

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-75143; File No. SR-C2-2015-013)

June 10, 2015

Self-Regulatory Organizations; C2 Options Exchange, Incorporated; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Automated Improvement Mechanism Order Allocations

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 3, 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 6.51 relating to the functionality of its Automated Improvement Mechanism (“AIM”). The text of the proposed rule change is 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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

The Exchange proposes to amend its AIM auction Rule 6.51 to provide that in instances where an Initiating Participant electronically submits an order that it represents as agent (“Agency Order”) into an AIM Auction (“Auction”), which the Initiating Participant is willing to automatically match (“auto-match”) as principal the price and size of all Auction responses up to an optional designated limit price and there is only one competing Participant at the final Auction price level, the Initiating Participant may be allocated up to fifty percent (50%) of the size of the order. The Exchange also proposes to add language in Rule 6.51 to more fully describe the manner in which any remaining contracts will be allocated at the conclusion of an Auction and make other non-substantive changes to Rule 6.51 to update terminology in the Rule. This is a competitive filing that is substantially and materially based on the price improvement auction rules of BOX Options Exchange, LLC (“BOX”),³ Nasdaq PHLX MKT (“PHLX”),⁴ and NYSE MKT LLC (“NYSE MKT”).⁵ Also, the filing is, in all material respects, substantially similar to Chicago Board Options Exchange, Incorporated (“CBOE”) filing, SR-CBOE-2015-043, which was recently filed with the Securities and Exchange Commission (the “Commission”).⁶

³ See BOX Rule 7150(h).

⁴ See PHLX Rule 1080(n).

⁵ See NYSE MKT Rule 9.71.1NY(c).

⁶ See Securities and Exchange Act Release No. 74864 (May 4, 2015), 80 F.R. 26601 (May 8, 2015) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Automated Improvement Mechanism Order Allocation) (SR-CBOE-2015-043); see also CBOE Rule 6.74A.

Pursuant to Rule 6.51(b)(3), upon conclusion of an Auction, an Initiating Participant will retain certain priority and trade allocation privileges for both Agency Orders that the Initiating Participant seeks to cross at a single price (“single-price submissions”) and Agency Orders that the Initiating Participant⁷ is willing to automatically match, as principal, the price and size of all Auction responses (“auto-match submissions”). Under current Rule 6.51(b)(3)(F), if the best competing Auction response price equals the Initiating Participant's single-price submission, the Initiating Participant's single-price submission shall be allocated the greater of one contract or a certain percentage of the order, which percentage will be determined by the Exchange and may not be larger than 40%. However, if only one competing Participant matches the Initiating Participant's single price submission then the Initiating Participant may be allocated up to 50% of the order.

Similarly, current Rule 6.51(b)(3)(G) provides that if the Initiating Participant selects the auto-match option for the Auction, the Initiating Participant shall be allocated its full size at each price point until a price point is reached where the balance of the order can be fully executed. At such price point, the Initiating Participant shall be allocated the greater of one contract or a certain percentage of the remainder of the order, which percentage will be determined by the Exchange and may not be larger than 40%. Notably, unlike the single-price submission rules in Rule 6.51(b)(3)(F), current Rule 6.51(b)(3)(G) provides that an Initiating Participant would only receive an allocation of up to 40% for orders that are matched at the final price level by only one competing Participant when the auto-match option is selected for the Agency Order. The Exchange believes this result to be inconsistent within the Rules and that Initiating Participants that price orders more

⁷ Rule 6.51(b)(3)(F) currently contains a typographical error in that it provides that if only one Market-Maker matches the Initiating Participant's single price submission then the Initiating Participant may be allocated up to 50% of the order. Under Rule 6.51(b)(1)(D), however, responses to RFRs may be submitted by all Participant that have subscribed to receive auction messages, not only Market-Makers. As described below, this typographical error would be changed upon the operability of the instant filing.

aggressively using the auto-match option should receive allocations at least equal to Participants that select the single-price submission option for an Auction.

Accordingly, the Exchange proposes to amend Rule 6.51(b)(3)(G) to provide that if only one competing Participant is present at the final Auction price, then the Initiating Participant may be allocated up to 50% of the remainder of the Agency Order at the final Auction price level. As discussed above, current Rule 6.51(b)(3)(G) provides that an Initiating Participant will receive an allocation of up to 40% for orders that are matched at the final price level by only one competing Participant when the auto-match option is selected by the Initiating Participant for the Auction. The Exchange believes this result to be inconsistent within the Rules and believes that Initiating Participants that price orders more aggressively using the auto-match option should receive allocations at least equal to those that select the single-price submission option. The Exchange also believes proposed rule change will more closely align the language in Rule 6.51(b)(3)(G) with the language in Rule 6.51(b)(3)(F) and will thus, provide additional internal consistency within the Rules by harmonizing order allocations of single-price submissions and auto-match Auction orders in instances where there is only one competing order at the final Auction price level. Furthermore, the proposed rule change will bring the Exchange's AIM rules in line with the Rules of other competitor exchanges with which the Exchange competes for order flow.

