has a written agreement with the exchange-traded fund or one of its service providers that allows the authorized participant to place orders for the purchase and redemption of creation units. See SEC Rule 6c-11(a)(1).

manipulation.

*Trading Data for the ETFs Proposed for Cash Settlement*

The Exchange believes that average daily notional value is an appropriate proxy for selecting underlying securities that are not readily susceptible to manipulation for purposes of establishing a settlement price. Average daily notional value considers both the trading activity and the price of an underlying security. As a general matter, the more expensive an underlying security's price, the less cost-effective manipulation could become. Further, manipulation of the price of a security encounters greater difficulty the more volume that is traded. To calculate average daily notional value (provided in the table below), the Exchange summed the notional value of each trade for each symbol (i.e., the number of shares times the price for each execution in the security) and divided that total by the number of trading days in the six-month period (from June 1, 2024 through January 1, 2025) reviewed by the Exchange.

Further, the Exchange proposes that qualifying ETFs also meet an ADV standard. The purpose for this second criteria is to prevent unusually expensive underlying securities from qualifying under the average daily notional value standard while not being one of the most actively traded securities. The Exchange believes an ADV requirement of 4,680,000 shares a day is appropriate because it represents average trading in the underlying ETF of 200 shares per second. While no security is immune from all manipulation, the Exchange believes that the combination of average daily notional value and ADV as prerequisite requirements would limit cash settlement of FLEX ETF Options to those underlying ETFs that would be less susceptible to manipulation in order to establish a settlement price.

The Exchange believes that the proposed objective criteria would ensure that only the most robustly traded and deeply liquid ETFs would qualify to have cash settlement as a contract

term. As provided in the table below, from June 1, 2024 through January 1, 2025, the Exchange would be able to provide cash settlement as a contract term for FLEX ETF Options on 43 underlying ETFs, as only this group of securities would currently meet the requirement of \$500 million or more average daily notional value and a minimum ADV of 4,680,000 shares. The table below provides the list of the 43 ETFs that, for the period covering June 1, 2024 through January 1, 2025, would be eligible to have cash settlement as a contract term.<sup>35</sup>

<b>Symbol</b>	<b>Security Name</b>	<b>Average Daily Notional Value (in dollars) (6/1/24 – 1/1/25)</b>	<b>Average Daily Volume (in shares) (6/1/24 – 1/1/25)</b>
AGG	iShares Core U.S. Aggregate Bond ETF	\$808,194,739.75	8,159,744.00
BIL	SPDR Bloomberg 1-3 Month T-Bill ETF	\$668,214,176.18	7,295,621.00
EEM	iShares MSCI Emerging Markets ETF	\$1,196,012,849.70	27,259,213.00
EFA	iShares MSCI EAFE ETF	\$913,104,330.98	11,503,196.00
EMB	iShares JPMorgan USD Emerging Markets Bond ETF	\$519,976,132.45	5,703,324.00
EWZ	iShares MSCI Japan ETF	\$574,349,879.69	20,807,973.00
FXI	iShares MSCI Brazil ETF	\$1,539,357,273.49	50,493,372.00
GDX	VanEck Gold Miners ETF	\$746,379,655.25	19,509,726.00
GLD	SPDR Gold Shares	\$1,541,653,631.78	6,490,081.00
HYG	iShares iBoxx \$ High Yield Corporate Bond ETF	\$2,723,491,055.11	34,489,565.00
<del>IBIT</del>	<del>iShares Bitcoin Trust</del>	<del>\$1,659,299,733.28</del>	<del>37,749,329.00</del>
IEF	iShares 7-10 Year Treasury Bond ETF	\$693,171,900.95	7,236,292.00

<sup>35</sup> The Exchange notes that for the period covering June 1, 2024 to January 1, 2025 the iShares Bitcoin Trust ETF (IBIT) meets the requirements of \$500 million or more average daily notional value and a minimum ADV of 4,680,000 shares. IBIT is not listed in the above table because as discussed above, the Exchange prohibits FLEX trading on IBIT options.



IEFA	iShares Core MSCI EAFE ETF	\$548,015,922.16	7,418,222.00
IVV	iShares Core S&P 500 ETF	\$3,187,859,024.25	5,519,115.00
IWM	iShares Russell 2000 ETF	\$6,488,562,445.58	29,367,233.00
IYR	iShares U.S. Real Estate ETF	\$517,310,602.25	5,312,072.00
KRE	SPDR S&P Regional Banking ETF	\$848,057,189.53	14,491,828.00
KWEB	KraneShares CSI China Internet ETF	\$662,016,207.20	21,406,471.00
LQD	Shares iBoxx \$ Investment Grade Corporate Bond ETF	\$2,742,822,293.24	24,887,127.00
MSTU	T-Rex 2X Long MSTR Daily Target ETF	\$682,394,963.59	11,775,427.00
NVDL	GraniteShares 2x Long NVDA Daily ETF	\$1,324,631,298.53	20,697,044.00
QQQ	Invesco QQQ Trust	\$16,164,306,968.91	33,284,939.00
RSP	Invesco S&P 500 Equal Weight ETF	\$1,079,569,216.48	6,151,579.00
SGOV	iShares 0-3 Month Treasury Bond ETF	\$521,472,061.40	5,190,380.00
SLV	iShares Silver Trust	\$548,250,701.76	19,612,185.00
SMH	VanEck Semiconductor ETF	\$1,753,218,476.35	7,207,552.00
SOXL	Direxion Daily Semiconductor Bull 3x Shares	\$3,007,198,965.72	85,315,964.00
SOXS	Direxion Daily Semiconductor Bear 3x Shares	\$1,227,212,654.16	52,816,849.00
SPY	SPDR S&P 500 ETF Trust	\$27,831,313,813.49	48,952,050.00
SQQQ	ProShares UltraPro Short QQQ ETF	\$1,353,608,018.34	130,517,916.00
TLT	iShares 20+ Year Treasury Bond ETF	\$3,684,141,591.91	39,147,976.00
TNA	Direxion Daily Small Cap Bull 3X Shares	\$740,041,950.49	16,703,439.00
TQQQ	ProShares UltraPro QQQ	\$3,658,741,627.49	50,944,211.00
TSL	Direxion Daily TSLA Bull 2X Shares	\$1,034,795,626.07	62,340,588.00

VCIT	Vanguard Intermediate-Term Corp Bond Idx Fund ETF	\$514,517,213.57	6,272,369.00
VOO	Vanguard S&P 500 ETF	\$2,975,793,273.23	5,659,792.00
XBI	SPDR S&P Biotech ETF	\$787,292,481.73	8,079,838.00
XLE	Energy Select Sector SPDR Fund	\$1,229,618,238.99	13,670,996.00
XLF	Financial Select Sector SPDR Fund	\$1,774,349,746.62	38,499,533.00
XLI	Industrial Select Sector SPDR Fund	\$1,046,361,996.67	7,937,499.00
XLK	Technology Select Sector SPDR Fund	\$1,057,017,686.45	4,719,572.00
XLP	Consumer Staples Select Sector SPDR Fund	\$791,212,649.82	9,807,343.00
XLU	Utilities Select Sector SPDR Fund	\$786,241,506.05	10,225,418.00
XLV	Health Care Select Sector SPDR Fund	\$1,052,717,556.59	7,088,605.00

The Exchange believes that permitting cash settlement as a contract term for FLEX ETF Options for the ETFs in the above table would broaden the base of investors that use FLEX Equity Options to manage their trading and investment risk, including investors that currently trade in the OTC market for customized options, where settlement restrictions do not apply.

