



8011-01p
SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-83209; File No. SR-Phlx-2018-22)

May 10, 2018

Self-Regulatory Organizations; Nasdaq PHLX LLC; Order Granting Approval of Proposed Rule Change To Create a New Rule 1081, To Amend Electronic Market Maker Obligations and Quoting Requirements for Electronic ROTs, Which Will Be Defined To Include SQTs, RSQTs, Directed SQTs, Directed RSQTs, Specialists, and Remote Specialists

I. Introduction

On March 20, 2018, Nasdaq PHLX LLC (“Phlx” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend the market maker obligations and quoting requirements for an SQT, RSQT, Directed SQT, Directed RSQT, and Specialist (including Remote Specialist) who enters electronic quotations into the Exchange’s System.³ The proposed rule change was published for comment in the Federal Register on April 5, 2018.⁴ The Commission received no comments on the proposed rule change. This order grants approval of the proposed rule change.

II. Description of the Proposed Rule Change

The Exchange proposes to amend the market maker obligations and quoting

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See infra notes 5-9 for definitions of SQT, RSQT, Directed SQT, Directed RSQT, Specialist, Remote Specialist, and System.

⁴ See Securities Exchange Act Release No. 82975 (March 30, 2018), 83 FR 14690 (April 5, 2018) (“Notice”).

requirements for an “electronic ROT,” which would be defined to include an SQT,⁵ RSQT,⁶ Directed SQT, Directed RSQT,⁷ and Specialist (including Remote Specialist)⁸ who enters electronic quotations into the Exchange’s System,⁹ and move these modified provisions to new Phlx Rule 1081.¹⁰ The Exchange notes that non-SQT ROTs¹¹ would not be subject to the

⁵ An “ROT” is a regular member of the Exchange located on the trading floor who has received permission from the Exchange to trade in options for his own account. See Phlx Rule 1014(b)(i). A “Streaming Quote Trader” or “SQT” is an ROT who has received permission from the Exchange to generate and submit option quotations electronically in options to which such SQT is assigned. An SQT may only submit such quotations while such SQT is physically present on the floor of the Exchange. An SQT may only trade in a market making capacity in classes of options in which the SQT is assigned. See Phlx Rule 1014(b)(ii)(A).

⁶ A “Remote Streaming Quote Trader” or “RSQT” is an ROT that is a member affiliated with a “Remote Streaming Quote Trader Organization” or “RSQTO” with no physical trading floor presence who has received permission from the Exchange to generate and submit option quotations electronically in options to which such RSQT has been assigned. See Phlx Rule 1014(b)(ii)(B). See also Phlx Rule 507(a).

⁷ A “Directed SQT” or “Directed RSQT” is an SQT or RSQT that receives a Directed Order. A “Directed Order” is any order (other than a stop or stop-limit order as defined in Phlx Rule 1066) to buy or sell which has been directed to a particular Specialist, RSQT, or SQT by an Order Flow Provider. An “Order Flow Provider” is any member or member organization that submits, as agent, orders to the Exchange. See Phlx Rule 1068(a)(i).

⁸ A “Specialist” is an Exchange member who is registered as an options specialist pursuant to Phlx Rule 501 and Phlx Rule 1020(a). A “Remote Specialist” is an options specialist that does not have a physical presence on an Exchange floor. See Phlx Rule 1020(a)(i) and (ii).

⁹ The “System” is the automated system for order execution and trade reporting owned and operated by the Exchange which comprises: (A) an order execution service that enables members to automatically execute transactions in “System Securities” (defined as all options that are currently trading on the System); and provides members with sufficient monitoring and updating capability to participate in an automated execution environment; (B) a trade reporting service that submits “locked-in” trades for clearing to a registered clearing agency for clearance and settlement; transmits last-sale reports of transactions automatically to the Options Price Reporting Authority for dissemination to the public and industry; and provides participants with monitoring and risk management capabilities to facilitate participation in a “locked-in” trading environment; and (C) the data feeds described in Phlx Rule 1070. See Phlx Rule 1000(b)(45) and (46).

