

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-78444; File No. SR-BOX-2016-37)

July 29, 2016

Self-Regulatory Organizations; BOX Options Exchange LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Detail How Complex Orders Will Execute Through the Facilitation Auction Mechanism

Pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (the “Act”)<sup>2</sup> and Rule 19b-4 thereunder,<sup>3</sup> notice is hereby given that on July 26, 2016, BOX Options Exchange LLC (“BOX” or the “Exchange”) filed with the Securities and Exchange Commission (the “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 detail how Complex Orders will execute through the Facilitation Auction mechanism. The text of the proposed rule change is available from the principal office of the Exchange, at the Commission’s Public Reference Room and also on the Exchange’s Internet website at <http://boxexchange.com>.

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

<sup>2</sup> 15 U.S.C. 78a.

<sup>3</sup> 17 CFR 240.19b-4.

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

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of the proposed rule change is to detail how the Facilitation Auction mechanism will treat Complex Orders on the Exchange.<sup>4</sup> Pursuant to BOX Rule 7270, the Exchange has two block-sized auction mechanisms, the Facilitation Auction Mechanism and the Solicitation Auction Mechanism whereby Order Flow Providers (OFPs) can provide price improvement opportunities for a transaction where the OFP seeks to facilitate an order it represents as agent, and/or a transaction where the OFP solicited interest to execute against an order it represents as agent. Transactions executed through the Facilitation or Solicitation auction mechanisms are comprised of the order the OFP represents as agent (the "Agency Order") and the contra order for the full size of the Agency Order (either the "Facilitation" or "Solicitation" Order).<sup>5</sup> The contra order may represent interest for the Participant's own account or interest the Participant has solicited from one or more other parties, or a combination of both.

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<sup>4</sup> Complex Orders are not currently traded through the Facilitation Auction mechanism. Prior to implementation, BOX will issue an informational circular to inform Participants of the implementation date for Complex Orders to trade through the Facilitation Auction.

<sup>5</sup> The Exchange notes that it does not trade stock option orders.

This proposal only addresses how the Facilitation Auction mechanism will treat Complex Orders on the Exchange. Similar to the ISE's Block-Trade rules,<sup>6</sup> Complex Orders<sup>7</sup> executed through the Facilitation auction on BOX function in substantially the same manner as single-leg orders executed through this mechanism. To detail how this mechanism treats Complex Orders, the Exchange proposes to insert IM-7270-7. IM-7270-7 will state that Participants may use the Facilitation Mechanism according to paragraph (a) of Rule 7270 to execute block-size Complex Orders at a net price. The OFP must be willing to execute the entire size of the Agency Order through the submission of a contra order; and block-size Complex Orders executed through the Facilitation Mechanism will continue to be limited to Complex Orders of fifty (50) contracts per leg or more.<sup>8</sup>

Upon the entry of a block-sized order into the Facilitation mechanism, a broadcast message will be sent to Options Participants, giving them one second to enter responses with the prices and sizes at which they would be willing to participate opposite the Agency Order ("Responses").<sup>9</sup> Responses to a Complex Order within the Facilitation Auction mechanism may be submitted for any size up to the size of the entire Complex Order, however, the Responses must be for all Legs of

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<sup>6</sup> See International Securities Exchange Rule 716 and Supplementary Material .08 to Rule 716.

<sup>7</sup> Under Rule 7240(a)(5) a "Complex Order" is defined as "any order involving the simultaneous purchase and/or sale of two or more different options series in the same underlying security, for the same account, in a ratio that is equal to or greater than one-to-three (.333) and less than or equal to three-to-one (3.00) and for the purpose of executing a particular investment strategy.) A Complex Order that does not meet this definition will be automatically rejected.

<sup>8</sup> Complex Orders comprised of less than fifty (50) contracts on each leg will automatically be rejected.

<sup>9</sup> The Exchange believes that 1 second is an adequate duration for the Facilitation Auction. Specifically, the Exchange believes customers are capable of responding within this duration and has not received any complaints regarding the duration of the Facilitation Auction broadcast since the mechanism was adopted in 2011.

the unique Complex Order. Responses must be priced at the price of the Agency Order or at a better price and must not exceed the size of the Agency Order.<sup>10</sup> At the end of the one second period for the entry of Responses, the block-sized Facilitation Complex Order will be automatically executed with the Agency Order.<sup>11</sup> However, as is also the case for single-leg orders executed through the Facilitation mechanism, if the Facilitation Price is outside the NBBO at the end of the auction, the auction will be canceled.

