

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-91637; File No. SR-CBOE-2021-013)

April 22, 2021

Self-Regulatory Organizations; Cboe Exchange, Inc.; Order Approving a Proposed Rule Change to Amend Rule 5.52(d) in Connection with a Market-Maker's Electronic Volume Transacted on the Exchange

I. Introduction

On February 22, 2021, Cboe Exchange, Inc. (the "Exchange") 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 proposed rule change to amend Rule 5.52(d) in connection with a Market-Maker's electronic volume transacted on the Exchange. The proposed rule change was published for comment in the Federal Register on March 12, 2021.<sup>3</sup> The Commission received no comment letters on the proposed rule change. This order approves the proposed rule change.

II. Description of the Proposal

The Exchange proposes to amend Rule 5.52(d) in connection with a Market-Maker's electronic volume transacted on the Exchange. Rule 5.52(d)(1) provides that if a Market-Maker never trades more than 20% of the Market-Maker's contract volume electronically in an appointed class during any calendar quarter ("Electronic Volume Threshold")<sup>4</sup>, a Market-Maker will not be obligated to quote electronically in any designated percentage of series within that

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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. 91275 (March 8, 2021), 86 FR 14166 ("Notice").

<sup>4</sup> The proposed rule change provides additional clarity within Rule 5.52(d)(1) by defining this threshold and adding the defined term throughout Rule 5.52(d)(1).

class pursuant to subparagraph (d)(2) (which governs the continuous electronic quoting requirements for Market-Makers in their appointed classes). That is, once a Market-Maker surpasses the Electronic Volume Threshold in an appointed class, the Market-Maker is required to provide continuous electronic quotes in that appointed classes going forward. Neither Rule 5.52(d)(1) nor (d)(2) permit a Market-Maker to reduce its electronic volume after surpassing the Electronic Volume Threshold in order to reset the electronic volume trigger or otherwise undo the resulting obligation to stream electronic quotes once the Electronic Volume Threshold is triggered in an appointed class.

According to the Exchange, Market-Makers accustomed to executing volume on the trading floor have sophisticated and complicated risk modeling associated with their floor trading activity, including quoting, monitoring, and responding to the trading crowd. However, the Exchange understands that while such Market-Makers do have separate systems or third-party platforms for quoting, monitoring and responding to electronic markets, because these Market-Makers are almost exclusively floor-based, their technology or other platforms enabling them to quote electronically do not achieve the level of sophistication or complexity as the systems used by Market-Makers accustomed to quoting electronically. Indeed, to satisfy the continuous electronic quoting requirements, a Market-Maker must provide continuous bids and offers for 90% of the time the Market-Maker is required to provide electronic quotes in an appointed option class on a given trading day and must provide continuous quotes in 60% of the series of the Market-Maker's appointed classes. The Exchange determines compliance by a Market-Maker with this quoting obligation on a monthly basis. In addition to this, a Market-Maker must, among other things, compete with other Market-Makers in its appointed classes, update quotations in response to changed market conditions in its appointed classes, maintain active

markets in its appointed classes, and, overall, engage in a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market. Market-Makers that are predominantly floor-based generally do not have the technology or electronic trading sophistication to fully satisfy the continuous electronic quoting obligations, as well as other heightened standards required of a Market-Maker in its appointed classes electronically, once the Electronic Volume Threshold is triggered.

