

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-81999; File No. SR-Phlx-2017-85)

November 2, 2017

Self-Regulatory Organizations; Nasdaq PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend the Price Improvement XL Auction

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on October 26, 2017, Nasdaq PHLX LLC (“Phlx” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III, 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 1080(n) related to Phlx’s Price Improvement XL (“PIXL”) auction.

The text of the proposed rule change is available on the Exchange’s Website at <http://nasdaqphlx.cchwallstreet.com/>, at the principal office of the Exchange, 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 the PIXL rule at 1080(n) to: (1) include a surrender provision; (2) update a reference to the NBBO to provide specificity to the rule; and (3) correct a typographical error, update a cross-reference and relocate rule text.

Surrender

The Exchange proposes to adopt a surrender provision within Rule 1080(n) for its PIXL auction similar to the surrender provision that is applicable to Nasdaq BX, Inc.’s (“BX”) surrender provision in the BX price improvement auction (“PRISM”) at Chapter VI, Section 9.

Current PIXL

By way of background, today, only one PIXL Auction may be conducted at a time in any given series. Once commenced, an Auction may not be cancelled and would proceed as described herein. To initiate the Auction, the Initiating Member must mark the PIXL Order for Auction processing, and specify either: (a) a single price at which it seeks to execute the PIXL Order (a “stop price”); (b) that it is willing to automatically match as principal or as agent on behalf of an Initiating Order the price and size of all PIXL Auction Notifications (“PAN”) responses, and trading interest (“auto-match”) in which case the PIXL Order will be stopped at the better of the NBBO or the Reference BBO³ on the Initiating Order side;⁴ or (c) that it is willing to either: (i) stop the entire order at a single stop price and auto-match PAN responses

³ The Reference BBO shall mean the internal best bid and offer on Phlx.

⁴ This is accomplished by marking the Initiating Order with a market price.

and trading interest at a price or prices that improve the stop price to a specified price (a “No Worse Than” or “NWT” price); (ii) stop the entire order at a single stop price and auto-match all PAN responses and trading interest at or better than the stop price; or (iii) stop the entire order at the better of the NBBO or Reference BBO on the Initiating Order side, and auto-match PAN responses and trading interest at a price or prices that improve the stop price up to the NWT price. In all cases, if the PBBO on the same side of the market as the PIXL Order represents a limit order on the book, the stop price must be at least one minimum price improvement increment better than the booked limit order’s limit price. Once the Initiating Member has submitted a PIXL Order for processing as described herein, such PIXL Order may not be modified or cancelled.⁵

Proposed PIXL Amendment

At this time, the Exchange proposes to add a paragraph to Rule 1080(n)(ii)(A)(1) stating that, when starting an Auction, the Initiating Member may submit the Initiating Order with a designation of “surrender” to other PIXL participants (“Surrender”), which will result in the Initiating Member forfeiting priority and trade allocation privileges which he or she is otherwise entitled to as per subsection (n)(ii)(E)(a) of Rule 1080(n).⁶ If Surrender is specified the Initiating Order will only trade if there is not enough interest available to fully execute the PIXL Order at

⁵ Under no circumstances will the Initiating Member receive an allocation percentage, at the final price point, of more than 50% with one competing quote, order or PAN response or 40% with multiple competing quotes, orders or PAN responses when competing quotes, orders or PAN responses have contracts available for execution.

⁶ Depending on the option selected, the Initiating Member may elect in the single stop option selection to give up the allocation priority, if Surrender is selected, or with the auto-match option the Initiating Member will only be allocated the remainder in accordance with the allocation percentages specified in Rule 1080(n)(ii)(E)(2)(b). The Surrender feature only applies to the single stop price feature. By definition the purpose of the auto-match feature is that the Initiating Member is going to match all responses and seek a greater allocation. This language is at odds with the Surrender feature where the Initiating Member is not seeking allocation.

prices which are equal to or improve upon the stop price. Phlx will allow surrender only for the entire amount, not for a partial amount. Surrender will not be applied if both the Initiating Order and PIXL Order are Public Customer Orders.

