

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-80134; File No. SR-BOX-2016-48)

March 1, 2017

Self-Regulatory Organizations; BOX Options Exchange LLC; Notice of Filing of Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as Modified by Amendment No. 1, to Adopt Rules for an Open-Outcry Trading Floor

I. Introduction

On November 16, 2016, BOX Options Exchange LLC (the “Exchange” or “BOX”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposal to adopt rules for an open-outcry trading floor. The proposed rule change was published for comment in the Federal Register on December 05, 2016.<sup>3</sup> On January 10, 2017, the Commission extended the time period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change to March 05, 2017.<sup>4</sup> The Commission received three comment letters on the proposed

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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> See Securities Exchange Act Release No. 79421 (November 29, 2016), 81 FR 87607 (December 5, 2016) (“Notice”).

<sup>4</sup> See Securities Exchange Act Release No. 79768 (January 10, 2017), 82 FR 4956 (January 17, 2017).

rule change<sup>5</sup> and one response letter from BOX.<sup>6</sup> On February 21, 2017, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>7</sup>

The Commission is publishing this notice to solicit comments on the proposed rule change, as modified by Amendment No. 1, from interested persons and to institute proceedings under Section 19(b)(2)(B) of the Act<sup>8</sup> to determine whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1. The institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved, nor does it mean that the Commission will ultimately disapprove the proposed rule change. Rather, as described in Section V below, the Commission seeks and encourages interested persons to provide additional comment on the proposed rule change in order to inform the Commission's analysis of whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1.

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<sup>5</sup> See letters to Brent J. Fields, Secretary, Commission, from Angelo Evangelou, Deputy General Counsel, The Chicago Board Options Exchange, Inc., dated January 10, 2017 ("CBOE Letter"); Steve Crutchfield, Head of Market Structure, CTC Trading Group, LLC, dated December 31, 2016 ("CTC Letter"); and Joan C. Conley, Senior Vice President and Corporate Secretary, The Nasdaq Stock Market LLC, dated December 22, 2016 ("Nasdaq Letter").

<sup>6</sup> See letter to Brent J. Fields, Secretary, Commission, from Lisa J. Fall, President, BOX Options, received February 21, 2017 ("BOX Response Letter").

<sup>7</sup> Amendment No. 1 partially amends the filing, SR-BOX-2016-48. In Amendment No. 1, the Exchange removed proposed rule language relating to its minor rule violation plan, proposed disciplinary process for the trading floor, and proposed rules for split price transactions. In addition, the Exchange clarified various aspects of how orders will be handled on the trading floor, revised its discussion of compliance with Section 11(a) of the Act, and made other clarifying changes to the filing and proposed rule text. Amendment No. 1 has been placed in the public comment file for SR-BOX-2016-048 at <https://www.sec.gov/comments/sr-box-2016-48/box201648.shtml> and also is available on the Exchange's website at [http://lynxstorageaccount.blob.core.windows.net/boxvr/SE\\_resources/SR-BOX-2016-48\\_Amendment\\_1.pdf](http://lynxstorageaccount.blob.core.windows.net/boxvr/SE_resources/SR-BOX-2016-48_Amendment_1.pdf).

<sup>8</sup> 15 U.S.C. 78s(b)(2)(B).

## II. Description of the Proposed Rule Change, as Modified by Amendment No. 1

The Exchange proposes to adopt rules to establish an open-outcry trading floor.<sup>9</sup>

Currently the Exchange only offers electronic trading, and proposes to add a physical trading floor to create a hybrid system that integrates both electronic and open-outcry trading.<sup>10</sup>

### A. Proposed BOX Floor Procedure

Under the proposed rules, upon receipt of an order, a Floor Broker<sup>11</sup> wishing to execute an order on the floor would be required to record specific information regarding the order into the Floor Broker's order entry mechanism.<sup>12</sup> All orders executed on the trading floor would be Qualified Open Outcry orders ("QOO Orders"),<sup>13</sup> which must be entered as a two-sided order. Each two-sided order contains an initiating side ("agency order"), which must be filled in its entirety, and a "contra-side," which must guarantee the full size of the initiating side of the QOO

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<sup>9</sup> See Notice, supra note 3, at 87607.

