

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-74718; File No. SR-C2-2015-006)

April 13, 2015

Self-Regulatory Organizations; C2 Options Exchange, Incorporated; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Exchange Opening Procedures

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934 (the “Act”)² and Rule 19b-4 thereunder,³ notice is hereby given that, on April 2, 2015, C2 Options Exchange, Incorporated (the “Exchange” or “C2”) 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 amend Rule 6.11 to provide additional clarity regarding the Exchange’s opening procedures. The text of the proposed rule change is provided below.

(additions are italicized; deletions are [bracketed])

* * * * *

**C2 Options Exchange, Incorporated
Rules**

* * * * *

Rule 6.11. Openings (and sometimes Closings)

(a) – (d) No change.

(e) Opening Conditions: Subject to subparagraph (f) below, the System will not open a series if one of the following conditions is met:

¹ 15 U.S.C. 78s(b)(1).

² 15 U.S.C. 78a.

³ 17 CFR 240.19b-4.

- (1) There is no quote present in the series;
- (2) The opening price is not within an acceptable range (as determined by the Exchange) compared to the lowest quote offer and the highest quote bid;
- (3) The opening trade would be at a price that is not the NBBO; or
- (4) The opening trade would leave a market order imbalance (i.e., there are more market orders to buy or to sell for the particular series than can be satisfied by the limit orders, quotes and market orders on the opposite side); however, in series that will open at a minimum price increment (e.g., at a price of \$0.05 or, in penny series, at a price of \$0.01), the System will open even if a sell market order imbalance exists.

(f) Presence of Opening Conditions:

- (1) If the condition in paragraph (e)(1) is present, the System will check to see if there is an NBBO quote on another market that falls within the acceptable opening range. If such an NBBO quote is present, the series will open and expose the marketable order(s) at the NBBO price. If such an NBBO quote is not present, the System will not open the series and will send a notification to Participants indicating the reason.
- (2) If the condition in paragraph (e)(2) is present, the System will match orders and quotes to the extent possible at a single clearing price within the acceptable range and then expose the remaining marketable order(s) at the widest price point within the acceptable opening range or the NBBO price, whichever is better.
- (3) If the condition in paragraph (e)(3) is present, the System will match orders and quotes to the extent possible at a single clearing price within the acceptable opening range or the NBBO price, whichever is better, and then expose the remaining marketable order(s) at the NBBO price.
- (4) If the condition in paragraph (e)(4) is present, the System will match orders and quotes to the extent possible at a single clearing price and then expose the remaining marketable order(s) at the widest price point within the acceptable opening range or the NBBO price, whichever is better.

(g) – (j) No change.

. . . Interpretations and Policies

.01 – .03 No change.

.04 Opening Auction Exposure: The Exchange may determine to expose orders at the opening via auction including under any of the scenarios described in paragraphs (f)(1)-(4) above. In such cases, the exposure process will be conducted via the Hybrid Agency Liaison (“HAL”) pursuant to Rule 6.18. Any remaining balance of orders not executed via HAL on the opening will be booked

at their limit price to the extent consistent with Rule 6.10 except that any remaining balance of orders not executed via HAL on the opening that are priced, or would be executed at a price, that is not within an acceptable tick distance from the initial HAL price will be cancelled. An "acceptable tick distance" ("ATD") shall be determined by the Exchange on a series-by-series and premium basis and shall be no less than 2 minimum increment ticks. When the HAL Opening Auction Exposure procedure is activated, the ATD will be the same as the ATD established under Rule 6.17.