The Exchange notes that the SEC has previously approved a rule filing of another exchange that allowed for the trading of cash-settled options<sup>36</sup> and, specifically, cash-settled FLEX ETF Options (which the Exchange proposes to list in the same manner as that

<sup>36</sup> See, e.g., PHLX FX Options traded on Nasdaq PHLX and S&P 500® Index Options traded on Cboe Options Exchange. The Commission approved, on a pilot basis, the listing and trading of RealDay™ Options on the SPDR S&P 500 Trust on the BOX Options Exchange LLC (“BOX”). See Securities Exchange Act Release No. 79936 (February 2, 2017), 82 FR 9886 (February 8, 2017) (“RealDay Pilot Program”). The RealDay Pilot Program was extended until February 2, 2019. See Securities Exchange Act Release No. 82414 (December 28, 2017), 83 FR 577 (January 4, 2018) (SR-BOX-2017-38). The RealDay Pilot Program was never implemented by BOX. See also Securities Exchange Act Release Nos. 56251 (August 14, 2007), 72 FR 46523 (August 20, 2007) (SR-Amex-2004-27) (Order approving listing of cash-settled Fixed Return Options (“FROs”)); and 71957 (April 16, 2014), 79 FR 22563 (April 22, 2014) (SR-NYSEMKT-2014-06) (Order approving name change from FROs to ByRDs and re-launch of these products, with certain modifications.

exchange).<sup>37</sup>

Today, equity options are settled physically at The Options Clearing Corporation (“OCC”), i.e., upon exercise, shares of the underlying security must be assumed or delivered. Physical settlement may possess certain risks with respect to volatility and movement of the underlying security at expiration against which market participants may need to hedge. The Exchange believes cash settlement may be preferable to physical delivery in some circumstances as it does not present the same risk. If an issue with the delivery of the underlying security arises, it may become more expensive (and time consuming) to reverse the delivery because the price of the underlying security would almost certainly have changed. Reversing a cash payment, on the other hand, would not involve any such issue because reversing a cash delivery would simply involve the exchange of cash. Additionally, with physical settlement, market participants that have a need to generate cash would have to sell the underlying security while incurring the costs associated with liquidating their position as well as the risk of an adverse movement in the price of the underlying security.

With respect to position and exercise limits, cash-settled FLEX ETF Options would be subject to the position limits set forth in proposed Options 8, Section 34(i). Accordingly, the Exchange proposes to add Options 8, Section 34(i)(1), which would provide that position limits for cash-settled FLEX Equity Options where the underlying security is an ETF pursuant to Options 8, Section 34(f)(6)(A)(2) shall be subject to the position limits set forth in Options 9,

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<sup>37</sup> See Securities Exchange Act Release Nos. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAMER-2019-38) (Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, to Allow Certain Flexible Equity Options To Be Cash Settled); 97231 (March 31, 2023), 88 FR 20587 (April 6, 2023) (SR-NYSEAMER-2023-22) (Notice of Filing and Immediate Effectiveness of Proposed Change to Make a Clarifying Change to the Term Settlement Style Applicable to Flexible Exchange Options); and 98044 (August 2, 2023), 88 FR 53548 (August 8, 2023) (SR-Cboe-2023-036) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Allow Certain Flexible Exchange Equity Options To Be Cash Settled).

Section 13, and subject to the exercise limits set forth in Options 9, Section 15.<sup>38</sup> The proposed rule would further state that positions in such cash-settled FLEX Equity Options shall be aggregated with positions in physically settled non-FLEX options on the same underlying ETF for the purpose of calculating the position limits set forth in Options 9, Section 13 and the exercise limits set forth in Options 9, Section 15.<sup>39</sup> The Exchange further proposes to add in Options 8, Section 34(i)(1) a cross-reference to subparagraph (f)(6)(A), as subparagraph (i)(1) would also contain provisions about position limits for FLEX Equity Options that would be exceptions to the first sentence in this paragraph stating that FLEX Equity Options have no position limits. The Exchange also proposes to add in paragraph (i)(4), a cross-reference to proposed subparagraphs (i)(1) and (i)(4)(a) - (c) as the proposed rule adds language regarding aggregation of positions for purposes of position limits, which will be covered by paragraph (i)(4). Given that there are established position and exercise limits applicable to physically settled options on each of the underlying ETFs for which cash-settled FLEX ETF options would be available under this proposal, the Exchange believes it is appropriate for the same position and exercise limits to apply to those cash settled FLEX ETF options. Accordingly, of the 43 FLEX ETF Options underlying securities that would currently be eligible to have cash settlement as a FLEX contract term, 30 would have a position limit of 250,000 contracts pursuant to Options 9,

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<sup>38</sup> The Exchange proposes to add to proposed Options 8, Section 34(i)(1) a cross reference to proposed subparagraph (f)(6)(A), as proposed Section 34(i)(1) also contains provisions about position limits for FLEX Equity Options that would be exceptions to the statement in proposed Section (i)(1) that FLEX Equity Options have no position limits (in addition to the language in proposed 34(i)(1)). The Exchange also proposes to add to proposed Options 8, Section 34(i)(4) a cross-reference to proposed subparagraph (i)(1), as the proposed rule adds language regarding aggregation of positions for purposes of position limits, which will be covered in proposed Section 34(i)(4).

<sup>39</sup> See proposed Options 8, Section 34(i)(1), which is based on Cboe Rule 8.35(c)(1)(B). The aggregation of position and exercise limits would include all positions on physically settled FLEX and non-FLEX Options on the same underlying ETFs.

Section 13(d)(5).<sup>40</sup> Further, pursuant to Supplementary Material .01 to Options 9, Section 13, six would have a position limit of 500,000 contracts (EWZ, TLT, HYG, XLF, LQD, and GDX); four (EEM, FXI, IWM, and EFA) would have a position limit of 1,000,000 contracts; one (QQQ) would have a position limit of 1,800,000 contracts; and one (SPY) would have a position limit of 3,600,000.<sup>41</sup>

The Exchange understands that cash-settled ETF options are currently traded in the OTC market by a variety of market participants, e.g., hedge funds, proprietary trading firms, and pension funds.<sup>42</sup> These options are not fungible with the exchange listed options. The Exchange believes some of these market participants would prefer to trade comparable instruments on an exchange, where they would be cleared and settled through a regulated clearing agency. The Exchange expects that users of these OTC products would be among the primary users of exchange-traded cash-settled FLEX ETF Options. The Exchange also believes that the trading of cash-settled FLEX ETF Options would allow these same market participants to better manage the risk associated with the volatility of underlying equity positions given the enhanced liquidity that an exchange-traded product would bring.

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<sup>40</sup> Options 9, Section 13(d)(5) provides that to be eligible for the 250,000 contract limit, either the most recent six (6) month trading volume of the underlying security must have totaled at least 100 million shares or the most recent six-month trading volume of the underlying security must have totaled at least seventy-five (75) million shares and the underlying security must have at least 300 million shares currently outstanding. Further as noted above, options on IBIT will not be available for FLEX trading.