<sup>10</sup> See id. Other exchanges that currently offer a combination of open-outcry and electronic trading are NYSE Arca, Inc. ("NYSE Arca"), NASDAQ PHLX LLC ("PHLX"), Chicago Board Options Exchange, Incorporated ("CBOE"), and NYSE MKT LLC ("NYSE MKT").

<sup>11</sup> See proposed BOX Rule 7540. A Floor Broker is an individual who is registered with the Exchange for the purpose, while on the trading floor, of accepting and handling options orders. Id. Proposed BOX Rule 7550 provides that the Exchange shall review applications for registration as a Floor Broker on such form or forms as the Exchange may prescribe, and that the Exchange shall consider an applicant's ability as demonstrated by his passing a Floor Broker's examination, if prescribed by the Exchange, and such other factors as the Exchange deems appropriate.

<sup>12</sup> See proposed BOX Rule 7580(e). The specific information required includes: (i) the order type (i.e., customer, firm, broker-dealer, professional, or Market Maker) and order receipt time; (ii) the option symbol; (iii) buy, sell, cross or cancel; (iv) call, put, complex (i.e., spread, straddle), or contingency order; (v) number of contracts; (vi) limit price or market order or, in the case of a multi-leg order, net debit or credit, if applicable; (vii) whether the transaction is to open or close a position; and (viii) the Options Clearing Corporation clearing number of the broker-dealer that submitted the order. See id.

<sup>13</sup> See proposed BOX Rule 7600(a)(1). QOO Orders may be multi-leg orders, including Complex Orders, as defined in BOX Rule 7240(a)(5) and tied to hedge orders as defined in IM-7600-2.

Order.<sup>14</sup> A Floor Broker may, but is not required to, provide a “book sweep size” for the contra-side of the QOO Order, which is the number of contracts, if any, of the contra-side order that the Floor Broker is willing to relinquish to orders and quotes on the BOX Book that have priority pursuant to proposed BOX Rule 7600(c).<sup>15</sup>

Prior to execution, the Floor Broker would be required to represent the order in the specific Crowd Area<sup>16</sup> designated for trading that particular options class in a process called the “market probe” (also known as “open outcry”).<sup>17</sup> The proposed BOX floor would consist of at least one “Crowd Area,” each marked with specific visible boundaries, as determined by the Exchange.<sup>18</sup> All series for a particular option class would be allocated to the same Crowd Area.<sup>19</sup> During the market probe, Floor Market Makers<sup>20</sup> physically located in the specific Crowd Area would be considered participants in the crowd and would be able to express interest in trading against the agency order. The Floor Broker would be responsible for determining the sequence in which bids or offers are vocalized on the trading floor in response to the Floor Broker’s bid, offer, or call for a market.<sup>21</sup>

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<sup>14</sup> See proposed BOX Rule 7600(a)(1).

<sup>15</sup> See proposed BOX Rule 7600(h).

<sup>16</sup> BOX’s proposed trading floor will consist of at least one “Crowd Area” or “Pit.” See proposed BOX Rule 100(a)(67).

<sup>17</sup> See proposed BOX Rule 7600(b). Under the proposed rules, an Options Exchange Official would be required to certify that the Floor Broker adequately represented the QOO Order to the trading crowd. See *id.*

<sup>18</sup> See proposed BOX Rule 100(a)(67).

<sup>19</sup> See *id.*

<sup>20</sup> See proposed BOX Rule 8510(b).

<sup>21</sup> See proposed BOX Rule 7600(d)(1). Any disputes regarding a Floor Broker’s determination of time priority sequence will be resolved by the Options Exchange Official. See *id.*

After the market probe, the Floor Broker would submit the QOO Order through the BOX Order Gateway (“BOG”).<sup>22</sup> Once an order is received by the BOG, it would be immediately sent to the Trading Host<sup>23</sup> for execution.<sup>24</sup> The QOO Order would not be deemed executed until it is received and processed by the Trading Host.<sup>25</sup> For a non-complex QOO Order, the execution price must be equal to or better than the NBBO.<sup>26</sup> Additionally, the following BOX Book interest would have priority over the contra-side of the QOO Order: (i) any equal or better priced Public Customer<sup>27</sup> bids or offers on the BOX Book; (ii) any non-Public Customer bids or offers on the BOX Book that are ranked ahead of such equal or better priced Public Customer bids or offers; and (iii) any non-Public Customer bids or offers on the BOX Book that are priced better than the proposed execution price.<sup>28</sup> If the number of contracts on the BOX Book that have priority over the contra-side of the QOO Order is greater than the book sweep size set by the Floor Broker, then the QOO Order will be rejected.<sup>29</sup> Otherwise, after priority interest on the BOX Book, if any, is executed, the remaining balance will be matched against the contra-side of

