

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-81010; File No. SR-CBOE-2017-049)

June 23, 2017

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Related to Rule 6.56 (Compression Forums)

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 16, 2017, Chicago Board Options Exchange, Incorporated (the “Exchange” or “CBOE”) 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 Exchange filed the proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act³ and Rule 19b-4(f)(6) thereunder.⁴ 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 6.56. The text of the proposed rule change is provided below.

(additions are underlined; deletions are [bracketed])

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Chicago Board Options Exchange, Incorporated
Rules

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¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(iii).

⁴ 17 CFR 240.19b-4(f)(6).

Rule 6.56. Compression Forums

(a) No change.

(b) Trades executed through compression forums are subject to trading rules applicable to trading in SPX during Regular Trading Hours (including without limitation manner of bids and offers, allocation and priority, and solicited transaction rules), except:

(1) opening transactions in SPX options may not execute against opening transactions through a compression forum; however, closing transactions in SPX options (including compression-list positions) that are represented in the compression forum may execute against closing or opening transactions; [only closing transactions in SPX options (including compression-list positions) may be executed through a compression forum;] and

(2) only closing transactions may be executed in \$0.01 increments, including simple and complex orders. Bids and offers for opening transactions made in response to the representation of a closing transaction must be priced in the standard increment for simple and complex orders set forth in Rule 6.42. [the minimum increment for bids and offers will be \$0.01, including for both simple and complex orders.]

(c) No change.

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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 proposes to amend Rule 6.56 (Compression Forums) in order to fine-tune the compression forum process. Specifically, the Exchange seeks to allow closing transactions that are represented in the compression forum to be executed against opening transactions. Allowing closing transactions that are represented in the compression forum to be executed against opening transactions increases the likelihood that existing positions creating high bank regulatory capital requirements will be closed – thus lowering a TPH’s bank capital footprint.

Background

SEC Rule 15c3-1 (Net Capital Requirements for Brokers or Dealers) (“Net Capital Rules”) requires registered broker-dealers, unless otherwise excepted, to maintain certain specified minimum levels of capital.⁵ The Net Capital Rules are designed to protect securities customers, counterparties, and creditors by requiring that broker-dealers have sufficient liquid resources on hand, at all times, to meet their financial obligations. Notably, hedged positions, including offsetting futures and options contract positions, result in certain net capital requirement reductions under the Net Capital Rules.⁶

Subject to certain exceptions, CBOE Clearing Trading Permit Holders (“CTPHs”)⁷ are subject to the Net Capital Rules. However, a subset of CTPHs are subsidiaries of U.S. bank holding companies, which, due to their affiliations with their parent U.S. bank holding

⁵ 17 CFR § 240.15c3-1.

⁶ In addition, the Net Capital Rules permit various offsets under which a percentage of an option position’s gain at any one valuation point is allowed to offset another position’s loss at the same valuation point (e.g., vertical spreads).

⁷ All CBOE CTPHs must also be clearing members of The Options Clearing Corporation (“OCC”).

companies, must comply with additional bank regulatory capital requirements pursuant to rulemaking required under the Dodd–Frank Wall Street Reform and Consumer Protection Act.⁸ Pursuant to this mandate, the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation have approved a regulatory capital framework for subsidiaries of U.S. bank holding company clearing firms.⁹ Generally, these rules impose higher minimum capital requirements, more restrictive capital eligibility standards, and higher asset risk weights than were previously mandated for CTPHs that are subsidiaries of U.S. bank holding companies under the Net Capital Rules. Furthermore, the new rules do not permit deductions for hedged securities or offsetting options positions.¹⁰ Rather, capital charges under these standards are, in large part, based on the aggregate notional value of short positions regardless of offsets. As a result, in general, CTPHs must hold substantially more bank regulatory capital than would otherwise be required under the Net Capital Rules. The impact of these regulatory capital rules are compounded in the SPX options market due to the large notional value of SPX contracts.

⁸ H.R. 4173 (amending section 3(a) of the Securities Exchange Act of 1934 (the “Act”) (15 U.S.C. § 78c(a))).

⁹ 12 CFR §50; 79 FR 61440 (Liquidity Coverage Ratio: Liquidity Risk Measurement Standards).