The Surrender function will never result in more than the maximum allowable allocation percentage to the Initiating Participant than that which the Initiating Member would have otherwise received in accordance with the allocation procedures set forth in this Rule. Surrender information will not be available to other market participants and may not be modified. The proposed provisions are similar to surrender provisions on BX PRISM.⁷

Similarly, the Exchange proposes to add a new paragraph at Rule 1080(n)(ii)(A)(2) which provides a similar provision for Complex Orders⁸. The proposed provision would provide that when starting a PIXL Complex Order Auction, the Initiating Member may submit the Initiating Order with a designation of Surrender to the other PIXL participants which will result in the Initiating Member forfeiting the priority and trade allocation privileges which he is otherwise entitled to as per subsection (n)(ii)(E)(2)(d) of Rule 1080(n). If Surrender is specified the Initiating Order will only trade if there is not enough interest available to fully execute the PIXL Order at prices which are equal to or improve upon the stop price. Throughout the rule where allocation is specified a notation is added to account for any surrender, if applicable such as in 1080(n)(ii)(E)(2)(a) and (d).

NBBO Reference

The Exchange proposes to reword Rule 1080(n)(ii)(F) to add specificity to the current rule text. The Exchange proposes to state that “If there are PAN responses (except if it is a

⁷ See Chapter VI, Section 9(ii)(A)(i).

⁸ Today, BOX Options Exchange LLC (“BOX”) utilizes a Surrender feature in its Complex Order Price Improvement Period or “COPIP.” See also BOX Rule 7245.

Complex Order) that cross the better of the Reference BBO and NBBO (provided such NBBO is not crossed) or Complex Order PAN responses that cross the then-existing cPBBO at the time of the conclusion of the Auction, such PAN responses will be executed, if possible, at their limit price(s).” In certain instances, a resting order or quote may be internally priced at a non-displayed price and would differ from the PBBO. The Internal BBO or “Reference BBO” would differ from the PBBO in a situation where the System prevents trade-throughs and locked and crossed markets. In these instances, interest will not be executed at a price that trades through another market or is displayed at a price that would lock or cross another market. If, at the time of entry, an order or quote would cause a locked or crossed market violation or would cause a trade-through violation, it will be re-priced to the current national best offer (for bids) or the current national best bid (for offers) and displayed at one minimum price variance above (for offers) or below (for bids) the national best price. For this reason, the Exchange is proposing more precise rule text at Rule 1080(n)(ii)(F) to account for these situations where there is an automatic repricing in order to prevent trade-throughs and locked and crossed markets. The Exchange proposes to change the rule text to acknowledge that repricing would result in the better of the NBBO (or PBBO) or the Reference BBO.

Typographical Error, Clarifying Change, Cross Reference and Relocated Text

The Exchange proposes to correct a word in Rule 1080(n)(i)(C) from “of” to “or” to correct an unintentional typographical error. The Exchange also proposes to replace a reference to “Rule 1080(n) at Commentary .07” to “Rule 1098” to properly reference rule text related to Complex Orders at Rule 1080(n)(ii)(E)(2)(f). A reference to “remaining” shares as Rule 1080(n)(ii)(E)(2)(f) is also proposed to be amended to “residual” simply to conform to the language utilized in other parts of the rule. Finally, rule text related to PIXL ISO in Commentary .08 to Rule 1080(n) is being relocated within the rule to new 1080(n)(ii)(K) simply to add the

text in an appropriate location within the rule. A space is also being added within the rule text that was inadvertently left out of a prior version.

Implementation

The Exchange proposes to implement this functionality before Q1 2018. Members will be notified of the deployment date by way of an Options Trader Alert.