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<sup>22</sup> See proposed BOX Rule 100(b)(2). All transactions occurring on the trading floor would be required to be processed through the BOG. See proposed BOX Floor Rule 7580(e)(1).

<sup>23</sup> “Trading Host” means the automated trading system used by BOX for the trading of options contracts. See BOX Rule 100(a)(66).

<sup>24</sup> See proposed BOX Rule 7580(e)(1). Under the proposal, orders on the trading floor would not route to an away exchange. See proposed BOX Rule 7580(e)(2).

<sup>25</sup> See proposed Rule 7600(c).

<sup>26</sup> See proposed BOX Rule 7600(c). The relevant priority BOX Book interest for complex QOO Orders is described in proposed BOX Rule 7600(c).

<sup>27</sup> “Public Customer” means a person that is not a broker or dealer in securities. See BOX Rule 100(a)(51).

<sup>28</sup> See proposed Rule 7600(c).

<sup>29</sup> See proposed Rule 7600(h). The Exchange believes that the book sweep size feature will assist Floor Brokers in executing orders when there are bids or offers on the BOX Book that have priority over the QOO Order, which BOX believes will result in a greater number of executions. See Notice, supra note 3, at 87612.

the QOO Order, regardless of whether the contra-side order submitted by the Floor Broker is ultimately entitled to receive an allocation.<sup>30</sup>

The executing Floor Broker would also be responsible for ensuring that any Floor Participant<sup>31</sup> that responded with interest during the market probe receives their allocation, and if interest was discovered during the market probe, the Floor Broker is required to enter the correct allocations into the Exchange's system where the trade will be recorded.<sup>32</sup> If the QOO Order is a certain size, determined by the Exchange on an option by option basis (at a size that may not be less than 500 contracts), the Floor Broker would be entitled to cross, after all equal or better priced Public Customer bids or offers on the BOX Book and any non-Public Customer bids or offers that are ranked ahead of such Public Customer bids or offers are filled, 40% of the remaining contracts in the order.<sup>33</sup> The Floor Broker is permitted to trade more than their percentage entitlement if other Floor Participants in the trading crowd do not choose to trade the remaining portion of the order.<sup>34</sup> Additionally, Floor Brokers would be responsible for handling all orders in accordance with the Exchange's priority and trade-through rules.<sup>35</sup>

#### B. Floor Market Makers

Proposed BOX Rule 8500(a) would require market makers on the BOX Floor to also be registered with BOX as a market maker on its electronic trading platform. As market makers on BOX's electronic trading platform, Floor Market Makers would have a continuous electronic

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<sup>30</sup> See proposed BOX Rule 7600(d).

<sup>31</sup> The term "Floor Participant" means Floor Brokers as defined in Rule 7540 and Floor Market Makers as defined in Rule 8510(b). See proposed BOX Rule 100(a)(26).

<sup>32</sup> See proposed BOX Rule 7600(d).

<sup>33</sup> See proposed BOX Rule 7600(f).

<sup>34</sup> See proposed BOX Rule 7600(f)(4).

<sup>35</sup> See proposed BOX Rule 7580(e)(2).

quoting obligation pursuant to proposed BOX Rule 8510(c)(1), which would require Floor Market Makers to quote electronically in all classes that they quote on the trading floor.<sup>36</sup> The Exchange believes that these electronic quoting requirements will preserve liquidity in BOX's electronic marketplace, which might otherwise decrease with the launch of BOX's trading floor.<sup>37</sup> The Exchange also notes that the electronic quoting requirements are already in place on BOX's electronic book, and would be uniformly applied to all BOX market makers, both floor and electronic.<sup>38</sup>