¹⁰ See proposed Phlx Rule 1081.

proposed quoting requirements described herein; instead, they are subject to quarterly trading requirements as specified in Phlx Rule 1014, Commentary .01.¹²

A. Market Maker Obligations

The Exchange proposes first to amend the generalized description of the market making obligations of an electronic ROT on the Exchange. Today, the Exchange provides that transactions of a Specialist and an ROT should constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market, and that those members should not enter into transactions or make bids or offers that are inconsistent with such a course of dealings.¹³ In the Exchange's proposal, new Phlx Rule 1081 would specify that, in registering as an electronic ROT, a member organization would be committing to various obligations. Transactions of an electronic ROT in its market making capacity¹⁴ would be required to constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market, and those member organizations would not be permitted to make bids or offers or enter into transactions that are inconsistent with such course of dealings. Electronic ROTs would be prohibited from effecting purchases or sales except in a reasonable and orderly manner.¹⁵

¹¹ A non-SQT ROT is an ROT who is neither an SQT nor an RSQT. See Phlx Rule 1014(b)(ii)(C).

¹² See Notice, supra note 4, at 14690.

¹³ See Phlx Rule 1014(a).

¹⁴ According to the Exchange, orders, which electronic ROTs may enter pursuant to Phlx Rule 1080(b)(i)(B), are not considered market making activity for purposes of fulfilling the proposed quoting requirements or other obligations. See Notice, supra note 4, at 14690 n.5.

¹⁵ See proposed Phlx Rule 1081(a).

In addition, ordinarily during trading hours, an electronic ROT would be required to: (i) maintain a two-sided market in those options in which the electronic ROT is registered to trade, in a manner that enhances the depth, liquidity, and competitiveness of the market; (ii) engage, to a reasonable degree under the existing circumstances, in dealings for its own account when there exists, or it is reasonably anticipating that there will exist, a lack of price continuity, a temporary disparity between the supply of (or demand for) a particular option contract, or a temporary distortion of price relationships between option contracts of the same class; (iii) compete with other electronic ROTs in all options in all capacities in which the electronic ROT is registered to trade; (iv) make markets that will be honored for the number of contracts entered into the System in all options in which the electronic ROT is registered to trade; (v) update quotations in response to changed market conditions in all options in which the electronic ROT is registered to trade; (vi) maintain active markets in all options in which the electronic ROT is registered; and (vii) honor all orders attributed to the electronic ROT that the System routes to away markets pursuant to Phlx Rule 1080(m).¹⁶

The proposed rules provide further that, if Phlx Regulation found any substantial or continued failure to engage in a course of dealings as described above, the electronic ROT would be subject to disciplinary action or suspension or revocation of registration in one or more of the securities in which the electronic ROT is registered. The proposed rule stipulates that nothing in the rule would limit any other power of the Board under the rules, or procedures of the Exchange, with respect to the registration of an ROT or any violation by an ROT pursuant to the

¹⁶ See proposed Phlx Rule 1081(a).

rule.¹⁷ The Exchange states that the proposed obligations are similar to those imposed on market makers by another options exchange.¹⁸

B. Quoting Requirements

The Exchange further proposes to amend the quoting requirements for electronic ROTs. Electronic ROTs would be required to enter bids and offers for the options to which they are registered, except in an assigned options series listed intra-day on the Exchange. On a daily basis, an electronic ROT would be required to make markets consistent with the applicable quoting requirements, as described further below. A member organization would be required to meet each quoting requirement separately depending on the role that the member organization plays with respect to different options series.¹⁹

The proposed rules would state explicitly that an electronic ROT's bid and offer for a series of options contracts would need to be accompanied by the number of contracts at that price that the electronic ROT is willing to buy or sell. Similar to under current rules, the best bid or best offer submitted by an electronic ROT would be required to have a size of not less than the minimum number of contracts determined by the Exchange on a class-by-class basis, which

¹⁷ See proposed Phlx Rule 1081(b). The Exchange explains that it added this rule text to make clear that the obligations noted within this proposed rule are not an exclusive list, because an electronic ROT may be found to have violated other by-laws and rules of the Exchange that are separate and apart from these obligations. See Notice, *supra* note 4, at 14691 n.9.