Below is an example of the manner in which the Surrender feature would operate:

EXAMPLE (Related to Rule 1080(n)(ii)(A)(i) (Initiating Participant utilizing Surrender):

NBBO = .97 – 1.03

PHLX BBO = .95 – 1.03(60) with Market Maker A and Market Maker B offering 30 contracts each PIXL Order to buy 100 contracts stopped at 1.02 marked as ‘Surrender’ is received,

Auction begins,

During auction, Market Maker C responds to sell 5 at 1.01, Market Maker A responds to sell 5 contracts at 1.02, Market Maker B responds to sell 40 contracts at 1.02, and Market Maker D responds to sell 20 contracts at 1.02.

During auction, Market Maker A moves his quote and PHLX BBO becomes .95 – 1.02 for 5 contracts and NBBO becomes .97 – 1.02.

Auction ends, Market Maker C trades 5 at 1.01; Remaining Market Maker interest trades 70 contracts in a Pro-Rata fashion: Market Maker A executes 10 contracts with 5 being given to the Market Maker A response at 1.02 and 5 to the Market Maker A quote at 1.02; Market Maker B response executes 40 contracts at 1.02; Market Maker D response executes 20 contracts at 1.02. The PIXL Contra executes the remaining 25 contracts at 1.02. This is because the initiator will end up trading if not enough interest is there to satisfy the stop price.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,⁹ in general, and furthers the objectives of Section 6(b)(5) of the Act,¹⁰ in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, by proposing a functionality which allows members more optionality to transact orders in the PIXL auction. The Exchange believes that the proposed feature will provide members with more flexibility, similar to functionality currently offered on BX. In addition the Exchange proposes other amendments which add clarity to the rule text so that members will gain a greater understanding of the rule. Each proposal is discussed below.

Surrender

The Exchange believes that the Surrender feature is consistent with the Act because it promotes just and equitable principles of trade by allowing members who submit orders into the PIXL Auction to continue to be executed pursuant to a pre-determined set of rules which would allow members to forfeit priority and trade allocation privileges and only trade if there is not enough interest available to fully execute the PIXL Order at prices which are equal to or improve upon the stop price. Members are not required to elect this feature, but it would be available, as it is today on BX, if a member desired to utilize the Surrender feature. The new Surrender feature would provide the Initiator with flexibility, thereby increasing the likelihood that the Initiator would be inclined to commence more auctions.

The feature would only permit the member to surrender the entire amount, not a partial amount. Also, Surrender will not be applied if both the Initiating Order and PIXL Order (or

⁹ 15 U.S.C. 78f(b).

¹⁰ 15 U.S.C. 78f(b)(5).

PIXL Complex Order) are Public Customer Orders. The Surrender feature will not permit a member to have any control over an order. Further, the election to Surrender an order would be available prior to the submission of the order and therefore could not be utilized to gain influence or guide the execution of the PIXL Order or PIXL Complex Order. Initiating Members submitting PIXL Orders or PIXL Complex Orders will relinquish control of their PIXL Orders or PIXL Complex Orders upon transmission to the Exchange's System. Further, no Participant, including the Initiating Participant, will see a PAN response submitted into PIXL and therefore and will not be able to influence or guide the execution of their PIXL Orders or PIXL Complex Orders. The information provided with respect to the Surrender feature by the member will not be broadcast and further, the information may not be modified by the member during the auction.

NBBO Reference

The Exchange's proposal to amend Rule 1080(n)(ii)(F) to amend the current rule text for the addition of language to include the "Reference BBO" to clarify where the price is equal to or better than the NBBO or PBBO and the Reference BBO (internal market BBO), due to repricing for trade-throughs or locked and crossed markets, adds clarity and precision to the current rule text. The Exchange believes that these proposed amendments are consistent with the Act and do not otherwise create an impediment to a free and open market because today investors are subject to this repricing. Also, by reflecting the proper rule text to account for these order types the Exchange is providing members with additional information with which to anticipate the manner in which the Exchange's trading system reprices interest to prevent a trade-through or locked and crossed market.