<sup>41</sup> These were based on position limits as of January 28, 2025. Position limits are available on at <https://www.theocc.com>. Position limits for ETFs are always determined in accordance with the Exchange's Rules regarding position limits.

<sup>42</sup> As noted above, other options exchanges have received approval to list certain cash-settled FLEX ETF Options. See Securities Exchange Act Release No. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAmer-2019-38) (Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Allow Certain Flexible Equity Options To Be Cash Settled). Cboe also filed an immediately effective rule change to allow certain FLEX Options to be cash settled. See Securities Exchange Act Release No. 98044 (August 2, 2023), 88 FR 53548 (August 8, 2023) (SR-Cboe-2023-036) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Allow Certain Flexible Exchange Equity Options To Be Cash Settled).

In the Exchange’s view, cash-settled FLEX ETF Options traded on the Exchange would have three important advantages over the contracts that are traded in the OTC market. First, as a result of greater standardization of contract terms, exchange-traded contracts should develop more liquidity. Second, counter-party credit risk would be mitigated by the fact that the contracts are issued and guaranteed by OCC. Finally, the price discovery and dissemination provided by the Exchange and its members would lead to more transparent markets. The Exchange believes that its ability to offer cash-settled FLEX ETF Options would aid it in competing with the OTC market and at the same time expand the universe of products available to interested market participants. The Exchange believes that an exchange-traded alternative may provide a useful risk management and trading vehicle for market participants and their customers. Further, the Exchange believes listing cash-settled FLEX ETF Options would provide investors with competition on an exchange platform, as other options exchanges have received Commission approval to list the same options.<sup>43</sup>

The Exchange notes that OCC has received approval from the Commission for rule changes that will accommodate the clearance and settlement of cash-settled ETF options.<sup>44</sup> The Exchange has analyzed its capacity and represents that it has the necessary systems capacity to handle the additional traffic associated with the listing of cash-settled FLEX ETF Options. Also, the Exchange understands that The Options Price Reporting Authority (“OPRA”) has the necessary capacity as the products are already trading on OPRA today. The Exchange believes any additional traffic that would be generated from the introduction of cash-settled FLEX ETF Options would be manageable. The Exchange expects that members will not have a capacity

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<sup>43</sup> See supra notes 25-27.

<sup>44</sup> See Securities Exchange Act Release No. 34-94910 (May 13, 2022), 87 FR 30531 (May 19, 2022) (SR-OCC-2022-003).

issue as a result of this proposed rule change. The Exchange also does not believe this proposed rule change will cause fragmentation of liquidity. The Exchange will monitor the trading volume associated with the additional options series listed as a result of this proposed rule change and the effect (if any) of these additional series on market fragmentation and on the capacity of the Exchange's automated systems.

The Exchange does not believe that allowing cash settlement as a contract term would render the marketplace for equity options more susceptible to manipulative practices. The Exchange believes that manipulating the settlement price of cash-settled FLEX ETF Options would be difficult based on the size of the market for the underlying ETFs that are the subject of this proposed rule change. The Exchange notes that each underlying ETF in the table above is sufficiently active to alleviate concerns about potential manipulative activity. Further, in the Exchange's view, the vast liquidity in the 43 underlying ETFs that would currently be eligible to be traded as cash-settled FLEX options under the proposal ensures a multitude of market participants at any given time. Moreover, given the high level of participation among market participants that enter quotes and/or orders in physically settled options on these ETFs, the Exchange believes it would be very difficult for a single participant to alter the price of the underlying ETF or options overlying such ETF in any significant way without exposing the would-be manipulator to regulatory scrutiny. The Exchange further believes any attempt to manipulate the price of the underlying ETF or options overlying such ETF would also be cost prohibitive. As a result, the Exchange believes there is significant participation among market participants to prevent manipulation of cash-settled FLEX ETF Options.

Still, the Exchange believes it has an adequate surveillance program in place and intends to apply the same program procedures to cash-settled FLEX ETF Options that it applies to the

Exchange's other options products.<sup>45</sup> FLEX options products and their respective symbols will be integrated into the Exchange's existing surveillance system architecture and will thus be subject to the relevant surveillance processes, as applicable. The Exchange believes that the existing surveillance procedures at the Exchange are capable of properly identifying unusual and/or illegal trading activity, which procedures the Exchange would utilize to surveil for aberrant trading in cash-settled FLEX ETF Options.

With respect to regulatory scrutiny, the Exchange believes its existing surveillance technologies and procedures adequately address potential concerns regarding possible manipulation of the settlement value at or near the close of the market. The Exchange notes that the regulatory program operated by and overseen by Phlx<sup>46</sup> includes cross-market surveillance designed to identify manipulative and other improper trading, including spoofing, algorithm gaming, marking the close and open, as well as more general, abusive behavior related to front running, wash sales, and quoting/routing, which may occur on the Exchange or other markets.<sup>47</sup>

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<sup>45</sup> For example, the regulatory program for the Exchange includes surveillance designed to identify manipulative and other improper options trading, including, spoofing, marking the close, front running, wash sales, etc.

<sup>46</sup> Phlx maintains a regulatory services agreement with Financial Industry Regulatory Authority, Inc. ("FINRA") whereby FINRA provides certain regulatory services to the exchanges, including cross-market surveillance, investigation, and enforcement services.

<sup>47</sup> As it relates to Reg SHO violations, the Exchange will enforce this through its Stock-Tied Reg SHO price protections in Options 3, Section 16(b). Specifically, Options 3, Section 16(e) provides that when the short sale price test in Rule 201 of Regulation SHO is triggered for a covered security, NES will not execute a short sale order in the underlying covered security component of a Complex Order if the price is equal to or below the current national best bid. However, NES will execute a short sale order in the underlying covered security component of a Complex Order if such order is marked "short exempt," regardless of whether it is at a price that is equal to or below the current national best bid. If NES cannot execute the underlying covered security component of a Complex Order in accordance with Rule 201 of Regulation SHO, the Exchange will hold the Complex Order on the Complex Order Book, if consistent with Member instructions. The order may execute at a price that is not equal to or below the current national best bid. For purposes of this paragraph, the term "covered security" shall have the same meaning as in Rule 201(a)(1) of Regulation SHO. This risk protection will apply wholesale to complex FLEX Orders with a stock component. NES will only execute the underlying covered security component of a Complex Order if the underlying covered security component is in accordance with Rule 201 of Regulation SHO. Additionally, FINRA's regulatory program addresses Reg SHO compliance for its member firms (which includes Exchange Members).



These cross-market patterns incorporate relevant data from various markets beyond the Exchange and its affiliates and from markets not affiliated with the Exchange. The Exchange represents that, today, its existing trading surveillances are adequate to monitor trading in the underlying ETFs and subsequent trading of options on those securities listed on the Exchange. Further, with the introduction of cash-settled FLEX ETF Options, the Exchange would leverage its existing surveillances to monitor trading in the underlying ETFs and subsequent trading of options on those securities listed on the Exchange with respect to cash-settled FLEX ETF options.<sup>48</sup>

Additionally, for options, the Exchange utilizes an array of patterns that monitor manipulation of options, or manipulation of equity securities (regardless of venue) for the purpose of impacting options prices on the Exchange (i.e., mini-manipulation strategies). That surveillance coverage is initiated once options begin trading on the Exchange. Accordingly, the Exchange believes that the cross-market surveillance performed by the Exchange or FINRA, on behalf of the Exchange, coupled with Phlx's own monitoring for violative activity on the Exchange comprise a comprehensive surveillance program that is adequate to monitor for manipulation of the underlying ETF and overlying option. Furthermore, the Exchange believes that the existing surveillance procedures at the Exchange are capable of properly identifying unusual and/or illegal trading activity, which the Exchange would utilize to surveil for aberrant trading in cash-settled FLEX ETF Options.