Identical to the process for single-leg orders, Participants may enter Responses for Complex Orders in these auctions at net prices, and bids and offers for Complex Orders will participate in the execution of an order being executed as provided in paragraphs (a) and (b) of Rule 7270. However, the execution rules for Complex Orders detailed in BOX Rule 7240(b)(2) and (3) will continue to apply.<sup>12</sup> For example, if there is sufficient interest on the BOX Book for the individual legs to be executed at a permissible ratio, this “Implied Order”<sup>13</sup> will have priority here and will execute against the Agency Order, provided that each of its component Legs is equal to or better than its respective NBBO.

If there is no execution against the Implied Order, the Agency Order can execute against the Complex Order interest. The priority rules for the Facilitation Auction,<sup>14</sup> including the surrender quantity designation, will continue to apply. The following example illustrates the

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<sup>10</sup> A Response that doesn’t meet the requirements will be automatically rejected

<sup>11</sup> Assuming there are no Responses to the auction or interest on the BOX Book that could execute against the Agency Order.

<sup>12</sup> The Exchange notes that this includes the Complex Order Filter outlined in BOX Rule 7240(b)(3)(iii).

<sup>13</sup> An “Implied Order” is a Complex Order that is derived from the orders on the BOX Book for each component leg of a strategy.

<sup>14</sup> See BOX Rule 7270(a)(3).

execution priority of interest on the BOX Book for a Complex Order within the Facilitation Auction. An OFP submits a Complex Order through the Facilitation Order to sell 500 A+B+C at \$3.00. During the one second auction, BOX receives the following bids (offers) in time priority:

- 1) Market Maker Complex Order Response to buy 500 of A+B+C at \$3.00
- 2) Public Customer Complex Order Response to buy 40 A+B+C at \$3.00

Interest on the BOX Book (Implied Order):

- Market Maker Option A – Order to buy 500 at \$1.00
- Market Maker Option B – Order to buy 500 at \$1.00
- Broker Dealer Option C – Order to buy 500 at \$1.00

Since it is possible to execute the entire Complex Order against interest on the BOX Book (Implied Order) at the same price, the sell order will execute against the bids on A, B and C at \$1.00 for 100 contracts each. And since this execution will exhaust the sell order, all the Responses, including the Public Customer's Response and the OFP's Facilitation Order will receive no trade allocation.

The pricing provision in BOX Rule 7270(a)(3)(i) will apply to Public Customer Complex Orders and Public Customer Responses. If there is not sufficient size to execute the entire Agency Order at a better price and there are Public Customer Complex Order bids (offers) and Public Customer Responses on BOX at the time the Agency Order is executed that are priced higher (lower) than the facilitation price, these will maintain their price priority but execute at the Facilitation Price.<sup>15</sup> Non-Public Customer and Market Maker bids (offers) and Non-Public Customer and Market Maker Responses on BOX at the time the Agency Order is executed that are priced higher (lower) than the facilitation price will be executed against the Agency Order at their

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<sup>15</sup> If there is sufficient interest to execute the Agency Order at a better price, Public Customer Complex Order bids (offers) will receive their stated price.

stated price, providing the Agency Order [sic] execution at a better price for the number of contracts associated with such higher bids (lower offers) and Responses. When an Implied Order executes against an Agency Order, the Implied Order will be executed at its stated price.<sup>16</sup>

The following example illustrates the allocation priority of BOX Rule 7270(a)(3)(ii). An OFP submits a Complex Order through the Facilitation auction to sell 500 A+B+C at \$3.00. During the one second auction, BOX receives the following bids (offers) in time priority:

- 1) Public Customer #1 Complex Order Response to buy 100 A+B+C at \$3.00
- 2) Public Customer #2 Complex Order Response to buy 100 A+B+C at \$3.02
- 3) Market Maker #1 Complex Order Response to buy 105 of A+B+C at \$3.06
- 4) Market Maker #2 Complex Order Response to buy 95 of A+B+C at \$3.04

Interest on the BOX Book (Implied Order):

- Market Maker Option A – Order to buy 125 at \$1.00
- Market Maker Option B – Order to buy 125 at \$1.00
- Public Customer Option C – Order to buy 125 at \$1.00

The Facilitated Complex Order will be allocated in the following order:

- 1) 105 contracts at \$3.06 to Market Maker #1 (price priority)
- 2) 95 contracts at \$3.04 to Market Maker #2 (price priority)
- 3) 100 contracts at \$3.00 to Public Customer #2 (the Public Customer retains its price priority, but executes at the facilitation price because there was not sufficient interest to execute the entire Agency Order at a Better Price)
- 4) 125 contracts at \$3.00 to BOX Book Interest (Implied Order)<sup>17</sup>

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<sup>16</sup> See IM-7270-7. The Exchange notes that the provisions of BOX Rule 7270(a)(3)(i) do not apply to Implied Orders created from BOX Book interest.