In addition, proposed BOX Rule 100(b)(5) would require a Floor Market Maker to be considered "in" on a bid or offer only if the Floor Market Maker makes an affirmative assertion that he is "in."<sup>39</sup> Specifically, the proposed rule states that a Floor Market Maker "shall be considered 'out' on a bid or offer if he does not respond to the Floor Broker who is announcing the order."<sup>40</sup> The Exchange believes that requiring an affirmative response from Floor Market Makers will enhance the efficiency of order execution on the trading floor because it will prevent unnecessary delays associated with requiring every Floor Market Maker to affirmatively opt "out" of an order before it is executed.<sup>41</sup>

The BOX proposal would not impose a requirement on market makers to be present in the trading crowd before a Floor Broker may represent an order to the trading crowd.<sup>42</sup> The Exchange notes that even if a Floor Market Maker is not present, any orders executed by a Floor

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<sup>36</sup> See proposed BOX Rule 8510(c)(1).

<sup>37</sup> See Notice, *supra* note 3, at 87627.

<sup>38</sup> See *id.* at 87627-28.

<sup>39</sup> See proposed BOX Rule 100(b)(5).

<sup>40</sup> See *id.*

<sup>41</sup> See Notice, *supra* note 3, at 87608, n.9.

<sup>42</sup> See *id.* at 87610, n.32.

Broker without exposure to participants in the trading crowd will still have to respect priority interest on the BOX Book, and that all classes listed on BOX must have at least one Market Maker quoting electronically. Therefore, the Exchange believes that there will be electronic quotes in the particular class even if no Floor Market Maker is present when the QOO Order is announced. Additionally, the Exchange notes that all orders executed on the trading floor must trade at a price equal to or better than the NBBO regardless of whether a Floor Market Maker is present in the Crowd Area when the order is announced. The Exchange further states that the robust electronic quoting of options that will be traded on the trading floor “eliminates any concerns of not having a Floor Market Maker present when the order is executed by the Floor Broker due to the fact that there are other Market Makers providing electronic quotations.”<sup>43</sup>

### III. Summary of Comments

As previously noted, the Commission received three comment letters on the proposed rule change, and one response letter from BOX. All three commenters raised specific concerns with respect to the proposed rule change,<sup>44</sup> and two of the three commenters raised concerns about issues relating to options trading floors in general.<sup>45</sup> No commenter expressed support for the proposed rule change.

Commenters raised concerns about the following aspects of the proposal, each of which is discussed in greater detail below: (1) whether the proposal would impede opportunities for price improvement; (2) the requirement that Floor Market Makers quote electronically in all

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<sup>43</sup> See Notice, supra note 3, at 87625.

<sup>44</sup> See CBOE Letter, CTC Letter, and Nasdaq Letter, supra note 5.

<sup>45</sup> See CTC Letter and Nasdaq Letter, supra note 5. The Commission notes that these commenters expressed concerns about options floors in general and requested Commission action on certain issues related to existing options trading floors that are beyond the scope of the BOX proposal.

classes offered on the proposed BOX trading floor; (3) the ability for a Floor Broker to execute a trade in the absence of any Floor Market Maker; (4) the restriction of Floor Market Makers to a “single crowd area at a time;” (5) the book sweep size feature; (6) the lack of clarity regarding compliance with trade-through and priority rules; (7) the lack of a single-sided order type on the proposed floor; and (8) the potential impact on options market structure.

A. Opportunities for Price Improvement

Two commenters expressed concern that the proposed rule change would negatively impact opportunities for orders to receive price improvement.<sup>46</sup> Specifically, one commenter stated that the proposed rule change is “structured to minimize the ability of market maker and public customer trading interest to interact with, and provide price improvement to, orders being crossed on the BOX floor.”<sup>47</sup> This commenter claimed that the proposed rule change “is simply offering a frictionless crossing mechanism, which can be utilized to the detriment of customers.”<sup>48</sup> Another commenter stated that the proposed rule change will not ensure robust market maker participation on the proposed BOX floor, and this would provide a way for internalizers to avoid exposure to market makers who might otherwise provide price improvement.<sup>49</sup>

B. Requirement for Floor Market Makers to Quote Electronically in All Classes Offered on the Proposed BOX Floor

Two commenters expressed concern with the proposed requirement that Floor Market Makers would have to quote electronically in all classes offered on the proposed trading floor.<sup>50</sup>

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<sup>46</sup> See CBOE Letter and CTC Letter, supra note 5.

