8011-01
SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-87537; File No. SR-Phlx-2019-48)

November 14, 2019

Self-Regulatory Organizations; Nasdaq PHLX LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend the Customer Rebate Program

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 1, 2019, Nasdaq PHLX LLC ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("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 the Exchange's Customer Rebate Program, as set forth in the Pricing Schedule at Options 7, Section 1, Part B.

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

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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 purpose of the proposed rule change is to amend the Exchange's Customer Rebate Program, as set forth in the Pricing Schedule at Options 7, Section 1, Part B. As described in greater detail below, the Exchange proposes to adopt an alternative method for members or member organizations (hereinafter, "members") to qualify for the program's Tier 2 rebates based on the member meeting a certain percentage threshold of total national Customer[3] volume in multiply-listed options classes, reaching the Monthly Firm Fee Cap,[4] and meeting the Exchange's Market Access and Routing Subsidy ("MARS") System Eligibility[5] requirements.

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3 The term "Customer" applies to any transaction that is identified by a member for clearing in the Customer range at The Options Clearing Corporation ("OCC") which is not for the account of a broker or dealer or for the account of a "Professional" (as that term is defined in Rule 1000(b)(14)). See Options 7, Section 1.

4 Firms are subject to a maximum fee of $75,000 ("Monthly Firm Fee Cap"). Firm Floor Option Transaction Charges and QCC Transaction Fees, as set forth in Options 7, Section 4, in the aggregate, for one billing month will not exceed the Monthly Firm Fee Cap per member organization when such members are trading in their own proprietary account. All dividend, merger, and short stock interest strategy executions (as defined in this Options 7, Section 4) will be excluded from the Monthly Firm Fee Cap. NDX and NDXP Options Transactions will be excluded from the Monthly Firm Fee Cap. Reversal and conversion, jelly roll and box spread strategy executions (as defined in this Options 7, Section 4) will be included in the Monthly Firm Fee Cap. QCC Transaction Fees are included in the calculation of the Monthly Firm Fee Cap. See Options 7, Section 4.

5 To qualify for MARS, a Phlx member's routing system (hereinafter "System") would be required to: (1) enable the electronic routing of orders to all of the U.S. options exchanges, including Phlx; (2) provide current consolidated market data from the U.S. options exchanges; and (3) be capable of interfacing with Phlx's API to access current Phlx match engine functionality. Further, the member's System would also need to cause Phlx to be the one of the top five default destination exchanges for individually executed marketable orders if Phlx is at the national best bid or offer ("NBBO"), regardless of size or time, but allow any user to manually override Phlx as a default destination on an order-

With the proposed changes, the Exchange seeks to attract additional liquidity and order flow to the Exchange, which will benefit all market participants from increased opportunities for price improvement.

Background

Options 7, Section 4 sets forth a Monthly Firm Fee Cap that limits, or caps, at $75,000 per month the Firm[6] Floor Option Transaction Charges and Firm QCC Transaction Fees incurred by members trading in their own proprietary account.[7] The Monthly Firm Fee Cap is designed to provide an incentive for members to bring additional Firm floor and QCC order flow to the Exchange.

Options 7, Section 6, Part E sets forth the Exchange's MARS program, which provides rebates to qualifying members with System Eligibility and that execute the requisite number of Eligible Contracts[8] in a month. MARS is designed to attract electronic equity and ETF options

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by-order basis. Notwithstanding the above, with respect to Complex Orders a Phlx member's routing system would not be required to enable the electronic routing of orders to all of the U.S. options exchanges or provide current consolidated market data from the U.S. options exchanges. Any Phlx member would be permitted to avail itself of this arrangement, provided that its order routing functionality incorporates the features described above and satisfies Phlx that it appears to be robust and reliable. The member remains solely responsible for implementing and operating its system. See Options 7, Section 6, Part E.

6 The term "Firm" applies to any transaction that is identified by a member or member organization for clearing in the Firm range at OCC. See Options 7, Section 1.

7 The Firm Floor Option Transaction Charges and QCC Transaction Fees are set forth in Options 7, Section 4. QCC Transaction Fees apply to both electronic and floor QCC orders.

8 Eligible Contracts include the following: Firm, Broker-Dealer, Joint Back Office or "JBO" or Professional equity option orders that are electronically delivered and executed. Eligible Contracts do not include floor-based orders, qualified contingent cross or "QCC" orders, price improvement or "PIXL" orders, Mini Option orders or Singly Listed Orders. Options overlying NDX and NDXP are not considered Eligible Contracts. See Options 7, Section 6, Part E.

volume to the Exchange, particularly electronic Firm, Broker-Dealer,[9] JBO[10] and Professional[11] order flow.