In addition to the surveillance procedures and processes described above, improvements in audit trails (i.e., the Consolidated Audit Trail), recordkeeping practices, and inter-exchange

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<sup>48</sup> Such surveillance procedures generally focus on detecting securities trading subject to opening price manipulation, closing price manipulation, layering, spoofing or other unlawful activity impacting an underlying security, the option, or both. The Exchange has price movement alerts, unusual market activity and order book alerts active for all trading symbols.

cooperation over the last two decades have greatly increased the Exchange's ability to detect and punish attempted manipulative activities. In addition, the Exchange is a member of the Intermarket Surveillance Group ("ISG"). The ISG members work together to coordinate surveillance and investigative information sharing in the stock and options markets. For surveillance purposes, the Exchange would therefore have access to information regarding trading activity in the pertinent underlying securities.

The proposed rule change is designed to allow investors seeking to effect cash-settled FLEX ETF Options with the opportunity for a different method of settling option contracts at expiration if they choose to do so. As noted above, market participants may choose cash settlement because physical settlement possesses certain risks with respect to volatility and movement of the underlying security at expiration that market participants may need to hedge against. The Exchange 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 innovative products for reasons that are generally debated in academic literature. The Exchange believes that introducing cash-settled FLEX ETF Options would further broaden the base of investors that use FLEX Equity Options to manage their trading and investment risk, including investors that currently trade in the OTC market for customized options, where settlement restrictions do not apply. The proposed rule change is also designed to encourage market makers to shift liquidity from the OTC market onto the Exchange, which, it believes, would enhance the process of price discovery conducted on the Exchange through increased order flow. The Exchange also believes that this may open up cash-settled FLEX ETF Options to more retail investors. The Exchange does not believe that this proposed

rule change raises any unique regulatory concerns because existing safeguards—such as position limits (and the aggregation of cash-settled positions with physically-settled positions), exercise limits (and the aggregation of cash-settled positions with physically-settled positions), and reporting requirements—would continue to apply. The Exchange believes the proposed position and exercise limits may further help mitigate the concerns that the limits are designed to address about the potential for manipulation and market disruption in the options and the underlying securities.<sup>49</sup>

Given the novel characteristics of cash-settled FLEX ETF Options, the Exchange will conduct a review of the trading in cash-settled FLEX ETF Options over an initial five-year period. The Exchange will furnish five reports to the Commission based on this review, the first of which would be provided within 60 days after the first anniversary of the initial listing date of the first cash-settled FLEX ETF Option under the proposed rule and each subsequent annual report to be provided within 60 days after the second, third, fourth and fifth anniversary of such initial listing. At a minimum, each report will provide a comparison between the trading volume of all cash-settled FLEX ETF Options listed under the proposed rule and physically settled options on the same underlying security, the liquidity of the market for such options products and the underlying ETF, and any manipulation concerns arising in connection with the trading of cash-settled FLEX ETF Options under the proposed rule. The Exchange will also provide additional data as requested by the Commission during this five year period. The reports will also discuss any recommendations the Exchange may have for enhancements to the listing standards based on its review. The Exchange believes these reports will allow the Commission

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<sup>49</sup> See proposed Options 8, Section 34(i)(1), which is based on Cboe Rule 8.35(c)(1)(B). The aggregation of position and exercise limits would include all positions on physically settled FLEX and non-FLEX Options on the same underlying ETFs.

and the Exchange to evaluate, among other things, the impact such options have, and any potential adverse effects, on price volatility and the market for the underlying ETFs, the component securities underlying the ETFs, and the options on the same underlying ETFs and make appropriate recommendations, if any, in response to the reports.

### Implementation

The Exchange will implement this rule change on or before December 20, 2025. Phlx would commence its implementation with a limited symbol migration and continue to migrate symbols over several weeks. The Exchange will issue an Options Trader Alert to member organizations to provide notification of the symbols that will migrate and the relevant dates.<sup>50</sup>

The Exchange will announce the implementation dates to member organizations in an Options Trader Alert.<sup>51</sup>

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,<sup>52</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act.<sup>53</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>54</sup> requirements that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with

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<sup>50</sup> See <https://www.nasdaqtrader.com/MicroNews.aspx?id=OTA2024-17>.

<sup>51</sup> Phlx Options 8, Section 34 rule text was previously amended by two rule changes which are effective, but not yet operative. See Securities Exchange Act Release Nos. 97658 (June 7, 2023), 88 FR 38562 (June 13, 2023) (SR-Phlx-2023-22); and 100321 (June 12, 2024), 89 FR 51580 (June 18, 2024) (SR-Phlx-2024-24). Phlx further delayed the implementation so that it could implement SR-Phlx-2023-22 while also completing an OCC industry rule change prior. These two prior rule changes will be implemented at the same time as the rule changes proposed herein.

<sup>52</sup> 15 U.S.C. 78f(b)

<sup>53</sup> 15 U.S.C. 78f(b)(5).

<sup>54</sup> 15 U.S.C. 78f(b)(5).

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.

### *Permissible Series*

The Exchange’s proposal to not authorize for trading a FLEX Option on iShares Bitcoin Trust ETF (“IBIT”) is consistent with ISE’s Approval Order of iShares Bitcoin Trust.<sup>55</sup> ISE stated that the position limit for IBIT options shall be 25,000 contracts.<sup>56</sup> Phlx proposes to exclude IBIT Options from trading as a FLEX Options to continue to limit the position limits for IBIT Options.

### *Characteristics of ETFs*

The Exchange’s proposal to provide in Options 8, Section 34(f)(1)(B) that, “an underlying equity security or index, as applicable (the index multiplier for FLEX Index Options is 100)” is consistent with the Act and will protect investors and the general public because this rule text adds transparency to the current characteristics of underlying interest for FLEX Option.

### *Minimum Trading Increments*

The Exchange’s proposal to amend Options 8, Section 34(f)(3) to provide that, “The Exchange may determine the smallest increment for exercise prices of FLEX Options on a class-by-class basis without going lower than the \$0.01.” is consistent with the Act and will protect investors and the general public because this rule text provides clear, transparent language

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<sup>55</sup> See Securities Exchange Act Release No. 101128 (September 20, 2024), 89 FR 78942 (September 26, 2024) (SR-ISE-2024-03) (Notice of Filing of Amendment Nos. 4 and 5 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment Nos. 1, 4, and 5, To Permit the Listing and Trading of Options on the iShares Bitcoin Trust).

<sup>56</sup> Id.

regarding the minimum trading increments for FLEX Options. The language is consistent with Cboe Rule 5.3(e)(3) except the Exchange is not proposing to provide for Micro FLEX Index Options or to allow prices to be expressed as a percentage value because the Exchange does not offer these features today. Also, this rule text is identical to ISE Options 3A, Section 3(c)(6).