<sup>47</sup> See CBOE Letter, supra note 5, at 1-2.

<sup>48</sup> See id. at 2.

<sup>49</sup> See CTC Letter, supra note 5, at 4-5.

<sup>50</sup> See CBOE Letter and CTC Letter, supra note 5.

One commenter stated that the “imposition” of an electronic quoting requirement could limit potential market maker price improvement.<sup>51</sup> Another commenter suggested that the proposed requirement appears to “be a means to impose a costly and unprofitable burden on would-be Market Makers, thereby discouraging them from establishing a presence on the BOX floor and preserving the value of the proposed floor as a crossing venue devoid of meaningful order exposure or price improvement.”<sup>52</sup> This commenter further argued that the proposed rule change would discourage competitive market maker participation on the proposed BOX floor.<sup>53</sup>

In response to the commenter’s suggestion that the requirement to quote electronically would discourage market makers from establishing a presence on the BOX floor, BOX stated that to the contrary, it believes the proposed rule change will ensure that electronic quoting keeps pace with the robust level of activity anticipated on the trading floor.<sup>54</sup> In this regard, BOX further stated that the requirement to quote electronically can help ensure that market making activity on the trading floor does not diminish electronic quoting on BOX.<sup>55</sup>

C. Ability to Execute a Trade in the Absence of a Floor Market Maker

One commenter expressed concern that the proposed rule change would allow a Floor Broker to execute crossing orders on the BOX Floor when no Floor Market Makers are present.<sup>56</sup> The commenter argued that existing options trading floors grew from crowded equities or futures

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<sup>51</sup> See CBOE Letter, supra note 5, at 2, n.2.

<sup>52</sup> See CTC Letter, supra note 5, at 5.

<sup>53</sup> See id. at 5.

<sup>54</sup> See BOX Response Letter, supra note 6, at 3. BOX also noted its belief that commenter’s concerns about the finite resources available to firms to staff another physical trading floor are beyond the scope of this proposal. See id. at 4.

<sup>55</sup> See id. at 3.

<sup>56</sup> See CTC Letter, supra note 5, at 4.

floors and so were certain to have robust and active market maker populations.<sup>57</sup> The commenter further stated that the lack of rules to ensure robust market maker participation on the proposed BOX floor would provide a way for internalizers to avoid exposure to market makers, and would act directly counter to investor protection and the public interest.<sup>58</sup>

In response to the commenter's concern regarding the absence of a requirement that Floor Market Makers be present when an order is represented, BOX stated that allowing a Floor Broker to execute an order when no Floor Market Maker is present is "simply a safeguard to ensure that the trading floor operates efficiently and without undue delays or interruptions."<sup>59</sup> BOX further stated that there are other protections in place even if a pit may not have a Market Maker present when a Floor Broker crosses an order.<sup>60</sup> According to BOX, these protections include a requirement that orders must not trade at a price worse than the NBBO, orders must respect the BOX Book, and orders represented to the trading crowd must be certified by an options exchange official as being adequately represented to the crowd.<sup>61</sup> Additionally, BOX noted that Floor Brokers may not violate priority and trade-through rules and must honor their obligations to their customers, including their best execution obligations.

#### D. Restriction of Floor Market Makers to a Single Crowd Area

Two commenters expressed concern regarding the proposed rule change's description and application of physical boundary requirements.<sup>62</sup> One commenter suggested that "physical boundary requirements" in the proposed rule change would limit potential opportunities for

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<sup>57</sup> See id.

<sup>58</sup> See id. at 5.

<sup>59</sup> See BOX Response Letter, supra note 6, at 3.

<sup>60</sup> See id.

<sup>61</sup> See id.

