

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-82245; File No. SR-Phlx-2017-99)

December 8, 2017

Self-Regulatory Organizations; Nasdaq PHLX LLC; Notice of Filing of Proposed Rule Change to Amend the Exchange Rules to Make Permanent a Program that Allows Transactions to Take Place in Open Outcry Trading at Prices of at Least \$0 But Less Than \$1 per Option Contract (“sub-dollar cabinet trades”)

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 November 29, 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 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 a proposal[sic] to amend the Exchange’s rules to make permanent a program that allows transactions to take place in open outcry trading at prices of at least \$0 but less than \$1 per option contract (“sub-dollar cabinet trades”).

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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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 1059 to make permanent a program that allows transactions to take place at a price that is below \$1 per option contract.³ The program is currently subject to a pilot that is scheduled to expire on January 5, 2018.⁴

An “accommodation” or “cabinet” trade refers to trades in listed options on the Exchange that are worthless or not actively traded. Trading is generally conducted in accordance with Exchange Rules, except as provided in Exchange Rule 1059, Accommodation Transactions (Cabinet Trades), which sets forth specific procedures for engaging in cabinet trades.

Rule 1059 provides that a “cabinet order” is a closing limit order at a price of \$1 per option contract for the account of a customer, firm, specialist or ROT. An opening order is not a “cabinet order” but may in certain cases be matched with a cabinet order. Prior to the pilot program, only closing limit orders at a price of \$1 per option contract for the accounts of customer, firm, specialists and Registered Options Traders (“ROTs”) could be placed in the cabinet.

³ See Commentary .02, Limit Orders Priced Below \$1, to Exchange Rule 1059, Accommodation Transactions.

⁴ See Securities Exchange Act Release No. 79782 (January 12, 2017), 82 FR 6667 (January 19, 2017) (SR-Phlx-2017-01). The Exchange initially adopted the program in 2010. See Securities Exchange Act Release No. 63626 (December 30, 2010), 76 FR 812 (January 6, 2011) (SR-Phlx-2010-185).

Rule 1059 currently provides that cabinet transactions at a price of \$1 per option contract may occur via open outcry in any options series open for trading on the Exchange. However, the \$1 Cabinet Trading procedures are not available in Penny Pilot Program classes because in those classes an option series can trade in a standard increment as low as \$ 0.01 per share (or \$1.00 per option contract with a 100 share multiplier).

The Exchange amended the Cabinet Trading procedures to allow transactions to take place in open outcry at a price of at least \$0 but less than \$1 per option contract. This amendment expires on January 5, 2018. These lower-priced transactions are permitted to be traded pursuant to the same procedures applicable to \$1 Cabinet Trades, except that (i) bids and offers for opening transactions are only permitted to accommodate closing transactions, and (ii) transactions in option classes participating in the Penny Pilot Program are permitted. The Exchange believes that allowing a price of at least \$0 but less than \$1 better accommodates the closing of options positions in series that are worthless or not actively traded, particularly when there has been a significant move in the price of the underlying security, resulting in a large number of series being out-of-the-money. For example, a market participant might have a long position in a put series with a strike price of \$30 and the underlying stock might be trading at \$100. In such an instance, there is likely no market to close-out the position, even at the \$1 cabinet price.

As with other accommodation liquidations under Rule 1059, transactions at prices less than \$1 are not disseminated to the public on the consolidated tape. In addition, as with other accommodation liquidations under Rule 1059, the transactions are exempt from the Consolidated Options Audit Trail (“COATS”) requirements of Exchange Rule 1063(e)(i). However, Rule

1059 requires all transactions, including transaction for less than \$1, to be reported to the Exchange following the close of each business day.

The Exchange notes that while the level of liquidation trades is not meaningful, such trades serve an essential purpose in that they allow market participants to close out options positions that are worthless or not actively trading. To illustrate, in 2016, there were a total of 442 Cabinet Trades comprising 244,734 contracts. Each contract was executed at a trade price of \$ 0.01. The Exchange believes this level of trading demonstrates the benefit of the current program to market participants.

The current rule was adopted on a pilot basis to provide the Exchange time to evaluate the efficacy of the change and to address any operational issues that might arise in processing Cabinet trades. In support of making the program permanent, the Exchange represents that there are no operational issues in processing and clearing Cabinet Trades in penny and subpenny increments. The Exchange is also not aware of the Options Clearing Corporation (“OCC”) having operational issues with processing Cabinet trades submitted by the Exchange. Each Cabinet Trade is input manually into the clearing system, and then flows seamlessly for settlement at OCC. More specifically, upon receiving an order for a Cabinet Trade, a Floor Broker fills out a designated cabinet transaction form provided by the Exchange noting the order details. The Floor Broker subsequently calls for a market for the order by announcing the terms of the order to the trading crowd. The Floor Broker proceeds to execute the order and submits the designated cabinet transaction form to the Nasdaq Market Operations staff for clearance and reporting at the close of the business day. Nasdaq Market Operations staff then enter the transaction into the Phlx system, which transmits the trade to OCC for clearance and settlement.

At the time of adoption of the pilot the Phlx system permitted reporting a cabinet trade at a price as small as \$0.0001, as it does today. The Exchange system allows Cabinet trades to be processed in a manner similar to how all other trades are processed by the exchange.

Additionally, the Exchange notes that members and member organizations have not raised any concerns with the processing of Cabinet Trades.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,⁵ in general, and furthers the objectives of Section 6(b)(5) of the Act,⁶ 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. The Exchange believes that liquidation trades promote competition and afford market participants the opportunity to close out their options positions. The Exchange believes that permanently approving the rules that allow for liquidations at a price less than \$1 per option contract would better facilitate the closing of options positions that are worthless or not actively trading, especially in Penny Pilot issues where Cabinet Trades are not otherwise permitted. The Exchange believes that approving the program on a permanent basis is also consistent with the Act. With respect to the level of liquidation trades transacted on the Exchange, the Exchange believes that the data gathered provides meaningful support to make the program permanent.

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

⁵ 15 U.S.C. 78f(b).

⁶ 15 U.S.C. 78f(b)(5).

Exchange believes that approving the program on a permanent basis will not impact competition, as it will continue to facilitate members' ability to close positions in worthless or not actively traded series.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission shall: (a) by order approve or disapprove such proposed rule change, or (b) institute proceedings to determine whether the proposed rule change should be 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-2017-99 on the subject line.

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-Phlx-2017-99. 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-2017-99 and should be submitted on or before [insert date 15 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁷

Eduardo A. Aleman
Assistant Secretary

⁷ 17 CFR 200.30-3(a)(12).