### *FLEX PM Third Friday Options*

The Exchange's proposal to amend Options 8, Section 34(f)(5) to allow the listing of FLEX PM Third Friday Options, is consistent with the Commission's recent approval of Cboe's proposal to make its pilot a permanent program.<sup>57</sup> The Exchange believes that aligning to Cboe will allow Phlx to compete effectively with Cboe's product offering. Like Cboe, the Exchange believes that FLEX PM Third Friday Options will provide investors with greater trading opportunities and flexibility. The Exchange notes that the Commission recently approved proposals to make other pilots permitting p.m.-settlement of index options permanent after finding those pilots were consistent with the Act and the options subject to those pilots had no significant impact on the market.<sup>58</sup>

The Exchange further believes that permitting Phlx to list FLEX PM Third Friday

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<sup>57</sup> See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) ("FLEX Settlement Pilot Approval"). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission's Division of Economic and Risk Analysis ("DERA") staff. See FLEX Settlement Pilot Approval, notes 18 and 35.

<sup>58</sup> See Securities Exchange Act Release Nos. 98454 (September 20, 2023) (SR-CBOE-2023-005) (order approving proposed rule change to make permanent the operation of a program that allows the Exchange to list p.m.-settled third Friday-of-the-month SPX options series) ("SPXPM Approval"); 98455 (September 20, 2023) (SR-CBOE-2023-019) (order approving proposed rule change to make permanent the operation of a program that allows the Exchange to list p.m.-settled third Friday-of-the-month XSP and MRUT options series) ("XSP and MRUT Approval"); and 98456 (September 20, 2023) (SR-CBOE-2023-020) (order approving proposed rule change to make the nonstandard expirations pilot program permanent) ("Nonstandard Approval"). See also Securities Exchange Act Release Nos. 98451 (September 20, 2023), 88 FR 66088 (September 26, 2023) (SR-Phlx-2023-07) (Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Make Permanent Certain P.M.-Settled Pilots); and 98950 (November 15, 2023), 88 FR 81172 (November 21, 2023) (SR-Phlx-2023-45) (Order Approving a Proposed Rule Change To Permit the Listing and Trading of P.M.-Settled Nasdaq-100 Index Options With a Third-Friday-of-the-Month Expiration).

Options, similar to Cboe, will remove impediments to and perfect the mechanism of a free and open market and a national market system and protect investors, while maintaining a fair and orderly market. As described in the FLEX Settlement Pilot Approval, Cboe observed no significant adverse market impact or identified any meaningful regulatory concerns during the nearly 14-year operation of the FLEX PM Third Friday Program as a pilot nor during the 15 years since P.M.-settled index options (SPX) were reintroduced to the marketplace.<sup>59</sup>

As discussed in the FLEX Settlement Pilot Approval, the DERA staff study<sup>60</sup> and corresponding Cboe study concluded that a significantly larger amount of non-FLEX p.m.-settled index options had no significant adverse market impact and caused no meaningful regulatory concerns. Therefore, Cboe concluded that the relatively small amount of FLEX Index Option volume would similarly have no significant adverse market impact or cause no meaningful regulatory concerns.<sup>61</sup>

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<sup>59</sup> Notably, Cboe did not identify any significant economic impact (including on pricing or volatility or in connection with reversals) on related futures, the underlying indexes, or the underlying component securities of the underlying indexes surrounding the close as a result of the quantity of FLEX PM Third Friday Options or the amount of expiring open interest in FLEX PM Third Friday Options, nor any demonstrated capacity for options hedging activity to impact volatility in the underlying markets. See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) (“FLEX Settlement Pilot Approval”). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission’s Division of Economic and Risk Analysis (“DERA”) staff. See FLEX Settlement Pilot Approval, notes 18 and 35.

<sup>60</sup> See FLEX Settlement Pilot Approval, citing to Securities and Exchange Commission, Division of Economic Risk and Analysis, Memorandum dated February 2, 2021 on Cornerstone Analysis of PM Cash-Settled Index Option Pilots (September 16, 2020), available at: [https://www.sec.gov/files/Analysis\\_of\\_PM\\_Cash\\_Settled\\_Index\\_Option\\_Pilots.pdf](https://www.sec.gov/files/Analysis_of_PM_Cash_Settled_Index_Option_Pilots.pdf).

<sup>61</sup> See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) (“FLEX Settlement Pilot Approval”). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission’s Division of Economic and Risk Analysis (“DERA”) staff. See FLEX Settlement Pilot Approval, notes 18 and 35. Additionally, these studies measured any impact on related futures, the underlying indexes, or the underlying component securities of the underlying indexes surrounding the close. Despite FLEX SPX options (which represent approximately half of the year-to-date 2023 volume of FLEX Index Options but only approximately 0.3% of total SPX volume) not being included in the DERA staff study and corresponding Cboe study, those studies concluded that during the time periods covered (which included the period of time in which the Pilot Program has been operating), there was no significant

Cboe also concluded that the introduction of FLEX PM options had no significant impact on the market quality of corresponding a.m.-settled options or other options. As discussed in the FLEX Settlement Pilot Approval, Cboe’s analysis conducted after the introduction of SPXW options with Tuesday and Thursday expirations demonstrated no statistically significant impact on the bid-ask or effective spreads of SPXW options with Monday, Wednesday, and Friday expirations after trading in the SPXW options with Tuesday and Thursday expirations began.<sup>62</sup> Further, Cboe concluded that large FLEX PM Third Friday Options trades had no material negative impact (and likely no impact) on quote quality of non-FLEX a.m.-settled options overlying the same index with similar terms as the FLEX PM Third Friday Option upon evaluating data that showed that the spreads were relatively stable before and after large trades.<sup>63</sup> Therefore, Cboe concluded it is likely that FLEX PM Third Friday Options have had no significant negative impact on the market quality of non-FLEX Options with a.m.-settlement.<sup>64</sup>

Additionally, Cboe noted that the significant changes in the closing procedures of the

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economic impact on the underlying index or related products. Therefore, Cboe concluded that any FLEX SPX Options that executed during the timeframes covered by the studies had no significant impact on the underlying index or related products, as neither DERA staff nor Cboe observed any significant economic impact on the underlying index or related product.

<sup>62</sup> See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) (“FLEX Settlement Pilot Approval”). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission’s Division of Economic and Risk Analysis (“DERA”) staff. See FLEX Settlement Pilot Approval, notes 18 and 35.

<sup>63</sup> Specifically, Cboe evaluated each FLEX PM Third Friday Options trade for more than 500 contracts that occurred on Cboe during a two-year timeframe and analyzed the market quality (specifically, the average time-weighted quote spread and size 30 minutes prior to the trade and the average time-weighted quote spread and size 30 minutes after the trade) of series non-FLEX a.m.-settled options overlying the same index with similar terms as the FLEX PM Third Friday Option that traded (time to expiration, type (call or put), and strike price) as set forth in the Cboe’s data. See Securities Exchange Act Release No. 99222 (December 21, 2023), 88 FR 89771 (December 28, 2023) (SR-CBOE-2023-018) (“FLEX Settlement Pilot Approval”). In support of making the pilot a permanent program, Cboe cited to its own review of pilot data during the course of the pilot program and a study by the Commission’s Division of Economic and Risk Analysis (“DERA”) staff. See FLEX Settlement Pilot Approval, notes 18 and 35.