* * * * *

The text of the proposed rule change is also available on the Exchange's website (<http://www.cboe.com/AboutCBOE/CBOELegalRegulatoryHome.aspx>), at the Exchange's Office of the Secretary, 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

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 is proposing to adopt Interpretation and Policy .04 to Rule 6.11 relating to the Exchange's opening procedures to provide additional clarity in the Rules regarding the manner in which marketable orders may be exposed at the opening of trading. Specifically, proposed Interpretation and Policy .04 to Rule 6.11 would provide that the Exchange may determine to expose marketable orders on the opening via the Hybrid Agency Liaison ("HAL") auction procedures described in Rule 6.18.⁴ Proposed Interpretation and Policy .04 to Rule 6.11

⁴ Such determination as to whether to expose marketable orders on the opening via the

would also provide that any remaining balance of orders not executed via HAL on the opening will be booked at their limit price to the extent consistent with Rule 6.10⁵ except that any remaining balance of orders not executed via HAL on the opening that are priced, or would be executed at a price, that is not within an acceptable tick distance from the initial HAL price will be cancelled..^[sic]⁶ The proposed Interpretation and Policy is substantially based, in all material respects, on the HAL Opening Procedure set forth in Interpretation and Policy .03 to Chicago Board Options Exchange, Incorporated (“CBOE”) Rule 6.2B (Hybrid Opening System (“HOSS”)).

Under the Exchange’s current opening procedures, pre-opening orders and quotes and orders resting in the book from the prior business day are matched in the Exchange’s automated trading system (“System”) at a single clearing price.⁷ Bids and offers that cannot be matched at a single clearing price are left to rest in the book. Subject to certain conditions, the System will not open a series for trading if there are no quotes in the series, the opening price is not within an acceptable range (as determined by the Exchange) compared to the lowest quote offer and the

HAL auction procedures described in Rule 6.18 would be made prior to activation and announced via Regulatory Circular.

⁵ Notably, certain order types, or portions thereof, may not, by rule, be booked. See, e.g., Rule 6.10(6) (Immediate-or-Cancel Order); 6.10(7) (Opening Rotation Order). Accordingly, under proposed Interpretation .04 to Rule 6.11, any remaining balance of orders not executed via HAL on the opening would be booked at their limit price, but only to the extent consistent with Rule 6.10.

⁶ This includes a market order, which cannot be filled in total. In such cases, the remainder of a market order would be cancelled when the order cannot be filled on an away exchange and no quotes are present on C2.

⁷ In determining the priority of orders and quotes to be traded at a single clearing price, the System gives priority to market orders first, then to limit orders and quotes whose price is better than the opening price, and then to limit orders and quotes at the opening price. See Rule 6.11(g)(1).

highest quote bid⁸ or at a price at or within the national best bid or offer (“NBBO”), or the opening trade would leave an order imbalance.⁹ If one of these conditions is present at the opening, the Exchange will follow the opening procedures set forth in Rule 6.11(f) (as described below) to open trading in the affected series. Notably, each of the procedures described in Rule 6.11(f) explicitly permit the Exchange to expose marketable orders at the opening of trading.¹⁰

For example, under Rule 6.11(f)(1), if a marketable order is resting in the book of a series for which no quotes are disseminated on the Exchange, the System will look for another market that is quoting the NBBO within an acceptable opening price range. If such quotes exist, the System will open the series and expose the marketable order at the NBBO. If there are no quotes on C2 and no quotes on any away exchange that are within the APR for the series, the System will not open the series and will send a notification to participants indicating the reason. Thus, assume that the NBBO for a particular option is \$1.00 - \$1.20 for 100 contracts on either side. The APR in the series is set at \$0.50 above the \$0.375 minimum APR for series with quote bids less than \$2.00. There are no quotes in the series on C2, but there is a market order to buy 100

⁸ The Exchange will not automatically execute eligible orders that are marketable if (1) the width between the national best bid and national best offer is not within an acceptable price range (as determined by the Exchange on a series by series basis for market orders and/or marketable limit orders and announced to the Trading Permit Holders via Regulatory Circular), or (2) the execution would follow an initial partial execution on the Exchange and would be at a subsequent price that is not within an acceptable tick distance from the initial execution (as determined by the Exchange on a series by series and premium basis for market orders and/or marketable limit orders and announced to the Trading Permit Holders via Regulatory Circular). The “acceptable price range” (“APR”) shall be determined by the Exchange on a class-by-class basis and shall be no less than: \$0.375 between the bid and offer for each option contract for which the bid is less than \$2, \$0.60 where the bid is at least \$2 but does not exceed \$5, \$0.75 where the bid is more than \$5 but does not exceed \$10, \$1.20 where the bid is more than \$10 but does not exceed \$20, and \$1.50 where the bid is more than \$20. An “acceptable tick distance” (“ATD”) shall be no less than 2 minimum increment ticks. See Rule 6.17.