The Exchange notes that the proposed rule change would not affect the priority of public customer orders under Rule 6.51(b)(3)(B). Public customer orders in the book would continue to have priority even in cases in which a public customer order is resting in the book at the final Auction price. For example, suppose that the national best bid ("NBB") for a particular option is \$1.00 and the national best offer ("NBO") for the option is \$1.20 and that the NBB is an order to buy 10 contracts resting in the book on C2. The minimum increment in the option series is \$0.01.

An Initiating Participant at C2 submits an auto-match Agency Order to sell 100 options contracts in the series. The Auction begins and, during the auction, one competing Participant submits an Auction response to buy 50 contracts at \$1.00. The Auction then concludes. In this case, the public customer order resting in the book would have priority and be allocated 10 contracts with the remaining 90 contracts being allocated 50/50 to the responding Participant and the Initiating Participant, 45 contracts each.

Similarly, a public customer order resting in the book at a final Auction price level worse than the best Auction response will also retain priority in the book. Accordingly, assume again that the national best bid (“NBB”) for a particular option is \$1.00 and the national best offer (“NBO”) for the option is \$1.20 and that the NBB is an order to buy 10 contracts resting in the book on C2. The minimum increment in the option series is \$0.01. An Initiating Participant at C2 submits an auto-match Agency Order to sell 100 options contracts in the series. The Auction begins and during the Auction, one competing Participant (“P1”) submits an Auction response to buy 20 contracts at \$1.02, a second Participant (“P2”) submits an Action response to buy 20 contracts at \$1.01, and a third Participant (“P3”) submits an Auction response to buy 20 contracts at \$1.00. The Auction then concludes. In this case, P1 and the Initiating Participant would each be allocated 20 contracts at \$1.02 and P2 and the Initiating Participant would each be allocated 20 contracts at \$1.01 since the Initiating Participant is willing to match the price and size at each improved price level. The remaining 20 contracts would be allocated 10 to the public customer order resting in the book at

\$1.00 because the public customer would retain priority at that price level with the remaining 10 contracts being allocated 50/50 to P3 and the Initiating Participant, 5 contracts each.⁸

The Exchange believes that increasing the Initiating Participant's allocation priority for auto-match submissions that only have one competing order at the final price level fairly distributes the order when there are only two counterparties to the Agency Order involved in the Auction at the final Auction price, and that doing so is reasonable because of the value that Initiating Participants provide to the market. Initiating Participants selecting the auto-match option for Agency Orders guarantee an execution at the NBBO or at a better price, and are subject to a greater market risk than single-price submissions while the order is exposed to other AIM participants. As such, the Exchange believes that the value added from Initiating Participants, guaranteeing execution of Agency Orders at a price equal to or better than the NBBO in combination with the additional market risk of initiating auto-match submissions warrants an allocation priority of at least the same percentage as Initiating Participants that submit single-price orders into AIM. The Exchange also believes that the proposed rule change, like other price improvement allocation programs currently offered by competitor exchanges, will benefit investors by attracting more order flow as well as increasing the frequency that Participants initiate Auctions, which may result in greater

⁸ The Exchange notes that an unrelated public customer market or marketable limit order on the opposite side of the market from the Agency Order that is received during an Auction will end the Auction and trade against the Agency Order at the midpoint of the best RFR response and the NBBO on the other side of the market from the RFR responses. See Rule 6.51(b)(3)(D). For example, assume that the NBBO is \$1.00 - \$1.20. An Initiating Participant submits a matched Agency Order to sell 100 options contracts at in the series at \$1.10. The Auction begins and during the Auction, one competing Participant submits an Auction response to buy 100 contracts at \$1.15. Assume that after the first response is received, an unrelated public customer order to buy 100 contracts at \$1.20 is received. This would conclude the auction early after which the public customer order would trade 100 contracts with the Agency Order at \$1.17 (i.e. the midpoint between the best RFR response (\$1.15) and the NBBO on the other side of the market from the RFR responses (\$1.20)).

opportunities for customer order price improvement. Moreover, as discussed above, the proposed rule change is consistent with the rules of other exchanges, including CBOE.⁹

The Exchange also proposes to add text to Rules 6.51(b)(3)(F) and (G) to describe the manner in which remaining contracts would be allocated at the conclusion of an Auction under the scenarios therein. Specifically, the Exchange proposes to amend paragraphs (F) and (G) to provide that (subject to public customer priority), after the Initiating Participant has received an allocation of up to 40% of the Agency Order (or 50% of the Agency Order if there is only one other RFR response), contracts shall be allocated among remaining quotes, orders, and auction responses (i.e. interests other than the Initiating Participant) at the final auction price in accordance with the matching algorithm in effect for the subject class. If all RFR Responses are filled (i.e. no other interests remain), any remaining contracts will be allocated to the Initiating Participant at the single-price submission price for single-price submissions or, for auto-match submissions, to the Initiating Participant at the auction start price as specified under Rule 6.51(b)(1)(A). The Exchange believes that this additional language would add clarity in the Rules with respect to how remaining odd-lots will be allocated at the conclusion of an Auction.¹⁰

For example, suppose that the NBBO for a particular option is \$1.00 - \$1.20. The minimum increment for the series is \$0.01 and the matching algorithm in effect for the option class is pro rata.