<sup>64</sup> The Exchange acknowledges that, while FLEX PM Third Friday Options has historically represented a very small percentage of overall volume, it is possible trading in these options may grow in the future.



primary markets in recent decades, including considerable advances in trading systems and technology, has significantly minimized risks of any potential impact of FLEX PM Third Friday Options on the underlying cash markets. As such, Cboe concluded that listing FLEX PM Third Friday Options did not raise any unique or prohibitive regulatory concerns and that such trading has not, and will not, adversely impact fair and orderly markets on expiration Fridays for the underlying indexes or their component securities.

The Exchange notes that p.m.-settled options were previously approved on Phlx's standard market,<sup>65</sup> including p.m.-settled third-Friday-of-the-month expirations for NDX and NXD options.<sup>66</sup> In the P.M.-Settled Pilot Permanency Approval, the Commission stated it believed that the evidence contained in the Exchange's filing, the Exchange's pilot data and reports, and the DERA staff study<sup>67</sup> analysis demonstrate that the Exchange's pilot programs have benefitted investors and other market participants by providing more flexible trading and hedging opportunities while also having no disruptive impact on the market.<sup>68</sup> The Commission also stated that the market for p.m.-settled options has grown in size over the course of the Exchange's pilot programs, and analysis of the pilot data did not identify any significant economic impact on the underlying component securities surrounding the close as a result of expiring p.m.-settled options nor did it indicate a deterioration in market quality (as measured by

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<sup>65</sup> See Securities Exchange Act Release No. 98451 (September 20, 2023), 88 FR 66088 (September 26, 2023) (SR-Phlx-2023-07) (Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Make Permanent Certain P.M.-Settled Pilots) ("P.M.-Settled Pilot Permanency Approval").

<sup>66</sup> See Securities Exchange Act Release No. 98950 (November 15, 2023), 88 FR 81172 (November 21, 2023) (SR-Phlx-2023-45) (Order Approving a Proposed Rule Change To Permit the Listing and Trading of P.M.-Settled Nasdaq-100 Index® Options With a Third-Friday-of-the-Month Expiration) ("P.M. Third Friday NDX Options Approval").

<sup>67</sup> See P.M.-Settled Pilot Permanency Approval, citing to Securities and Exchange Commission, Division of Economic Risk and Analysis, Memorandum dated February 2, 2021 on Cornerstone Analysis of PM Cash-Settled Index Option Pilots (September 16, 2020) (also referred to therein as the "Pilot Memo"), available at: [https://www.sec.gov/files/Analysis\\_of\\_PM\\_Cash\\_Settled\\_Index\\_Option\\_Pilots.pdf](https://www.sec.gov/files/Analysis_of_PM_Cash_Settled_Index_Option_Pilots.pdf).

<sup>68</sup> See P.M.-Settled Pilot Permanency Approval.

relative quoted spreads) for an existing product when a new p.m.-settled expiration was introduced.<sup>69</sup> Further, the Commission stated that significant changes in closing procedures in the decades since index options moved to a.m. settlement may also serve to mitigate the potential impact of p.m.-settled index options on the underlying cash markets.<sup>70</sup>

In support of its proposal to list p.m.-settled third-Friday-of-the-month expirations for NDX and XND options on its standard market, the Exchange pointed to, among other things, the data it provided underlying the P.M.-Settled Pilot Permanency Approval.<sup>71</sup> In reviewing this data from the Exchange (and other options exchanges in support of similar proposals to list and trade certain p.m.-settled broad-based index options) as well as the DERA staff study analysis, the Commission concluded that analysis of the pilot data did not identify any significant economic impact on the underlying component securities surrounding the close as a result of expiring p.m.-settled options nor did it indicate a deterioration in market quality for an existing product when a new p.m.-settled expiration was introduced.<sup>72</sup> Further, the Commission made similar findings as those in the P.M.-Settled Pilot Permanency Approval that significant changes in closing procedures in the decades since index options moved to a.m. settlement may also serve to mitigate the potential impact of p.m.-settled index options on the underlying cash markets.<sup>73</sup> The Exchange has observed no significant adverse market impact or identified any meaningful regulatory concerns since the introduction of p.m.-settled index options on its standard market.<sup>74</sup>

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<sup>69</sup> See id.

<sup>70</sup> See id.

<sup>71</sup> See P.M.-Settled Pilot Permanency Approval and P.M. Third Friday NDX Options Approval in notes 55 and 56, respectively.

<sup>72</sup> See P.M. Third Friday NDX Options Approval.

<sup>73</sup> See id.

<sup>74</sup> While the Exchange has received approval to list p.m.-settled third Friday-of-the-month expirations for NDX options on its standard market pursuant to the Third Friday NDX Options Approval, the Exchange

Given that the Exchange anticipates FLEX PM Third Friday Options to have a relatively smaller amount of volume compared to its standard non-FLEX p.m.-settled index options market, the Exchange believes that introducing FLEX PM Third Friday coupled with the other findings in Cboe's FLEX Settlement Pilot Approval would likely have no significant adverse market impact or cause any meaningful regulatory concerns as well.

#### *FLEX Options Terms*

The Exchange's proposal to amend Options 8, Section 34(f)(6)(B) to note the settlement style for FLEX Index Options depending on whether it is a.m.-settled or p.m.-settled is consistent with the Act and will protect investors and the general public because this rule text adds transparency to the current settlement of FLEX Index Options.

#### *Position and Exercise Limits*

Position and exercise limits are designed to address potential manipulative schemes and adverse market impacts surrounding the use of options, such as disrupting the market in the security underlying the options. While position and exercise limits should address and discourage the potential for manipulative schemes and adverse market impact, if such limits are set too low, participation in the options market may be discouraged. The Exchange believes that any decision regarding imposing position and exercise limits for FLEX Options must therefore be balanced between mitigating concerns of any potential manipulation and the cost of inhibiting potential hedging activity that could be used for legitimate economic purposes.

As it relates to FLEX Index Options, the Exchange believes that the proposed amendments to position and exercise limits in Options 8, Section 34(i) and (j) are reasonably

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has not listed them to date. The Exchange will launch p.m.-settled third-Friday-of-the-month expirations on NDX options concurrent with the launch of this rule proposal.

designed to prevent a member organization from using FLEX Index Options to evade the position limits applicable to comparable non-FLEX Index Options. Further, by establishing the proposed position and exercise limits for FLEX Index Options and, importantly, aggregating such positions in the manner described in proposed Options 8, Section 34(i)(4) the Exchange believes that the position and exercise limit requirements for FLEX Index Options should help to ensure that the trading of FLEX Index Options would not increase the potential for manipulation or market disruption and could help to minimize such incentives. The Exchange also notes that proposed position and exercise limits are consistent with the rules of other options exchanges that offer FLEX Index Options, as well as the rules of its own standard non-FLEX index options market, and therefore raise no novel issues for the Commission.<sup>75</sup>

As it relates to FLEX Equity Options, while no position limits are proposed for FLEX Equity Options, there are several mitigating factors, which include aggregation of FLEX Equity Option and non-FLEX Equity Option positions that expire on a third Friday-of-the-month and subjecting those positions to position and exercise limits, and daily monitoring of market activity. Similar to the other exchanges that trade FLEX Equity Options, the Exchange believes that eliminating position and exercise limits for FLEX Equity Options, while requiring positions in FLEX Equity Options that expire on a third Friday-of-the-month to be aggregated with positions in non-FLEX Equity Options on the same underlying security,<sup>76</sup> removes impediments to and perfects the mechanism of a free and open market and a national market system because it allows the Exchange to create a product and market that is an improved but comparable

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<sup>75</sup> See Cboe Rules 8.35(a), (b), (d), and 8.42(g) and Phlx Options 4A, Sections 6(a), 9(a)(13), and 9(a)(14).