¹⁰ Many options strategies, including relatively simple strategies often used by retail customers and more sophisticated strategies used by market-makers and institutions, are risk-limited strategies or options spread strategies that employ offsets or hedges to achieve certain investment outcomes. Such strategies typically involve the purchase and sale of multiple options (and may be coupled with purchases or sales of the underlying securities), executed simultaneously as part of the same strategy. In many cases, the potential market exposure of these strategies is limited and defined. Whereas regulatory capital requirements have historically reflected the risk-limited nature of carrying offsetting positions, these positions may now be subject to higher regulatory capital requirements. Various factors, including administration costs; transaction fees; and limited market demand or counterparty interest, however, may discourage market participants from closing these positions even though many market participants likely would prefer to close the positions rather than carry them to expiration.

The Exchange believes that these higher regulatory capital requirements have the potential to impact liquidity in the SPX options market by limiting the amount of capital CTPHs can allocate to their clients' transactions. Specifically, the rules may cause CTPHs to impose stricter position limits on their client clearing members, which include CBOE Market-Makers. Such position limits may impact the liquidity Market-Makers might supply in the SPX market, and this impact may be compounded when a CTPH has multiple Market-Maker client accounts, each having largely risk-neutral portfolio holdings.¹¹ The Exchange believes that permitting Market-Makers and Floor Brokers (for their own proprietary accounts or for the account of another on an agency basis) to efficiently close existing SPX options positions through modified open outcry trading procedures on the Exchange floor may assist CTPHs and TPHs to address bank regulatory capital requirements and would likely have a beneficial effect on continued liquidity in the SPX options market without adversely affecting market quality.

In order to mitigate the potential negative effects of these additional bank regulatory capital requirements and foster continued liquidity in the SPX options market in a manner consistent with the requirements, the Exchange adopted Rule 6.56 pursuant to which TPHs can reduce (or "compress") existing positions in SPX at the end of each calendar month more efficiently through trading in an open outcry compression forum.¹² The Exchange believes that making available these periodic trading forums, which allow for closing transactions in SPX options series to occur at reduced transaction fees likely contributes to additional liquidity and

¹¹ Several TPHs have indicated to the Exchange that the heightened bank regulatory requirements could impact their ability to provide consistent liquidity in the SPX options market unless they are able to efficiently close their positions in SPX.

¹² See Securities Exchange Act Release No. 79610 (December 20, 2016), 81 FR 95219 (December 27, 2016) (Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to Compression of S&P 500(R) Index Options Positions) (SR-CBOE-2016-090).

continued competitiveness in the SPX market and promotes more efficient capital deployment in light of bank regulatory capital requirements.

Under current Rule 6.56, on the final three business days of each calendar month, the Exchange holds compression forums in the SPX trading crowd. Beforehand, in order to facilitate TPHs finding counterparty offsets against which they can trade closing positions, currently, TPHs may submit lists of existing SPX positions to the Exchange that they wish to close during a compression forum. Prior to the open of trading on the third-to-last business day of each calendar month (i.e., the first day of the month on which a compression forum is held), the Exchange makes available to all TPHs on its website a list including each series for which both long and short compression-list positions have been submitted to the Exchange (“compression-list positions file”). In addition, TPHs that submit compression positions list to the Exchange receive a compression-list positions file containing the names of the TPHs that contributed to the file, including contact information for each TPH’s designated point of contact. This list does not identify the specific positions that any TPH has submitted to the Exchange.

The Exchange then holds open outcry "compression forums" in which all TPHs may participate whether or not they submitted positions for inclusion in the compression-list position file. Currently, trades executed during compression forums are subject to trading rules applicable to trading in SPX during Regular Trading Hours, including manner of bids and offers and allocation and priority rules, except: (1) only closing transactions in SPX options (including compression-list positions) may be executed through a compression forum; and (2) the minimum increment for all series is \$0.01 during a compression forum. TPHs that trade positions previously submitted to the Exchange on a compression list may then take advantage of the

compression-list position fee rebate on portions of a transaction that involve their compression-list positions, which are executed through a compression forum.

The Exchange proposes to amend Rule 6.56 to enhance the effectiveness and utility of its compression forums process for market participants. Specifically, the Exchange seeks to allow closing transactions that are represented in the compression forum to be executed against opening transactions. Allowing closing transactions that are represented in the compression forum to be executed against opening transactions increases the likelihood that existing positions creating high bank regulatory capital requirements will be closed – thus lowering a TPH’s (or clearing firm’s) bank capital footprint.