<sup>62</sup> See CBOE Letter and CTC Letter, supra note 5.

market maker price improvement.<sup>63</sup> Another commenter suggested that the proposal to allow a Floor Market Maker to participate in a crowd only if he or she is physically located in a specific Crowd Area “at the time the order is represented in the crowd” is designed to discourage Floor Market Makers from providing liquidity.<sup>64</sup> The commenter suggested that the Exchange could open a trading floor comprised of a single Crowd Area with rules permitting all Floor Market Makers to trade all issues as a means to help ensure opportunities for price improvement.<sup>65</sup>

In response, BOX stated that the ability to divide the trading floor into multiple pits or crowd areas would aid BOX in monitoring trading activity and ensuring the trading floor operates in an orderly manner.<sup>66</sup> BOX also noted that trading floors on other exchanges also have multiple crowd areas or pits.<sup>67</sup>

E. Book Sweep Size Mechanism

One commenter expressed concern about the proposed “book sweep size” mechanism in the proposed rule change.<sup>68</sup> This commenter suggested that the book sweep size would be a feature that “explicitly prevents executions of orders on the BOX Book.”<sup>69</sup> The commenter further stated that the book sweep mechanism could prevent orders from executing in circumstances where there are orders on the BOX Book that could fill the order, possibly at a better price, and thus the mechanism “puts its participants’ compliance with best-execution

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<sup>63</sup> See CBOE Letter, supra note 5, at 2, n.2.

<sup>64</sup> See CTC Letter, supra note 5, at 6.

<sup>65</sup> See id. at 6.

<sup>66</sup> See BOX Response Letter, supra note 6, at 2.

<sup>67</sup> See id. at 2. BOX noted its belief that CBOE, PHLX, and NYSE Arca all have multiple crowd areas or pits on their respective trading floors. See id. at 2, n.11.

<sup>68</sup> See CTC Letter, supra note 5, at 7.

<sup>69</sup> See id. at 7.

obligations at risk and unfairly discriminates against investors with executable orders resting in the BOX Book.”<sup>70</sup>

In response to the commenter’s concerns regarding the book sweep size aspect of the proposal, BOX stated that the book sweep size is a tool that will aid Floor Brokers in satisfying duties owed to their customers, such as best execution.<sup>71</sup> For example, according to BOX, when a Floor Broker needs an order to be executed immediately, the broker could opt either to provide a book sweep size equal to the entire size of the order, which provides liquidity to the BOX Book, or to provide an execution price that is better than the current best price on BOX, which presents an opportunity for potential price improvement.<sup>72</sup> BOX also noted that it believes functionality similar to the book sweep size mechanism is available on at least one other trading floor, so the book sweep size aspect of its proposal is not unique.<sup>73</sup>

#### F. Compliance With Trade-Through and Priority Rules

One commenter stated that the proposed rule change is unclear regarding whether or not the proposed BOG trading system would systematically prevent violations of priority and trade-through requirements.<sup>74</sup> This commenter further stated that it is unclear whether exposure in the trading crowd is required and whether the market against which trades are validated differs depending on the method of execution.<sup>75</sup> Specifically, the commenter claimed that the proposed rule change “does not describe the process for validation of trades and whether validation occurs

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<sup>70</sup> See id. at 7-8.

<sup>71</sup> See BOX Response Letter, supra note 6, at 3-4.

<sup>72</sup> See id. at 4.

<sup>73</sup> See id. at 4. BOX states that the book sweep size mechanism is comparable to the PHLX Floor Broker Management System.

<sup>74</sup> See Nasdaq Letter, supra note 5, at 2.

<sup>75</sup> See id.

at the time of the Verbal Agreement or Reported Trade.”<sup>76</sup> Additionally, this commenter stated that the proposed rule change does not discuss the specific manner in which surveillance reviews transactions for violations of Exchange rules or the manner in which the BOG or the Exchange enforces compliance for on-floor transactions.<sup>77</sup>

In response to the commenter’s concern that the proposed rule change is unclear about whether the BOG would systematically prevent violations of priority and trade-through requirements, BOX stated that the method by which trades are received and processed by the Trading Host serves as a safeguard to prevent violations of the priority and trade-through requirements.<sup>78</sup> BOX further stated that it “has specifically designed the Proposal to prevent trade-through violations and protect priority interest on the BOX Book.”<sup>79</sup> In response to the commenter’s suggestion that the proposed rule change does not adequately discuss surveillance, BOX stated it has “robust surveillance procedures in place to monitor compliance with the Exchange’s rules.”<sup>80</sup> BOX further stated that their surveillance procedures will be used to monitor transactions occurring on the trading floor.