<sup>17</sup> The Exchange notes that once an Implied Order is created from BOX Book interest, the Participant types composing the Implied Order are no longer relevant, and have no impact on execution and allocation priority.

- 5) 75 contracts at \$3.00 to Public Customer #1 (remaining interest is allocated to the Public Customer at the facilitation price)

The following example illustrates allocation priority of interest on the BOX Book over an OFP's allocation priority.<sup>18</sup> An OFP submits a Complex Order through the Facilitation auction to sell 500 A+B+C at \$3.00. During the one second auction, BOX receives the following bids (offers) in time priority:

- 1) Market Maker #1 Complex Order Response to buy 95 of A+B+C at \$3.02
- 2) Market Maker #2 Complex Order Response to buy 150 of A+B+C at \$3.00

Interest on the BOX Book (Implied Order):

- Market Maker Option A – Order to buy 300 at \$1.00
- Market Maker Option B – Order to buy 300 at \$1.00
- Public Customer Option C – Order to buy 300 at \$1.00

The Facilitated Complex Order will be allocated in the following order:

- 1) 95 contracts at \$3.02 to Market Maker #1 (price priority)
- 2) 300 contracts at \$3.00 to BOX Book Interest (Implied Order)
- 3) 105 contracts at \$3.00 to OFP's Facilitation Order (the OFP receives the remaining contracts as there is insufficient size to satisfy the full 40% allocation)

The final example below illustrates allocation priority when the OFP has designated a surrender quantity under BOX Rule 7270(a)(3)(iii). An OFP submits a Complex Order through the Facilitation auction to sell 300 A+B+C at \$3.00 with a surrender quantity of 220. During the one second auction, BOX receives the following bids (offers) in time priority:

- 1) Market Maker #1 Complex Order Response to buy 120 of A+B+C at \$3.00

Interest on the BOX Book (Implied Order):

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<sup>18</sup> Under BOX Rule 7270(a)(3)(ii) the OFP is entitled to at least 40% of the original size of the Facilitation Order after better-priced bids (offers) and Responses on BOX, as well as Public Customer bids (offers) and Responses at the facilitation price.

- Market Maker Option A – Order to buy 100 at \$1.00
- Market Maker Option B – Order to buy 100 at \$1.00
- Public Customer Option C – Order to buy 100 at \$1.00

The Facilitated Complex Order will be allocated in the following order:

- 1) 100 contracts at \$3.00 to BOX Book Interest (Implied Order Priority)
- 2) 80 contracts at \$3.00 to OFP’s Facilitation Order with a Surrender Quantity
- 3) 120 contracts at \$3.00 to Market Maker #1

## 2. Statutory Basis

The Exchange believes that the proposal is consistent with the requirements of Section 6(b) of the Act,<sup>19</sup> in general, and Section 6(b)(5) of the Act,<sup>20</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to, and perfect the mechanism of, a free and open market and a national market system, and, in general, to protect investors and the public interest. In particular, the Exchange believes that the proposed rule change to amend BOX Rule 7270 to provide for the execution of Complex Orders through the Facilitation Auction mechanism on BOX. [sic] This proposed rule change is designed to help BOX remain competitive among options exchanges and provide market participants additional opportunities to execute block-size crossing transactions.

### (B) Self-Regulatory Organization’s Statement on Burden on Competition

The proposed change provides for the execution of Complex Orders through the Facilitation auction mechanism. As such, the Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the

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<sup>19</sup> 15 U.S.C. 78f(b).

<sup>20</sup> 15 U.S.C. 78f(b)(5).

purposes of the Act. The Exchange does not believe the proposal will impose any burden on intermarket competition, as the proposed rule will allow BOX to compete with other options exchanges in the industry. Specifically, ISE has a similar mechanism in place.<sup>21</sup>

Additionally, the Exchange does not believe the proposal will impose any burden on intramarket competition, as the Facilitation Auction mechanism is available to all Participants and all OFPs may submit orders through the mechanism.

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

The Exchange has neither solicited nor received comments on the proposed rule change.

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

(a) This proposed rule change is filed pursuant to paragraph (A) of section 19(b)(3) of the Exchange Act<sup>22</sup> and Rule 19b-4(f)(6) thereunder.<sup>23</sup>

(b) Because this proposed rule change does not significantly affect the protection of investors or the public interest, does not impose any significant burden on competition, and, by its terms, does not become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(6) thereunder.

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<sup>21</sup> See supra note 5.

<sup>22</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>23</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) under the Exchange Act requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of 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. BOX has satisfied this requirement.

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 (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-BOX-2016-37 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-BOX-2016-37. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those

that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing will also be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-BOX-2016-37 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>24</sup>

Robert W. Errett  
Deputy Secretary

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<sup>24</sup> 17 CFR 200.30-3(a)(12).