¹⁸ See Notice, *supra* note 4, at 14690-91 & n.8. See also BX Rules at Chapter VII, Section 5.

¹⁹ See proposed Phlx Rule 1081(c). Specifically, the proposed rule states that an SQT and RSQT who is also the Specialist would be held to the quoting requirements for Specialists in options series in which the Specialist is assigned and would be held to the quoting requirements for SQTs and RSQTs in all other options series where assigned. An SQT or RSQT who receives a Directed Order would be held to the quoting requirements for Directed SQTs and Directed RSQTs. See *id.*

minimum will be at least one contract.²⁰ The new rule would also state that an electronic ROT that enters a bid in a registered option series would be required to enter an offer and vice versa. The quotations would need to meet the legal quote width requirements in Phlx Rule 1014(c)(i)(A)(1) and (2).²¹

With respect to the specific quoting requirements, currently, the Exchange requires an SQT and an RSQT to quote two-sided markets in not less than 60% of the series in which such SQT or RSQT is assigned. To satisfy these requirements when quoting a series, an SQT or RSQT must quote such series 90% of the trading day (as a percentage of the total number of minutes in such trading day) or such higher percentage as the Exchange may announce in advance. These obligations apply collectively to all appointed issues, rather than on an issue-by-issue basis.²² Under the proposal, SQTs and RSQTs associated with the same member organization would be collectively required to provide two-sided quotations in 60% of the cumulative number of seconds, or such higher percentage as the Exchange may announce in advance, for which that member organization's assigned option series are open for trading.²³

In addition, currently, the Exchange requires a Specialist, including an RSQT functioning as a Remote Specialist, to quote two-sided markets in the lesser of 99% of the series or 100% of the series minus one call-put pair in each option in which such Specialist is assigned. To satisfy these requirements when quoting a series, a Specialist must quote such series 90% of the trading day (as a percentage of the total number of minutes in such trading day) or such higher

²⁰ See proposed Phlx Rule 1081(c)(i). See also Phlx Rule 1014(b)(ii)(D)(3) (specifying the minimum contract size for SQTs, RSQTs, and Specialists), the current equivalent provision that is being replaced.

²¹ See proposed Phlx Rule 1081(c)(ii).

²² See Phlx Rule 1014(b)(ii)(D)(1).

²³ See proposed Phlx Rule 1081(c)(ii)(A). See *infra*, notes 35-36 and accompanying text, regarding the method by which the percentage would be calculated.

percentage as the Exchange may announce in advance. These obligations apply collectively to all appointed issues, rather than on an issue-by-issue basis.²⁴ Under the proposal, Specialists (including Remote Specialists) associated with the same member organization would be collectively required to provide two-sided quotations in 90% of the cumulative number of seconds, or such higher percentage as the Exchange may announce in advance, for which that member organization's assigned options series are open for trading.²⁵ The Exchange states that the Specialists' heightened quoting requirements as compared to SQTs and RSQTs allow for Specialists to receive certain participation rights.²⁶

Further, currently, the Exchange requires a Directed SQT and a Directed RSQT to quote two-sided markets in the lesser of 99% of the series listed on the Exchange or 100% of the series listed on the Exchange minus one call-put pair,²⁷ in each case in at least 60% of the options in which such Directed SQT or Directed SQT is assigned.²⁸ To satisfy these requirements when quoting a series, a Directed SQT or Directed RSQT must quote such series 90% of the trading day (as a percentage of the total number of minutes in such trading day) or such higher percentage as the Exchange may announce in advance. These obligations apply collectively to

²⁴ See Phlx Rule 1014(b)(ii)(D)(2).

²⁵ See proposed Phlx Rule 1081(c)(ii)(B). See *infra*, notes 35-36 and accompanying text, regarding the method by which the percentage would be calculated.

²⁶ See Notice, *supra* note 4, at 14693. See also Phlx Rules 1014(g)(ii) and 1014(g)(vii)(B)(1)(c).

²⁷ "Call-put pair" refers to one call and one put that cover the same underlying instrument and have the same expiration date and exercise price. See Phlx Rule 1014(b)(ii)(D)(6).