⁹ See Rule 6.11(e).

¹⁰ See also Rule 6.11(g)(2).

contracts in the book. In this case, the System would verify that the NBBO quotes on the away exchange were within the APR for the series (the midpoint of the NBBO (i.e. \$1.00 - \$1.20) plus or minus half of the APR (i.e. \$0.25 in either direction of the midpoint or \$0.85 - \$1.35) and, if within the acceptable opening range (i.e. \$1.20 is within the APR), expose the marketable buy order at the NBO price of \$1.20.

Under Rule 6.11(f)(2), if the opening price is not within an acceptable range compared to the lowest quote offer and highest quote bid, the System will match orders and quotes to the extent possible at a single clearing price within the acceptable range and then expose the remaining marketable order(s) at the widest price point within the acceptable price range or the NBBO price, whichever is better. For example, assume that the NBBO for a particular option is \$0.90 - \$1.50 for 100 contracts on either side. The highest quote bid and lowest quote offer at C2 are \$0.80 - \$1.50 each for 100 contracts. Again, the APR for series in which the quote bid is less than \$2.00 is \$0.50 and there is a customer order in the book to buy 100 contracts at the market price. In this case, the System would check the marketable price of \$1.50 for the trade against the APR for the series (i.e. the midpoint between the highest bid and lowest offer (i.e. \$1.15) plus or minus half of the APR (i.e. \$0.25) or \$0.90 - \$1.40) and determine that the marketable price of \$1.50 would not be within the APR. The System would then expose the order at the widest point within the APR (i.e. \$1.40) or the NBBO (i.e. \$1.50), whichever is better. Thus, in this case the order would be exposed at \$1.40 (and booked provided there is no contra interest expressed at \$1.40 or better during the exposure period).

Similarly, Rule 6.11(f)(3) provides that if the opening trade would be at a price that is not the NBBO, the System will match orders and quotes to the extent possible at a single clearing price within the APR or the NBBO, whichever is better, and then expose the remaining

marketable order(s) at the NBBO. For example, assume that the NBBO for a particular option is \$0.05 - \$1.25 for 100 contracts on either side. The highest quote bid and lowest quote offer on C2 are \$0.05 - \$1.75 respectively, each for 100 contracts. Again, because the quote bid for the series is less than \$2.00, the APR is \$0.50. A customer order to buy 100 contracts at the market is resting in the book. In this case, the System would be unable to match the market with any quote (i.e. \$1.75) within the APR (i.e. \$1.10 (the midpoint between the highest bid and lowest offer (i.e. \$0.85) plus or minus half of the APR (i.e. \$0.25) or \$0.60 - \$1.10) or the NBO of \$1.25. Accordingly, the System would expose the order at the NBO of \$1.25.

Finally, if the opening trade would leave a market order imbalance, the System will match orders and quotes to the extent possible at a single clearing price and then expose the remaining marketable order(s) at the widest price point within the APR or the NBBO, whichever is better pursuant to Rule 6.11(f)(4). For example, assume that the NBBO for a particular option is \$1.00 - \$1.20 with quotes for 100 contracts on each side. The highest quote bid on CBOE is \$1.00 for 100 contracts and lowest quote offer is \$1.20 for 10 contracts. The quote bid being less than \$2.00, the APR is \$0.50. There is a customer order in the book to buy 100 contracts at the market. There are no other quotes or orders in the book. In this case, the System would match the orders and quotes at \$1.20 (within the APR of \$0.85 - \$1.35) and allocate 10 contracts according to the matching algorithm in effect in the class and the applicable rules. The remaining 90 contracts would then be exposed at the better of the widest point within the APR or the NBO (in this case \$1.20). Thus, each of the four scenarios for permitting the opening of trading in a series in which one of the four conditions described in Rule 6.11(e) is present contemplate exposing marketable orders at the NBBO (or, if better, the widest point of the APR).