#### G. Lack of Single-Sided Floor Order Type

One commenter raised concerns about the inability of floor participants to represent single sided orders on the proposed BOX Floor.<sup>81</sup> In response to the commenter’s concern about floor participants not being able to represent a single-sided order on the proposed BOX Floor, BOX stated that a Floor Broker may bring any unmatched order to the trading floor to seek

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<sup>76</sup> See id.

<sup>77</sup> See id. at 3.

<sup>78</sup> See BOX Response Letter, supra note 6, at 1.

<sup>79</sup> See id. at 2.

<sup>80</sup> See id.

<sup>81</sup> See CBOE Letter, supra note 5, at 2, n.2.

liquidity, and then enter the order into the BOX system using the QOO order type.<sup>82</sup> BOX noted that Floor Brokers also may enter single-sided orders into the BOX Book using BOX’s electronic interface.<sup>83</sup>

#### H. Potential Impact on Options Market Structure

Two commenters expressed concern that the proposed rule change would increase fragmentation of the options market.<sup>84</sup> One commenter stated that “[f]ragmentation is a growing concern in the U.S. securities markets,” and that the proposed BOX floor would “add[] yet another trading venue that must be staffed by firms with finite resources and liquidity without offering anything unique or beneficial to customers.”<sup>85</sup> Another commenter stated that opening a new trading floor will exacerbate the practice of “venue shopping,” and noted that the “number of market making firms is limited,” and that “market making firms lack infinite resources to staff an arbitrary number of physical trading floors with dedicated personnel.”<sup>86</sup> This commenter further suggested that the proposed rule could “open the floodgates” for new options trading floors, “engendering serious fragmentation of liquidity, imposing significant new costs on market making firms by obliging them to staff every floor or incur large opportunity costs.”<sup>87</sup>

In response, BOX argued that concerns about the general success of options trading floors is beyond the scope of its proposal.<sup>88</sup> BOX further asserted that commenters’ general

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<sup>82</sup> See BOX Response Letter, supra note 6, at 4.

<sup>83</sup> See id. at 4.

<sup>84</sup> See CBOE Letter and CTC Letter, supra note 5.

<sup>85</sup> See CBOE Letter, supra note 5, at 1.

<sup>86</sup> See CTC Letter, supra note 5, at 3.

<sup>87</sup> See CTC Letter, supra note 5, at 4.

<sup>88</sup> See BOX Response Letter, supra note 6, at 4.

concerns about options trading floors lack merit or are an attempt to delay the approval of its proposal.<sup>89</sup>

IV. Proceedings to Determine Whether to Approve or Disapprove SR-BOX-2016-48 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act,<sup>90</sup> to determine whether the proposed rule change, as modified by Amendment No. 1, should be approved or disapproved. Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described in greater detail below, the Commission seeks and encourages interested persons to comment on the proposed rule change to inform the Commission's analysis of whether to approve or disapprove the proposed rule change, as modified by Amendment No. 1.

Pursuant to Section 19(b)(2)(B) of the Act,<sup>91</sup> the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings because the proposal raises important issues that warrant further public comment and Commission consideration. The Commission is instituting proceedings to allow for additional analysis of, and input from commenters with respect to, the proposed rule change's consistency

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<sup>89</sup> See id.

<sup>90</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>91</sup> Id. Section 19(b)(2)(B) of the Act provides that proceedings to determine whether to disapprove a proposed rule change must be concluded within 180 days of the date of publication of the notice of the filing of the proposed rule change. The time for conclusion of the proceedings may be extended for up to 60 days if the Commission finds good cause for such extension and publishes its reasons for so finding. See id.

with Section 6(b)(5) of the Act,<sup>92</sup> which requires that the rules of a national securities exchange be designed, among other things, 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 and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers. In addition, the Commission is instituting proceedings to allow for additional analysis of, and input from commenters with respect to, whether or not the proposed rule change is consistent with Section 6(b)(8) of the Act, which requires the rules a national securities exchange not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.<sup>93</sup>

Specifically, the Commission notes that aspects of the proposed rule change may not be consistent with Section 6(b)(5) of the Act in that they could effectively limit the exposure of floor orders to a bona fide open outcry auction process, which could lead to, among other things, inefficient pricing for crossing transactions executed on the proposed BOX floor. In addition, the Commission notes that the impediments to becoming, and restrictions on, Floor Market Makers may impose a burden on competition that is inconsistent with 6(b)(8) of the Act. The Commission also notes that the proposed rule change raises questions regarding the ability of the Exchange and participants on the BOX trading floor to comply with the Act, Commission and/or Exchange rules regarding intramarket priority and intermarket trade-through.