Typographical Error, Clarifying Change, Cross Reference and Relocated Text

The Exchange's proposals to: (a) correct a word in Rule 1080(n)(i)(C) from "of" to "or"; (b) replace a reference to Rule 1080(n) at Commentary .07 to Rule 1098 to properly reference

rule text related to Complex Orders at Rule 1080(n)(ii)(E)(2)(f); (c) change a reference to “remaining” shares as Rule 1080(n)(ii)(E)(2)(f) to “residual”; and (d) relocate PIXL ISO in Commentary .08 to Rule 1080(n) to 1080(n)(ii)(K) are consistent with the Act because these amendments provide greater detail and clarity to the rule text.

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 not necessary or appropriate in furtherance of the purposes of the Act. The competition among the options exchanges is vigorous and this proposal is intended to afford the Exchange the opportunity to compete for order flow by offering an auction mechanism with a surrender feature similar to that of other exchanges.¹¹

With respect to intra-market competition, the auction will be available to all Phlx members. The Exchange’s proposal to submit the Surrender amendment does not result in less competition, the PIXL mechanism should continue to encourage Phlx members to compete amongst each other by responding with their best price and size for a particular auction. The Exchange believes that the Initiator may be incentivized to initiate more PIXL auctions in light of the proposal. The Exchange’s proposal is a competitive response to similar provisions in the price improvement auction rules of other options exchanges.¹² The Exchange believes this proposed rule change is necessary to permit fair competition among the options exchanges and to

¹¹ Today, BX offers a surrender feature. See BX Rule at Chapter VI, Section 9. The Chicago Board Options Exchange, Incorporated (“CBOE”) has a process whereby initiating participants may elect to receive last priority in an allocation. See CBOE Rule 6.74A(b)(3)(J), entitled Automated Improvement Mechanism (“AIM”). Finally, BOX utilizes a Surrender feature in its PIP and COPIP, similar to the proposed Phlx Surrender for simple and complex orders. The Exchange notes that BOX Initiators may forfeit less than the entire amount pursuant to the BOX rule. See BOX Rules 7150 and 7245. Phlx will allow surrender only for the entire amount, not for a partial amount.

¹² Id.

establish more uniform price improvement auction rules on the various options exchanges. The Exchange anticipates that this auction proposal will allow Phlx to compete on equal footing with other options exchanges and for this reason the proposal does not create an undue burden on inter-market competition.

The Exchange's proposal to amend Rule 1080(n)(ii)(F) to amend the current rule text for the addition of language to include the "Reference BBO" to clarify where the price is equal to or better than the NBBO or PBBO and the Reference BBO (internal market BBO), due to repricing for trade-throughs or locked and crossed markets, adds clarity and precision to the current rule text. The proposed amendments would apply uniformly to all Phlx members that elect to enter orders into the PIXL auction. The Exchange believes that these proposed amendments are consistent with the Act and do not otherwise create an impediment to a free and open market because today investors are subject to this repricing.

The Exchange's proposals to: (a) correct a word in Rule 1080(n)(i)(C) from "of" to "or"; (b) replace a reference to Rule 1080(n) at Commentary .07 to Rule 1098 to properly reference rule text related to Complex Orders at Rule 1080(n)(ii)(E)(2)(f); (c) change a reference to "remaining" shares as Rule 1080(n)(ii)(E)(2)(f) to "residual"; and (d) relocate PIXL ISO in Commentary .08 to Rule 1080(n) to 1080(n)(ii)(K) simply provide greater detail and clarity to the rule text.

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

No written comments were either solicited or received.

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)(iii) of the Act¹³ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹⁴

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: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule 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-Phlx-2017-85 on the subject line.

¹³ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁴ 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.

Paper Comments:

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

All submissions should refer to File Number SR-Phlx-2017-85. 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. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to

make available publicly. All submissions should refer to File Number SR-Phlx-2017-85 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.¹⁵

Eduardo A. Aleman
Assistant Secretary

¹⁵ 17 CFR 200.30-3(a)(12).