<sup>76</sup> See proposed Options 8, Section 34(i)(4)(c) and Section 34(j)(1)(c). See also Cboe Rules 8.35(d)(3) and 8.42(g)(3); NYSE Arca Rules 5.35-O(a)(iii), (b) and 5.36-O; NYSE American Rules 906G and 907G; and Phlx Options 8, Section 34(e) and (f).

alternative to the OTC market in customized options. OTC transactions occur through bilateral agreements, the terms of which are not publicly disclosed to the marketplace. As such, OTC transactions do not contribute to the price discovery process that exists on a public exchange.

The Exchange believes that the proposed elimination of position and exercise limits for FLEX Equity Options may encourage market participants to transfer their liquidity demands from OTC markets to exchanges and enable liquidity providers to provide additional liquidity to Phlx through transactions in FLEX Equity Options. The Exchange notes that the Commission previously approved the elimination of position and exercise limits for FLEX Equity Options, finding that such elimination would allow exchanges “to better compete with the growing OTC market in customized equity options, thereby encouraging fair competition among brokers and dealers and exchange markets.”<sup>77</sup> The Commission has also stated that the elimination of position and exercise limits for FLEX Equity Options “could potentially expand the depth and liquidity of the FLEX equity market without significantly increasing concerns regarding intermarket manipulations or disruptions of the options or the underlying securities.”<sup>78</sup>

Additionally, the Exchange believes that requiring positions in FLEX Equity Options that expire on a third Friday-of-the-month to be aggregated with positions in non-FLEX Equity Options on the same underlying security subjects FLEX Equity Options and non-FLEX Equity Options to the same position and exercise limits on third Friday-of-the-month expirations. These limitations are intended to serve as a safeguard against potential adverse effects of large FLEX Equity Option positions expiring on the same day as non-FLEX Equity Option positions. As

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<sup>77</sup> See Securities Exchange Act Release No. 42223 (December 10, 1999), 64 FR 71158, 71159 (December 20, 1999) (SR-Amex-99-40) (SR-PCX-99-41) (SR-CBOE-99-59) (Order Granting Accelerated Approval to Proposed Rule Change Relating to the Permanent Approval of the Elimination of Position and Exercise Limits for FLEX Equity Options).

<sup>78</sup> See id.

noted above, Cboe Rules 8.35(d)(3) and 8.42(g)(3) have the same requirements. Also, ISE Options 3A, Section 18(c)(1) has identical rule text.

The Exchange believes that any potential risk of manipulative activity is mitigated by existing surveillance technologies, procedures, and reporting requirements at the Exchange, which allows the Exchange to properly identify disruptive and/or manipulative trading activity. In addition to its own surveillance programs, the Exchange also works with other SROs and exchanges on intermarket surveillance related issues. Through its participation in ISG, the Exchange shares information and coordinates inquiries and investigations with other exchanges designed to address potential intermarket manipulation and trading abuses. The Exchange also notes that FINRA conducts cross-market surveillances on behalf of the Exchange pursuant to a regulatory services agreement.<sup>79</sup> The Exchange also represents that it is reviewing its procedures to detect potential manipulation in light of any changes required for FLEX Options to confirm appropriate surveillance coverage. These procedures utilize daily monitoring of market activity via automated surveillance techniques to identify unusual activity in both options and their underlying securities and are designed to protect investors and the public interest by ensuring that the Exchange has an adequate surveillance program in place.

Lastly, the Exchange notes that other exchanges currently trading FLEX options have similar position and exercise limits described above.<sup>80</sup>

### **Cash-Settled FLEX Equity Options on Exchange Traded Funds (“ETFs”)**

Introducing cash-settled FLEX ETF Options will increase order flow to the Exchange, increase the variety of options products available for trading, and provide a valuable tool for

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<sup>79</sup> The Exchange notes that it is responsible for FINRA’s performance under this regulatory services agreement.

<sup>80</sup> See Cboe Rules 8.35(d) and 8.42(g).

investors to manage risk.

The Exchange believes that the proposal to permit cash settlement as a contract term for options on the specified group of equity securities would remove impediments to and perfect the mechanism of a free and open market as cash-settled FLEX ETF Options would enable market participants to receive cash in lieu of shares of the underlying security, which would, in turn provide greater opportunities for market participants to manage risk through the use of a cash-settled product to the benefit of investors and the public interest. The Exchange does not believe that allowing cash settlement as a contract term for options on the specified group of equity securities would render the marketplace for equity options more susceptible to manipulative practices. As illustrated in the table above, each of the qualifying underlying securities is actively traded and highly liquid and thus would not be susceptible to manipulation because, over a six-month period, each security had an average daily notional value of at least \$500 million and an ADV of at least 4,680,000 shares, which indicates that there is substantial liquidity present in the trading of these securities, and that there is significant depth and breadth of market participants providing liquidity and of investor interest. The Exchange believes the proposed bi-annual review to determine eligibility for an underlying ETF to have cash settlement as a contract term would remove impediments to and perfect the mechanism of a free and open market as it would permit the Exchange to select only those underlying ETFs that are actively traded and have robust liquidity as each qualifying ETF would be required to meet the average daily notional value and average daily volume requirements, as well as to select the same underlying ETFs on which other exchanges may list cash-settled FLEX ETF Options.<sup>81</sup>

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<sup>81</sup> See Securities Exchange Act Release No. 88131 (February 5, 2020), 85 FR 7806 (February 11, 2020) (SR-NYSEAmer-2019-38) (Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, To Allow Certain Flexible Equity Options To

The Exchange believes the proposed change that, for FLEX ETF Options, at least one of exercise style, expiration date, and exercise price must differ from options in the non-FLEX market will provide clarity and eliminate confusion regarding permissible terms of FLEX ETF Options, including the proposed cash-settled FLEX ETF Options.

The Exchange believes that the data provided by the Exchange supports the supposition that permitting cash settlement as a FLEX term for the 43 underlying ETFs that would currently qualify to have cash settlement as a contract term would broaden the base of investors that use FLEX Equity Options to manage their trading and investment risk, including investors that currently trade in the OTC market for customized options, where settlement restrictions do not apply.

The Exchange believes that the proposal to permit cash settlement for certain FLEX ETF options would remove impediments to and perfect the mechanism of a free and open market because the proposed rule change would provide members and member organizations with enhanced methods to manage risk by receiving cash if they choose to do so instead of the underlying security. In addition, this proposal would promote just and equitable principles of trade and protect investors and the general public because cash settlement would provide investors with an additional tool to manage their risk. Further, the Exchange notes that another exchange has previously received approval that allows for the trading of cash-settled options, and, specifically, cash-settled FLEX ETF Options in an identical manner as the Exchange proposes to list them pursuant to this rule filing.<sup>82</sup> The proposed rule change therefore should

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Be Cash Settled). Cboe also filed an immediately effective rule change to allow certain FLEX Options to be cash settled. See Securities Exchange Act Release No. 98044 (August 2, 2023), 88 FR 53548 (August 8, 2023) (SR-Cboe-2023-036) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Allow Certain Flexible Exchange Equity Options To Be Cash Settled).