The Exchange has observed that, around the end of calendar year 2019, particularly given the significant increase in market volatility and unpredictability of market conditions in the months leading up to and during the COVID-19 pandemic,<sup>5</sup> Market-Makers that almost exclusively executed their volume in open outcry and had not previously triggered an electronic quoting obligation pursuant to Rule 5.52(d)(2), incidentally breached the Electronic Volume Threshold in certain appointed classes and were thereby obliged to provide continuous electronic quotes in those classes going forward. As stated above, once a Market-Maker surpasses the Electronic Volume Threshold in an appointed class, and the electronic quoting obligation is triggered, Rules 5.52(d)(1) and (d)(2) do not permit a Market-Maker to reset the trigger — a Market-Maker is required to stream electronic quotes in that appointed class beginning the next calendar quarter and from there on out. As such, once the Electronic Volume Threshold was

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<sup>5</sup> The Exchange notes that after volatility and unusual market conditions beginning at the end of 2019 and continuously increasing through 2020 as a result of the impact of COVID19 and related factors, some market participants may have experienced significant trading losses, resulting in their limiting their trading behavior and risk exposure. The Exchange understands that firms, not otherwise highly active in the electronic markets, may have executed electronically in order to close positions, reduce exposure, and otherwise mitigate losses and reduce risk in light of market conditions experienced at various points throughout the year. These firms may have also reduced open outcry activity as part of the same risk-reducing strategy, resulting in a coincidental change in the mix of electronic versus open outcry volume for such generally floor-based Market-Makers.

surpassed by Market-Makers accustomed to quoting on the trading floor, these Market-Makers had to be equipped to uphold continuous electronic quoting obligations by just the next calendar quarter, production of which was exacerbated by the volatile and unusual market conditions present in the markets over the past year. As a result, the Exchange has observed that at least one Market-Maker<sup>6</sup> has been unable to successfully fulfill its new continuous electronic quoting obligations in subsequent months. The Exchange understands this is due to the Market-Maker not having the appropriate technology to successfully provide continuous electronic quotes. Therefore, the Exchange proposes to amend Rule 5.52(d)(1) in a manner that provides a potential path of recourse for Market-Makers that incidentally exceed the Electronic Volume Threshold, due, for example, to extraordinary or extreme volatility as experienced in the markets in the last year, but that may not be able to satisfy the continuous electronic quoting requirement on a monthly basis going forward given their primarily floor-based operation. Specifically, the proposed rule change adopts Rule 5.52(d)(1)(B)<sup>7</sup> which provides that the Exchange may, in exceptional cases and where good cause is shown, grant a Market-Maker a reset of the Electronic Volume Threshold in subparagraph (d)(1)(A). If a Market-Maker trades more than 20% of the Market-Maker's contract volume electronically in an appointed class during a calendar quarter,

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<sup>6</sup> The Exchange is aware of at least two Market-Makers that triggered the Electronic Volume Threshold in the last months of 2019 and were subsequently unable to satisfy the continuous electronic quoting obligations. One such Market-Maker had been registered as a Market-Maker on the Exchange since 1997 (however, such firm has recently been dissolved) and one has been registered as a Market-Maker on the Exchange since 2001. The Exchange also notes that there are other Market-Makers that are not currently subject to the continuous electronic quoting requirements in their appointed classes. For example, the Exchange is aware of at least three Market-Makers that are not currently obligated to provide continuous electronic quotes in SPX.

<sup>7</sup> The proposed rule change also updates the format of Rule 5.51(d)(1) by adopting the title "Electronic Volume Threshold" and Rule 5.51(d)(1)(A) to govern the provision under current Rule 5.51(d)(1), and adopts the title "Continuous Electronic Quotes" for Rule 5.52(d)(2).

the Market-Maker may submit to the Exchange a request that the Exchange consider a reset of the Electronic Volume Threshold in the appointed class. If the Exchange determines that a Market-Maker qualifies for a reset of the 20% threshold in an appointed class, then the Market-Maker will not become subject to the continuous electronic quoting requirements pursuant to subparagraph (d)(2) in the appointed class in the next calendar quarter, and will again become subject to subparagraph (d)(1)(A) in the appointed class. In order to determine if a Market-Maker qualifies for a reset of the Electronic Volume Threshold in an appointed class, the Exchange may consider: (i) a Market-Maker's trading activity and business model in the appointed class; (ii) any previous requests for a reset of the Electronic Volume Threshold in the appointed class, including previously granted requests; (iii) market conditions and general trading activity in the appointed class; and (iv) any other factors as the Exchange deems appropriate in determining whether to approve a Market-Maker's request for an Electronic Volume Threshold reset. In this way, the proposed rule change allows those Market-Makers that predominantly provide liquidity on the trading floor and incidentally surpass (or have incidentally surpassed) the electronic volume threshold, and, subsequently, are not able to satisfy the continuous electronic quoting requirement on a monthly basis going forward, an opportunity to submit a request to the Exchange that they again be subject only to open outcry quoting requirements and continue to focus on providing liquidity in open outcry in accordance with their business models.<sup>8</sup>