Although Rule 6.11 expressly permits exposure of orders on the open, Rule 6.11 does not set forth a specific process by which orders will be exposed or specify how such orders be handled after they are exposed.¹¹ While the Exchange believes that Rule 6.11(g)(2) makes clear that such exposure may be via auction,¹² the Exchange also believes that additional detail should be added to the Rules to further clarify the auction process on the opening.¹³ Proposed Interpretation and Policy .04 to Rule 6.11 is intended to add this additional detail in the Rules. Specifically, the Exchange proposes to amend Rule 6.11 to include reference to the Exchange's HAL procedures. The Interpretation and Policy would provide that the Exchange could

¹¹ See Rule 6.11(g)(2) providing that all orders exposed pursuant to Rule 6.11 shall be exposed for a period of time designated by the Exchange that does not exceed 1.5 seconds.

¹² Under Rule 6.11(g)(2), "All orders exposed pursuant to this Rule [6.11 (Openings (and sometimes closings))] shall be exposed for a period of time which shall not exceed 1.5 seconds. Once an exposed order has received a response, a matching period begins which shall last for a period of time designated by the Exchange that shall not exceed 1 second." Accordingly, in context, the Exchange interprets the term "expose" to mean a designated period of time in which an interest will be represented to the trading crowd in an effort to solicit order responses or contra interests to trade against (i.e. an auction).

¹³ When C2 launched, C2RG10-005 announced that "upon opening, remaining marketable orders will be 'linked,' with no exposure period, to away exchanges disseminating better prices." This "linkage" was originally achieved on C2 by activating the Hybrid Agency Liaison (HAL) Opening Procedure (HAL-O) functionality (which incorporates the NBBO calculation and linkage processing into the opening rotation), but setting the HAL-O timer to zero and also restricting Trading Permit Holders (TPHs) from subscribing to auctions. In July 2011, the Exchange introduced Complex Order Auctions (COA) on C2. At that time, the ability for a TPH to subscribe to auctions was made available. This caused a HAL-O auction message to be sent to C2 auction subscribers whenever an order linked away. Additionally, it is noted that periodically, when systems experience heavy processing volumes, latency may cause the auction process to last longer than its prescribed timer setting of zero. On December 5, 2014, the following notification was posted to the Exchange's System Status webpage, "During periods of heavy systems processing at the open, remaining orders marketable against the NBBO may be exposed for short periods, generally not to exceed 110 MS. Until further notice, TPHs should subscribe to the exposure process to ensure response capabilities during these times." This filing proposes to remedy this issue by simply exposing orders at the opening to an HAL-O auction process not to exceed 1.5 seconds.

determine to expose orders at the opening via auction including under any of the scenarios described in paragraphs (f)(1)-(4) above and that in such cases, the exposure process would be conducted via HAL pursuant to Rule 6.18.¹⁴ The Exchange notes that proposed Interpretation and Policy .04 to Rule 6.11, including this provision, is substantially similar in all material respects to Interpretation and Policy .03 to CBOE Rule 6.2B, setting forth CBOE's HAL Opening Procedures.

In addition, the proposed rule would operate in a manner similar to the HAL Opening Procedures on CBOE with respect to the handling of remaining balances not executed via HAL exposure and provide that any remaining balance of orders not executed via HAL on the opening would be booked except that any remaining balance of orders not executed via HAL on the opening will be booked at their limit price to the extent consistent with Rule 6.10 except that any remaining balance of orders not executed via HAL on the opening that are priced, or would be executed at a price, that is not within an acceptable tick distance from the initial HAL price will be cancelled. The "acceptable tick distance" would be determined by the Exchange on a series-by-series and premium basis in increments not less than two minimum increment ticks. If the HAL Opening Auction Exposure procedure were activated, the acceptable tick distance would be the same as the acceptable tick distance established under Rule 6.17. This final provision of the Interpretation and Policy is consistent with the Exchange's Price Check Parameters rules in Interpretation and Policy .04 to Rule 6.13 and Rule 6.17 and would simply codify the extension of the Exchange's Market-Width and Drill-Through Parameters to Rule 6.11. These proposed provisions are substantially similar to the HAL Opening Procedures set forth in Interpretation