<sup>82</sup> See supra notes 25-27.



not raise issues for the Commission that it has not previously addressed.

The proposed rule change to permit cash settlement as a contract term for options on up to 50 ETFs is designed to promote just and equitable principles of trade in that the availability of cash settlement as a contract term would give market participants an alternative to trading similar products in the OTC market. By trading a product in an exchange-traded environment (that is currently traded in the OTC market), the Exchange would be able to compete more effectively with the OTC market. The Exchange believes the proposed rule change is designed to prevent fraudulent and manipulative acts and practices in that it would lead to the migration of options currently trading in the OTC market to trading on the Exchange. Also, any migration to the Exchange from the OTC market would result in increased market transparency. Additionally, the Exchange believes the proposed rule change is designed to remove impediments to and to perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest in that it should create greater trading and hedging opportunities and flexibility. The proposed rule change should also result in enhanced efficiency in initiating and closing out positions and heightened contra-party creditworthiness due to the role of OCC as issuer and guarantor of the proposed cash-settled options. Further, the proposed rule change would result in increased competition by permitting the Exchange to offer products that are currently available for trading only in the OTC market and are approved to trade on another options exchange.

The Exchange believes that establishing position limits for cash-settled FLEX ETF Options to be the same as physically settled options on the same underlying security, and aggregating positions in cash-settled FLEX ETF Options with physically settled options on the same underlying security for purposes of calculating position limits is reasonable and consistent

with the Act. By establishing the same position limits for cash-settled FLEX ETF Options as for physically settled options on the same underlying security and, importantly, aggregating such positions, the Exchange believes that the position limit requirements for cash-settled FLEX ETF Options should help to ensure that the trading of cash-settled FLEX ETF Options would not increase the potential for manipulation or market disruption and could help to minimize such incentives. For the same reasons, the Exchange believes the proposed exercise limits are reasonable and consistent with the Act.

Finally, the Exchange represents that it has an adequate surveillance program in place to detect manipulative trading in cash-settled FLEX ETF Options and the underlying ETFs. Regarding the proposed cash settlement, the Exchange would use the same surveillance procedures currently utilized for the Exchange's other FLEX Options. For surveillance purposes, the Exchange would have access to information regarding trading activity in the pertinent underlying ETFs. The Exchange believes that limiting cash settlement to no more than 50 underlying ETFs (currently, 43 ETFs would be eligible to have cash-settlement as a contract term) would minimize the possibility of manipulation due to the robust liquidity in both the equities and options markets.

As a self-regulatory organization, the Exchange recognizes the importance of surveillance, among other things, to detect and deter fraudulent and manipulative trading activity as well as other violations of Exchange rules and the federal securities laws. As discussed above, Phlx has adequate surveillance procedures in place to monitor trading in cash-settled FLEX ETF Options and the underlying securities, including to detect manipulative trading activity in both the options and the underlying ETF.<sup>83</sup> The Exchange further notes the liquidity and active

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<sup>83</sup> Among other things, Phlx's regulatory program includes cross-market surveillance designed to identify

markets in the underlying ETFs, and the high number of market participants in both the underlying ETFs and existing options on the ETFs, helps to minimize the possibility of manipulation. The Exchange further notes that under Section 19(g) of the Act, the Exchange, as a self-regulatory organization, is required to enforce compliance by its members and persons associated with its members with the Act, the rules and regulations thereunder, and the rules of the Exchange.<sup>84</sup> The Exchange believes its surveillance, along with the liquidity criteria and position and exercise limits requirements, are reasonably designed to mitigate manipulation and market disruption concerns and will permit it to enforce compliance with the proposed rules and other Exchange rules in accordance with Section 19(g) of the Act. The Exchange performs ongoing evaluations of its surveillance program to ensure its continued effectiveness and will continue to review its surveillance procedures on an ongoing basis and make any necessary enhancements and/or modifications that may be needed for the cash settlement of FLEX ETF Options.

Additionally, the Exchange will monitor any effect additional options series listed under the proposed rule change may have on market fragmentation and the capacity of the Exchange's

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manipulative and other improper trading, including spoofing, algorithm gaming, marking the close and open, as well as more general abusive behavior related to front running, wash sales, and quoting/routing, which may occur on the Exchange and other markets. Furthermore, the Exchange stated that it has access to information regarding trading activity in the pertinent underlying securities as a member of ISG. As it relates to Reg SHO violations, the Exchange will enforce this through its Stock-Tied Reg SHO price protections in Options 3, Section 16(b). Specifically, Options 3, Section 16(b) provides that when the short sale price test in Rule 201 of Regulation SHO is triggered for a covered security, NES will not execute a short sale order in the underlying covered security component of a Complex Order if the price is equal to or below the current national best bid. However, NES will execute a short sale order in the underlying covered security component of a Complex Order if such order is marked "short exempt," regardless of whether it is at a price that is equal to or below the current national best bid. If NES cannot execute the underlying covered security component of a Complex Order in accordance with Rule 201 of Regulation SHO, the Exchange will cancel back the Complex Order to the entering member organization. For purposes of this paragraph, the term "covered security" shall have the same meaning as in Rule 201(a)(1) of Regulation SHO. NES will only execute the underlying covered security component of a Complex Order if the underlying covered security component is in accordance with Rule 201 of Regulation SHO.

<sup>84</sup> 15 U.S.C. 78s(g).

automated systems. The Exchange will take prompt action, including timely communication with the Commission and with other self-regulatory organizations responsible for oversight of trading in options, the underlying ETFs, and the ETFs' component securities, should any unanticipated adverse market effects develop.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

The Exchange does not believe that the proposed rule change will impose any burden on intra-market competition that is not necessary or appropriate in furtherance of the purposes of the Act, as all member organizations who wish to trade FLEX Options will be able to trade such options in the same manner. Additionally, positions in FLEX Options of all member organizations will be subject to the same position limits, and such positions will be aggregated in the same manner as described in proposed Options 8, Section 34(i)(4).

The Exchange also does not believe that the proposed rule change will impose any burden on inter-market competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposal promotes inter-market competition by providing another alternative (i.e., exchange markets) to bilateral OTC trading of options with flexible terms. Exchange markets, in contrast with bilateral OTC trading, are centralized, transparent, and have the guarantee of OCC for options traded.

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

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

- (i) significantly affect the protection of investors or the public interest;
- (ii) impose any significant burden on competition; and
- (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>85</sup> and Rule 19b-4(f)(6)<sup>86</sup> thereunder.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's internet comment form (<https://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include file number SR-Phlx-2025-20 on the subject line.

##### Paper Comments:

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<sup>85</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>86</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

- 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-Phlx-2025-20. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's internet website (<https://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 a.m. and 3 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. Do not include personal identifiable information in submissions; you should submit only information that you wish to make available publicly. We may redact in part or withhold entirely from publication submitted material that is obscene or subject to copyright protection.

All submissions should refer to file number SR-Phlx-2025-20 and should be submitted on or before [INSERT DATE 21 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>87</sup>

**Sherry R. Haywood,**

*Assistant Secretary.*

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<sup>87</sup> 17 CFR 200.30-3(a)(12).