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<sup>8</sup> The Exchange notes that the proposed rule change does not preclude the application of Rule 13.15(g)(14)(A), which, as part of the Minor Rule Violation Plan ("MRVP"), allows the Exchange to impose a fine on Market-Makers for failure to meet their continuous quoting obligations, including on any Market-Maker that is able to "reset" upon Commission approval of this proposal. The Exchange additionally notes that the proposed rule change also does not preclude the Exchange from referring matters covered under the MRVP for formal disciplinary action, pursuant to Rule 13.15(f), whenever it determines that any violation is intentional, egregious or otherwise not minor in nature.

Finally, the proposed rule change also removes the rollout period for new classes in Rule 5.52(d)(1), which currently provides that for a period of 90 days commencing immediately after a class begins trading on the System, this subparagraph (d)(1) governs trading in that class. The rollout period was implemented in connection with the transition of certain classes to the Exchange's former Hybrid System.<sup>9</sup> As of 2018, all classes listed for trading on the Exchange now trade on the same platform, the Exchange's System. Therefore, a rollout period is no longer necessary. All Market-Makers in new classes and likewise all new Market-Makers will be equally subject to the electronic volume threshold pursuant to Rule 5.52(d)(1) and (d)(2) upon starting out.

### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>10</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>11</sup> which requires, among other things, that the rules of a national securities 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

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<sup>9</sup> See Securities Exchange Act Release No. 47959 (May 30, 2003), 68 FR 34441 (June 9, 2003) (SR-CBOE-2002-05).

<sup>10</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>11</sup> 15 U.S.C. 78f(b)(5).

free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission believes that the proposal to allow the Exchange, in exceptional cases and where good cause is shown, to grant a Market-Maker's request for a reset of the Electronic Volume Threshold in subparagraph (d)(1)(A) of Rule 5.52 should promote just and equitable principles of trade by not requiring a Market-Maker that is accustomed to floor trading, and potentially lacking the appropriate technology, to provide continuous electronic quotes. The Commission notes that in determining whether to grant a Market-Maker's request for a reset of the Electronic Volume Threshold, the Exchange may consider, among other things: (i) a Market-Maker's trading activity and business model in the appointed class; (ii) any previous requests for a reset of the Electronic Volume Threshold in the appointed class, including previously granted requests; and (iii) market conditions and general trading activity in the appointed class. The Commission believes that the proposed rule is reasonably designed to limit application of the reset to only those firms who incidentally breached the Electronic Volume Threshold in certain appointed classes due to extraordinary or extreme market volatility or other circumstances outside of the Market-Maker's control.

In addition, the Commission believes that the proposal to remove the rollout period for new classes in Rule 5.52(d)(1) is consistent with the Act. The Commission notes that the rollout period was implemented in connection with the transition of certain classes to the Exchange's former Hybrid System and that all classes listed for trading on the Exchange now trade on the same platform. The Commission believes the proposal will help to protect investors and the public interest by removing outdated and potentially confusing language from the Exchange's rules.

Based on the foregoing, the Commission finds that the proposed rule change is consistent with the Act.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>12</sup> that the proposed rule change (SR- CBOE-2021-013) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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<sup>12</sup> 15 U.S.C. 78s(b)(2).

<sup>13</sup> 17 CFR 200.30-3(a)(12).