⁹ See, e.g., BOX Rule 7150(h); NYSE MKT Rule 9.71.1NY(c)(5)(B). See also Securities and Exchange Act Release No. 74864 (May 4, 2015), 80 F.R. 26601 (May 8, 2015) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Automated Improvement Mechanism Order Allocation) (SR-CBOE-2015-043); CBOE Rule 6.74A.

¹⁰ The Exchange notes that such remaining contracts are currently allocated to the Initiating Participant in excess of the up to 40% (50% if there is only one other Market-Maker or Participant representing an Agency Order) of the order that the Initiating Participant may receive under the Exchange's existing Rules pursuant to the provision that the Initiating Participant will be allocated the greater of one contract or up to 40% (50% if there is only one other Market-Maker or Participant representing an Agency Order) at the final Auction price.

An Initiating Participant submits a matched Agency Order to sell 5 contracts at \$1.10. The Auction begins and, during the auction, one competing Participant (“P1”) submits an Auction response to buy 5 contracts at \$1.10, followed by another Participant (“P2”) submitting an Auction response to buy 5 contracts at \$1.10. The Auction concludes. In this case, under proposed Rule 6.51(b)(3)(F), the Initiating Participant would receive an allocation up to 40%, or, in this case, 2 contracts at \$1.10. P1 and P2 would then receive 1 contract each at \$1.10 according to the pro rata allocation algorithm in place for the class with P1, as the first responder, receiving the final 1 contract at the final auction price of \$1.10.¹¹

Similarly, suppose that the NBBO for a particular option is \$1.00 - \$1.20. The minimum increment for the series is \$0.01 and the matching algorithm in effect for the option class is pro rata. An Initiating Participant submits a matched Agency Order to sell 5 contracts at \$1.10. The Auction begins and, during the auction, one competing Participant (“P1”) submits an Auction response to buy 1 contract at \$1.10, followed by another Participant (“P2”) submitting an Auction response to buy 1 contract at \$1.10. The Auction concludes. In this case, under proposed Rule 6.51(b)(3)(F), the Initiating Participant would receive an allocation up to 40%, or, in this case, 2 contracts at \$1.10. P1 and P2 would then receive 1 contract each at \$1.10 according to the pro rata allocation algorithm in place for the class. With no other RFR responder interest for the Auction, however, proposed Rule 6.51(b)(3)(F) will simply make clear that if all RFR Responses are filled (i.e. no other interests remain), any remaining contracts will be allocated to the Initiating Participant at the single-price submission price. In this case, the final 1 contract would be allocated to the Initiating Participant at \$1.10.

¹¹ See Rules 6.12(a).

Remaining odd-lots for auto-match submissions would be similarly allocated under proposed Rule 6.51(b)(3)(G), except that if all RFR Responses are filled (i.e. no other interests remain), any remaining contracts will be allocated to the Initiating Participant at the auction start price as specified under Rule 6.51(b)(1)(A). Accordingly, suppose that the NBBO for a particular option is \$1.00 - \$1.20. The minimum increment for the series is \$0.01 and the matching algorithm in effect for the option class is pro rata. An Initiating Participant submits an auto-matched Agency Order to sell 5 contracts. In this case, because no Auction stop price is specified, the Auction would begin at the NBBO, or \$1.20.¹² Assume that the Auction begins and, during the auction, one competing Participant (“P1”) submits an Auction response to buy 1 contracts at \$1.18, followed by another Participant (“P2”) submitting an Auction response to buy 1 contract at \$1.17. The Auction concludes. In this case, P2 and the Initiating Participant would each receive 1 contract at \$1.17 and P1 and the Initiating Participant would each receive 1 contract at \$1.18. Because all RFR Responses would then be filled (i.e. no other interests remain), any remaining contracts will be allocated to the Initiating Participant at the Auction start price or, in this case, 1 contract at \$1.20.

The Exchange notes that the proposed amendments are based on, and consistent with, the rules of other competitor exchanges as well as a recent filing of CBOE.¹³ The Exchange believes that the value added from Initiating Participants guaranteeing execution of Agency Orders at a price equal to or better than the NBBO warrants (to the extent that the Initiating Participants is on the final Auction price), an Auction allocation priority of at least the same percentage of the order as any competing Auction responses. The Exchange also believes that the proposed rule change, like

¹² See Rule 6.51(b)(1)(A).