Proposal

The purpose of Rule 6.56 is to encourage the closing of positions that are creating high bank regulatory capital requirements. When Rule 6.56 was originally implemented, the Exchange was concerned that allowing opening transactions in the compression forum “would defeat the purpose of the proposed rule[.]”¹³ However, after observing the compression process for the past several months, the Exchange believes allowing closing transactions that are represented in the compression forum to execute against opening transactions will not discourage the closing of positions that are creating a high bank regulatory capital footprint nor will it adversely affect the compression forums. Allowing opening transactions will expand the liquidity available to close positions represented in a compression forum, thus, increasing the opportunity for TPHs to close positions that cause them to have high bank regulatory capital footprints. Ultimately the Exchange believes the increased opportunity for positions to be closed will in fact further encourage TPHs to close positions that

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Id.

cause them to have high bank regulatory capital footprints without adversely affecting the compression forums.

Thus, the Exchange proposes to amend Rule 6.56(b)(1) to remove the closing only restricting for compression forum executions. Specifically, the Exchange proposes to amend Rule 6.56(b)(1) to provide that transactions in SPX options (including compression-list positions) that are represented in the compression forum may execute against closing or opening transactions. To provide further clarity as to the limited application of this change, the Exchange proposes to amend Rule 6.56(b)(1) to provide that opening transactions in SPX options may not execute against opening transactions through a compression forum. The Exchange notes that Rule 6.56(b)(1) already effectively prohibits opening transactions from executing against opening transactions in a compression forum because Rule 6.56(b)(1) currently provides that only closing transactions are to be executed via a compression forum.

Currently, transactions executed via a compression forum may be executed in \$0.01 increments for both simple and complex orders, but as previously noted, compression forums are currently restricted to closing transactions. Thus, with the expansion of compression forums to opening transactions (provided they execute against closing transactions), the Exchange proposes to amend Rule 6.56(b)(2) to provide that only closing transactions may be executed in \$0.01 increments, including simple and complex orders whereas bids and offers for opening transactions made in response to the representation of a closing transaction must be priced in the standard increment for simple and complex orders set forth in Rule 6.42 (e.g., \$0.05 for option series below \$3, \$0.10 for option series at or above \$3, and \$0.05 increments for complex orders).¹⁴ The Exchange notes that the proposed minimum increment for opening transactions executed against

¹⁴ See Rule 6.42(1)-(4).

closing transactions in a compression forum is consistent with the minimum increment applicable to SPX transactions (opening or closing) executed outside a compression forum.

Currently, only a fraction of the offsetting interest provided in the compression-list positions have ultimately been closed out during previous compression forums.¹⁵ This proposal will allow a TPH that is representing closing transactions in a compression forum – but is unable to close the position against another party’s closing transaction – to solicit TPHs or non-TPH customers or broker-dealers to participate in the compression forum whether the TPH or non-TPH is opening or closing a position. Although the most impactful bank capital relief (in the context of listed options) occurs when two parties can each close offsetting open position, whenever a TPH is able to close a position – whether the TPH is transacting with a party that is opening or closing a position – the TPH will lower its bank capital footprint. Thus, the Exchange simply seeks to increase the opportunity for TPHs to lower their bank capital footprint.

A party’s bank capital footprint is largely a function of its investor profile and clearing firm. TPHs are sophisticated parties capable of assessing a transaction’s impact on their bank capital footprint and determining whether to close positions to reduce their bank capital footprint. For those TPHs concerned with their bank capital footprint, Rule 6.56 provides an opportunity for them to submit compression-list positions and participate in the compression process. The Exchange believes this proposal further encourages TPHs to close positions via the compression process by increasing the likelihood that there will be liquidity against which a closing position may execute.

¹⁵ In the months since the adoption of Rule 6.56, of the compression-list positions submitted to the Exchange, less than 10% of the offsetting interest were actually closed in transactions through a compression forum.

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.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 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 Exchange believes that its proposal is consistent with the Act in that it seeks to foster liquidity in the SPX options market in light of the bank regulatory capital requirements. As described above, the Exchange believes that the new bank regulatory capital requirements could potentially limit the amount of capital CTPHs can allocate to their clients’ transactions, which in turn, may impact liquidity, particularly in the SPX market. The Exchange believes the proposal encourages TPHs to close positions via the compression process by increasing the likelihood that there will be liquidity with which to execute a closing position,

¹⁶ 15 U.S.C. 78f(b).

¹⁷ 15 U.S.C. 78f(b)(5).

¹⁸ Id.

which, in general, helps to protect investors and the public interest because closing positions via the compression process serves to alleviate the adverse impact of bank capital requirements.