²⁸ See Phlx Rule 1014(b)(ii)(D)(1). Whenever a Directed SQT or Directed RSQT enters a quotation in an option in which such Directed SQT or Directed RSQT is assigned, such Directed SQT or Directed RSQT must maintain until the close of that trading day quotations for the lesser of 99% of the series of the option listed on the Exchange or 100% of the series of the option listed on the Exchange minus one call-put pair. See *id.*

all appointed issues, rather than on an issue-by-issue basis.²⁹ Under the proposal, Directed SQTs and Directed RSQTs associated with the same member organization would be collectively required to provide two-sided quotations in 90% of the cumulative number of seconds, or such higher percentage as the Exchange may announce in advance, for which that member organization's assigned options series are open for trading. A member organization would be considered directed in all assigned options once the member organization receives a Directed Order in any option in which they are assigned and would be considered a Directed SQT or Directed RSQT until such time as the member organization notifies the Exchange that they are no longer directed.³⁰ The Exchange notes that the Directed SQTs and Directed RSQTs' heightened quoting requirements as compared to SQTs and RSQTs allow for Directed SQTs and Directed RSQTs to receive certain participation rights.³¹

The Exchange states that the proposal better accommodates the occasional issues that may arise in a particular series, arguing that the existing quoting requirements may at times discourage liquidity in particular options series because an electronic ROT is forced to focus on a momentary lapse, rather than using the appropriate resources to focus on the options series that need and consume additional liquidity.³²

For SQTs, RSQTs, Directed SQTs, and Directed RSQTs, the Exchange would continue to exclude from the above quoting requirements any Quarterly Option Series, Adjusted Option Series, and any option series until the time to expiration for such series is less than nine

²⁹ See id.

³⁰ See proposed Phlx Rule 1081(c)(ii)(C). See infra, notes 35-36 and accompanying text, regarding the method by which the percentage would be calculated.

³¹ See Notice, supra note 4, at 14693. See also Phlx Rule 1014(g)(viii)(B).

³² See Notice, supra note 4, at 14695.

months.³³ Specialists would continue to be subject to the above quoting requirements for all assigned option series, including Quarterly Option Series, Adjusted Option Series, and any option series with an expiration of nine months or greater.³⁴

The Exchange would calculate compliance with the above quoting requirements by (i) taking the total number of seconds the member organization disseminates quotes in each assigned option series;³⁵ and (ii) dividing that time by the eligible total number of seconds each assigned option series is open for trading that day. Quoting would not be required in every assigned options series and compliance with this requirement would be determined by reviewing the aggregate of quoting in assigned options series for the member organization.³⁶ Similar to current requirements, the Exchange would consider exceptions to the quoting requirements based on demonstrated legal or regulatory requirements or other mitigating circumstances. The Exchange would determine compliance with quoting requirements on a monthly basis. However, this monthly compliance evaluation would not relieve a member organization of the obligation to provide continuous two-sided quotes on a daily basis or prohibit the Exchange from taking disciplinary action against a member organization for failure to meet the quoting

³³ See proposed Phlx Rule 1081(c)(ii)(A) and (C). See also Phlx Rule 1014(b)(ii)(D)(4), the current equivalent provision that is being replaced. An “Adjusted Option Series” would be defined as an option series wherein one option contract in the series represents the delivery of other than 100 shares of underlying stock or Exchange-Traded Fund Shares. See proposed Phlx Rule 1081(c)(ii)(A)(i). See also Phlx Rule 1014(b)(ii)(D)(4).

³⁴ See proposed Phlx Rule 1081(c)(ii)(B).

³⁵ With respect to SQTs, RSQTs, Directed SQTs, and Directed RSQTs, such calculation would exclude Quarterly Option Series, Adjusted Option Series, and any option series with an expiration of nine months or greater. See proposed Phlx Rule 1081(c)(ii)(D).

³⁶ See proposed Phlx Rule 1081(c)(ii)(D). See Notice, *supra* note 4, at 14694, for an example of how the Exchange would calculate compliance with the quoting requirements.

requirements each trading day.³⁷ If a technical failure or limitation of a System of the Exchange prevents a member organization from maintaining, or prevents a member organization from communicating to the Exchange timely and accurate quotes, the duration of such failure or limitation would not be included in any calculation of quoting requirements with respect to the affected quotes.³⁸

The Exchange states that the proposed quoting requirements as described above are similar to those of another options exchange.³⁹

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.⁴⁰ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,⁴¹ 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 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.