Finally, under the Commission's rules of procedure, a self-regulatory organization that proposes to amend its rules bears the burden of demonstrating that its proposal is consistent with

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<sup>92</sup> 15 U.S.C. 78f(b)(5).

<sup>93</sup> 15 U.S.C. § 78f(b)(8).

the Act.<sup>94</sup> In this regard:

the description of the proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with the applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding. Any failure of the self-regulatory organization to provide the information elicited by Form 19b-4 may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Exchange Act and the rules and regulations thereunder that are applicable to the self-regulation organization.<sup>95</sup>

V. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the concerns identified above, as well as any other concerns they may have with the proposal, as modified by Amendment No. 1. In particular, the Commission invites the written views of interested persons concerning whether the proposal, as modified by Amendment No. 1, is consistent with Sections 6(b)(5)<sup>96</sup> and 6(b)(8),<sup>97</sup> or any other provision of the Act, or the rules and regulations thereunder. Although there do not appear to be any issues relevant to approval or disapproval which would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.<sup>98</sup> In particular, the Commission seeks comment on the following:

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<sup>94</sup> Rule 700(b)(3), 17 CFR 201.700(b)(3).

<sup>95</sup> Id.

<sup>96</sup> 15 U.S.C. 78f(b)(5).

<sup>97</sup> 15 U.S.C. 78f(b)(8).

<sup>98</sup> Section 19(b)(2) of the Act, as amended by the Securities Acts Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Repts. No. 75, 94th Cong., 1st Sess. 30 (1975).

- Commenters’ views on the proposed requirement that a Floor Market Maker may only quote in classes on the trading floor which the market maker is already quoting electronically;<sup>99</sup>
- Commenters’ views on the aspect of the proposal that would allow a BOX Floor Broker to execute a crossing transaction without first exposing the order to any other Floor Participant;
- Commenters’ views on whether a minimum number of Floor Market Makers should be required to be present when an order is represented to the trading crowd, and if so, how many Floor Market Makers in each class should be required;
- Commenters’ views on the proposed book sweep size feature;<sup>100</sup>
- Commenters’ views on the aspect of the proposal that would require a Floor Market Maker to be physically located in a specific Crowd Area to be deemed participating in the crowd;<sup>101</sup>
- Commenters’ views on the Exchange’s argument that requiring “an affirmative response by a Floor Market Maker will allow for a more efficient process for executing orders on the Trading Floor” and that requiring a Floor Market Maker to affirmatively be “out” on every order “will lead to unnecessary delays on the Trading Floor and has the potential to cause disruptions.”<sup>102</sup>

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<sup>99</sup> See proposed BOX Rule 8500(a).

<sup>100</sup> See proposed BOX Rule 7600(h).

<sup>101</sup> See proposed BOX Rule IM-8510-2.

<sup>102</sup> See Notice, supra note 3, at 87608, n.9.

- Commenters' views on whether the provision allowing the Exchange the discretion to determine whether a Floor Broker examination could be required as a prerequisite to becoming a Floor Broker is consistent with the Act;<sup>103</sup>
- Whether the Exchange adequately describes how it will validate a trade for purposes of compliance with trade-through, priority and other Exchange rules; and
- Whether the Exchange adequately describes the mechanics of how orders will be received and executed on the proposed BOX trading floor.

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 1 and regarding whether the proposed rule change, as modified by Amendment No. 1, should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register].

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-2016-48 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-BOX-2016-48. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

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<sup>103</sup> See proposed BOX Rule 7550.

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 accommodation proposal that are filed with the Commission, and all written communications relating to the accommodation proposal 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 such filings also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer

to File Number SR-BOX-2016-48 and should be submitted on or before [insert date 21 days from publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>104</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>104</sup> 17 CFR 200.30–3(a)(57).