¹³ See, e.g., NYSE MKT Rule 9.71.1NY(c)(5); PHLX Rule 1080(n)(ii)(E). See also Securities and Exchange Act Release No. 74864 (May 4, 2015), 80 F.R. 26601 (May 8, 2015) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Automated Improvement Mechanism Order Allocation) (SR-CBOE-2015-043); CBOE Rule 6.74A.

other price improvement allocation programs currently offered by competitor exchanges, will benefit investors by attracting more order flow as well as increasing the frequency that Participants initiate Auctions, which may result in greater opportunities for customer order price improvement.

Additionally, the Exchange is proposing to add additional clarifying language to Rule 6.51. Specifically, the Exchange proposes correct a typographical error in the second sentence of Rule 6.51(b)(3)(F), deleting the term “Market-Maker” and replacing it with the term “competing Participant” to make clear that all Participants that subscribe to receive auction messages on the Exchange may respond to Auctions and thus, may be present at the final Auction price. The Exchange notes that the proposed language is consistent with the current Rule and would also be consistent with the rule text of Rule 6.51(b)(1)(D), which provides that “[r]esponses to RFRs may be submitted by Participants.” The Exchange also proposes to add a comma after the word submission in the second sentence of Rule 6.51(b)(3)(F) for grammatical purposes. The Exchange strives for transparency in its Rules and believes these non-substantive changes will provide greater clarity for market participants. The Exchange believes that these changes are non-controversial as they simply clarify the Exchange’s already existing AIM rules.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Securities Exchange Act of 1934 (the “Act”) and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.¹⁴ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁵ 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

¹⁴ 15 U.S.C. 78f(b).

¹⁵ 15 U.S.C. 78f(b)(5).

coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁶ requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes the proposed rule changes protect investors by fairly distributing the allocation of the AIM order between the Initiating Participant and Participants that respond to price improvement auctions, and clarifying the Rules with respect to the distribution of AIM orders when only there are only two counterparties to an Auction and/or the number of contracts remaining at the final Auction price cannot be evenly distributed at the end of an Auction. The Exchange believes that the proposed rule changes, like other price improvement programs currently offered by competing exchanges, will benefit investors by attracting more order flow as well as increasing the frequency that Participants submit orders to Auction, which may result in greater opportunity for price improvement for customers. Moreover, the proposed rule change is consistent with the Rules of other exchanges. With respect to the proposed clarifying additions to Rule 6.51, the Exchange believes that the proposed changes will benefit market participants by adding additional transparency and clarity to the Rules.

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

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Id.

proposed changes are meant to more fairly distribute the order allocation when there are only two counterparties to an Auction auto-match order. The Exchange does not believe that this change will discourage any market participants from entering into the AIM, as the auto-match option of the AIM is more aggressive in terms of risk and therefore, increasing the allocation to up to 50% of the remainder for the Initiating Participant when there is only one competing order at the final price level is a more fair and reasonable allocation mechanism and would likely only increase the number of Participants that select the auto-match option to initiate Auctions.

Furthermore, the Exchange notes that the proposed rule change is a competitive response to similar provisions in the price improvement auction rules of BOX, PHLX, and NYSE MKT.¹⁷ The Exchange believes this proposed rule change is necessary to permit fair competition among the options exchanges and to establish more uniform price improvement auction rules on the various exchanges. The Exchange is also seeking the proposed rule change to align the allocation priorities for AIM single-price and auto-match submissions for Initiating Participants when there is only one competing order at the final price level within its rules. As mentioned earlier, auto-match submissions carry more risk than single-price submissions and as a result, should be given at least the same allocation priority as single-price submissions. The Exchange believes this proposed rule change is necessary to permit fair competition among the options exchanges and to establish more uniform price improvement auction rules on the various exchanges.

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.

¹⁷ See BOX Rule 7150; NYSE MKT Rule 971.1NY, PHLX Rule 1080.

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

Because the foregoing proposed rule change does not:

- (i) significantly affect the protection of investors or the public interest;
- (ii) impose any significant burden on competition; and
- (iii) become operative for 30 days from the date on which it was filed, or such shorter

time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁸ and Rule 19b-4(f)(6)¹⁹ thereunder.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

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-C2-2015-013 on the subject line.

¹⁸ 15 U.S.C. 78s(b)(3)(A).

¹⁹ 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 short time as designated by the Commission. The Exchange has satisfied this requirement.

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-C2-2015-013. 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, D.C. 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-C2-2015-013 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.²⁰

Robert W. Errett
Deputy Secretary

²⁰ 17 CFR 200.30-3(a)(12).