³⁷ See proposed Phlx Rule 1081(c)(iii). See also Phlx Rule 1014(b)(ii)(D)(1) and (2), the current equivalent provision that is being replaced.

³⁸ See proposed Phlx Rule 1081(c)(iv). See also Phlx Rule 1014(b)(ii)(D)(5), the current equivalent provision that is being replaced.

³⁹ See Notice, supra note 4, at 14692-93. See also BX Rules at Chapter VII, Sections 6, 14, and 15.

⁴⁰ 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).

⁴¹ 15 U.S.C. 78f(b)(5).

The Exchange proposes to add specificity regarding the general description in its rules regarding market maker obligations of an electronic ROT. The Commission finds that the changes it is making in this regard are consistent with the Act and notes that, as the Exchange maintains, the changes are consistent with the rules of another options exchange.⁴²

The Exchange proposes to reduce the specific quoting requirements for electronic ROTs of the various types. SQTs and RSQTs associated with the same member organization would be collectively required to provide two-sided quotations in 60% of the cumulative number of seconds for which that member organization's assigned option series are open for trading. Specialists (including Remote Specialists) associated with the same member organization would be collectively required to provide two-sided quotations in 90% of the cumulative number of seconds for which that member organization's assigned option series are open for trading. Similarly, Directed SQTs and Directed RSQTs associated with the same member organization would be collectively required to provide two-sided quotations in 90% of the cumulative number of seconds for which that member organization's assigned option series are open for trading. The Exchange would be able to designate a higher percentage for any of these quoting requirements by announcing such percentage in advance.

These quoting requirements would apply to all of an electronic ROT's assigned options on a daily basis. These quoting requirements would be reviewed on a monthly basis, and would allow the Exchange to review the electronic ROT's daily compliance in the aggregate and determine the appropriate disciplinary action for single or multiple failures to comply with the continuous quoting requirement during the month period. The Commission notes that the proposed rules provide that determining compliance with the continuous quoting requirements

⁴² See BX Rules, Chapter VII, Section 5.

on a monthly basis would not relieve the electronic ROT of the obligation to provide continuous two-sided quotes on a daily basis, nor would it prohibit the Exchange from taking disciplinary action against an electronic ROT for failing to meet the continuous quoting requirements each trading day.

The Commission finds that the proposed changes to the quoting requirements of electronic ROTs are consistent with the Act. The Exchange believes that the revised requirements will enable electronic ROTs to focus on the options series that need and consume more liquidity than others. To the extent this is true, the proposal will enhance trading opportunities on the Exchange. Moreover, the Commission believes that, although the proposal would reduce the quoting requirements for the various electronic ROTs from their current levels, the proposed changes are consistent, as the Exchange argues, with the market maker quoting requirements in place on other markets.⁴³ The Commission further notes that, notwithstanding the proposed changes to the quoting requirements for Specialists, Directed SQTs, and Directed RSQTs, the revised quoting requirements continue to reflect meaningful market making obligations. Additionally, the proposed rules reflect a balance of rights and obligations consistent with the balance reflected in the rules of other exchanges for market participants fulfilling a similar role.⁴⁴ In addition, the Commission believes that the proposed changes to provide additional detail about how the Exchange will apply these quoting requirements adds further clarity to the rules.

⁴³ See, e.g., BX Rules, Chapter VII, Sections 6, 14, and 15; NYSE American Rules 925.1NY and 964.1NY; NYSE Arca Rules 6.37B-O and 6.88-O.

⁴⁴ See, e.g., Nasdaq GEMX Rules 713 and 804; Nasdaq ISE Rules 713 and 804; Nasdaq MRX Rules 713 and 804. See also supra notes 26 and 31 and accompanying text.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁴⁵ that the proposed rule change (SR-Phlx-2018-22), be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁶

Eduardo A. Aleman
Assistant Secretary

⁴⁵ Id.

⁴⁶ 17 CFR 200.30-3(a)(12).

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