The Exchange also believes the proposed rule change is consistent with the Act, because the proposed procedure is consistent with its current rules. The proposed rule would direct that all trading through compression forums be conducted in accordance with normal SPX trading rules and thus, in the same manner as transactions during normal SPX trading, except that opening transactions may not execute against opening transactions via a compression forum and that closing transactions executed against closing transactions may be in penny increments. The Exchange notes that Rule 6.56(b)(1) already effectively prohibits opening transactions from executing against opening transactions in a compression forum because Rule 6.56(b)(1) currently provides that only closing transactions are to be executed via a compression forum. The Exchange also notes that the proposed minimum increment for opening transactions executed against closing transactions in a compression forum (i.e., bids and offers for opening transactions made in response to the representation of a closing transaction must be priced in the standard increment for simple and complex orders set forth in Rule 6.42) is consistent with the minimum increment applicable to SPX transactions (opening or closing) executed outside a compression forum.

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

CBOE 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 proposed change would encourage the closing of positions, which, once closed, may serve to alleviate the capital requirement constraints on TPHs and improve overall market liquidity by freeing capital currently tied up in certain SPX positions. The Exchange does not believe that the proposed rule changes will impose any burden on intermarket competition that is not

necessary or appropriate in furtherance of the purposes of the Act because the proposed rule change applies only to the trading of SPX options, which are exclusively-listed on CBOE. To the extent that the proposed changes make the Exchange a more attractive marketplace for market participants at other exchanges, such market participants are eligible to participate through CBOE TPHs. Furthermore, participation in compression forums is completely voluntary and open to all TPHs.

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 comments on the proposed rule change.

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

The Exchange has filed the proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act¹⁹ and Rule 19b-4(f)(6) thereunder.²⁰ 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 public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act²¹ and Rule 19b-4(f)(6) thereunder.²²

¹⁹ 15 U.S.C. 78s(b)(3)(A)(iii).

²⁰ 17 CFR 240.19b-4(f)(6).

²¹ 15 U.S.C. 78s(b)(3)(A).

²² 17 CFR 240.19b-4(f)(6). As required under Rule 19b-4(f)(6)(iii), the Exchange provided the Commission with written notice of its intent to file the proposed rule change, along with a brief description and the text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission.

A proposed rule change filed under Rule 19b-4(f)(6)²³ normally does not become operative prior to 30 days after the date of the filing. However, pursuant to Rule 19b-4(f)(6)(iii),²⁴ the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the proposed rule change may become effective on June 27, 2017, permitting the proposed change to take effect for the compression forum scheduled to take place using the amended procedures prior to the end of the second quarter. In justifying its requested waiver, the Exchange noted that bank-imposed capital limits may impact certain TPHs on at least a quarterly basis, which can effectively limit the amount of liquidity that such TPHs, including some Market-Makers, are willing or able to provide in SPX options. The month of June is the end of a quarter, and the Exchange expressed concern that those bank capital requirements may have adverse consequences on investors if the impacted TPHs are not able to more effectively reduce their open interest in SPX. The Exchange therefore believes that it is in the best interest of investors and the general public to help ensure consistent continued depth of liquidity in the SPX options market by allowing TPHs to utilize the modified compression forum process set forth in this proposal on the final three days of trading of the second quarter.

The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because this waiver will enable the Exchange to hold a compression forum for SPX options under the proposed amended procedures prior to the end of the second quarter, thereby helping to facilitate transactions and remove impediments to quarter-end trading in SPX options. The Commission notes that CBOE's compression forum rule, as proposed to be amended, is limited in its application, involves no material changes to

²³ 17 CFR 240.19b-4(f)(6).

²⁴ 17 CFR 240.19b-4(f)(6)(iii).

how trading is conducted on the Exchange, involves a process in which participation is voluntary and open to all, and is designed as a means to help Market Makers and other market participants, as well as their clearing brokers, to close positions in SPX options that they carry on their books and which may impact their available capital. For this reason, the Commission hereby waives the 30-day operative delay and designates the proposal effective on June 27, 2017.²⁵

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-CBOE-2017-049 on the subject line.

²⁵ For purposes only of waiving the 30-day operative delay, the Commission also has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

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-CBOE-2017-049. 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-CBOE-2017-049 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.²⁶

Eduardo A. Aleman
Assistant Secretary

²⁶ 17 CFR 200.30-3(a)(12).