¹⁴ See note 3 supra.

and Policy .03 to CBOE Rule 6.2B in all material respects other than they do not provide for manual handling of orders and in open outcry.

As proposed, the Exchange is seeking merely to extend the opening order exposure procedures already in place on CBOE.¹⁵ The Exchange believes that extending the HAL Opening Procedures to C2 is will provide clarity to the Exchange's rules as well as harmonize the procedures of the two exchanges, ultimately to the benefit of all market participants. The Exchange believes the proposed rule change would serve to further enhance the efficiency of opening rotations with procedures to accommodate a process for addressing opening quotes, acceptable opening ranges, and market order imbalance conditions that may occur on the openings, as well as address NBBO condition scenarios where the Exchange's opening trade might occur at an improved price rather than routing to an away market. Moreover, the Exchange believes that exposing orders on the open helps facilitate transactions in securities and is consistent with the goals of a free and open market and national market system.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.¹⁶ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁷ 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 persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to

¹⁵ See CBOE Rule 6.2B Interpretation and Policy .03.

¹⁶ 15 U.S.C. 78f(b).

¹⁷ 15 U.S.C. 78f(b)(5).

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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁸ requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the proposed rule change is designed to align the Exchange's rules with those of CBOE by extending the procedures of CBOE's HAL on the open to C2. The Exchange believes that extending the HAL Opening Procedures to C2 is will provide clarity to the Exchange's rules as well as harmonize the procedures of the two exchanges, ultimately to the benefit of all market participants. The Exchange believes the proposed rule change would serve to further enhance the efficiency of opening rotations with procedures to accommodate a process for addressing opening quotes, acceptable opening ranges, and market order imbalance conditions that may occur on the openings, as well as address NBBO condition scenarios where the Exchange's opening trade might occur at an improved price rather than routing to an away market. The proposed rule change will increase competition on C2 by providing an opportunity for market participants to benefit from additional exposure of orders and participation in auctions at the open. Furthermore, the Exchange believes that exposing orders on the open helps facilitate transactions in securities and is consistent with the goals of a free and open market and national market system.

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

¹⁸

Id.

Exchange does not believe that the proposed rule change will impose any burden on intramarket competition that is not necessary or appropriate in furtherance of the purposes of the Act because the proposed change will be equally applied and will equally affect all market participants' orders that qualify for the HAL function. Moreover, the Exchange believes that the proposed rule change will increase competition amongst exchanges and market participants. The proposed will expose allow orders to be exposed to meaningful price improvement mechanisms at the opening of trading. The HAL on the opening procedure will allow C2 TPHs to compete with quotes on other exchanges and step up to the best national prices offered before orders are linked away. This price improvement process will not only ensure that orders on C2 are afforded the best prices available, but also afford additional opportunities to C2 TPH to compete with quotes on away exchanges at the opening of trading. The Exchange believes that price improvement mechanisms increase competition in the marketplace and increase opportunities for orders to receive best execution at the Exchange.

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

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

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, if consistent with the protection of investors and the public

interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁹ and Rule 19b-4(f)(6)(iii) thereunder.²⁰

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 will institute proceedings to determine whether the proposed rule change 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. Please include File Number SR-C2-2015-006 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.

¹⁹ 15 U.S.C. 78s(b)(3)(A).

²⁰ 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.

All submissions should refer to File Number SR-C2-2015-006. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you

wish to make available publicly. All submissions should refer to File Number SR-C2-2015-006 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.²¹

Brent J. Fields
Secretary

²¹ 17 CFR 200.30-3(a)(12).