As set forth in Options 7, Section 1, Part B, the Exchange presently offers a Customer Rebate Program that is designed to attract electronic Customer order flow to the Exchange. In particular, the program consists of the following five tiers that pay Customer rebates on four Categories, A,[12] B,[13] C,[14] D,[15] of transactions:[16]

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9 The term "Broker-Dealer" applies to any transaction which is not subject to any of the other transaction fees applicable within a particular category.

10 The term "Joint Back Office" or "JBO" applies to any transaction that is identified by a member or member organization for clearing in the Firm range at OCC and is identified with an origin code as a JBO. A JBO will be priced the same as a Broker-Dealer. A JBO participant is a member, member organization or non-member organization that maintains a JBO arrangement with a clearing broker-dealer ("JBO Broker") subject to the requirements of Regulation T Section 220.7 of the Federal Reserve System as further discussed at Exchange Rule 703.

11 The term "Professional" applies to transactions for the accounts of Professionals, as defined in Exchange Rule 1000(b)(14) means any person or entity that (i) is not a broker or dealer in securities, and (ii) places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s).

12 The Category A Rebate is paid to members executing electronically-delivered Customer Simple Orders in Penny Pilot Options and Customer Simple Orders in Non-Penny Pilot Options in Options 7, Section 4 symbols.

13 The Category B Rebate is paid on Customer PIXL Orders in Options 7, Section 4 symbols that execute against non-Initiating Order interest. In the instance where member qualify for Tier 4 or higher in the Customer Rebate Program, Customer PIXL Orders that execute against a PIXL Initiating Order are paid a rebate of $0.14 per contract. Rebates on Customer PIXL Orders are capped at 4,000 contracts per order for Simple PIXL Orders.

14 The Category C Rebate is paid to members executing electronically-delivered Customer Complex Orders in Penny Pilot Options in Options 7, Section 4 symbols. Rebates are paid on Customer PIXL Complex Orders in Options 7, Section 4 symbols that execute against non-Initiating Order interest. Customer Complex PIXL Orders that execute against a Complex PIXL Initiating Order are not paid a rebate under any circumstances. The Category C Rebate is not paid when an electronically-delivered Customer Complex Order, including Customer Complex PIXL Order, executes against another electronically-delivered Customer Complex Order.

Customer Rebate Tiers	Percentage Thresholds of National Customer Volume in Multiply-Listed Equity and ETF Options Classes, excluding SPY Options (Monthly)	Category A	Category B	Category C	Category D
Tier 1	0.00% - 0.60%	$0.00	$0.00	$0.00	$0.00
Tier 2	Above 0.60% - 1.10%	$0.10	$0.10	$0.16	$0.21
Tier 3	Above 1.10% - 1.60%	$0.15	$0.12	$0.18	$0.22
Tier 4	Above 1.60% - 2.50%	$0.20	$0.16	$0.22	$0.26
Tier 5	Above 2.50%	$0.21	$0.17	$0.22	$0.27

A Phlx member qualifies for a particular Customer Rebate Tier based on the percentage of total national Customer volume in multiply-listed options that it transacts monthly on the Exchange. Specifically, the Exchange totals Customer volume in multiply listed options (including SPY) that is electronically-delivered and executed, except volume associated with electronic QCC Orders, as defined in Exchange Rule 1080(o), and calculates this as a percentage of total national customer volume in multiply-listed equity and ETF options classes, excluding SPY. Members under Common Ownership[17] may aggregate their Customer volume for purposes

15 The Category D Rebate is paid to members executing electronically-delivered Customer Complex Orders in Non-Penny Pilot Options in Options 7, Section 4 symbols. Rebates are paid on Customer PIXL Complex Orders in Options 7, Section 4 symbols that execute against non-Initiating Order interest. Customer Complex PIXL Orders that execute against a Complex PIXL Initiating Order are not paid a rebate under any circumstances. The Category D Rebate is not paid when an electronically-delivered Customer Complex Order, including Customer Complex PIXL Order, executes against another electronically-delivered Customer Complex Order.

16 Rebates are not paid on NDX or NDXP contracts in any Category; however, NDX and NDXP contracts count toward the volume requirement to qualify for a Customer Rebate Tier.

17 The term "Common Ownership" shall mean members or member organizations under 75% common ownership or control. See Options 7, Section 1.

of calculating the Customer Rebate Tiers and receiving rebates. Affiliated Entities[18] may aggregate their Customer volume for purposes of calculating the Customer Rebate Tiers and receiving rebates.

Proposal

The Exchange now proposes to adopt an alternative method for members to qualify for the applicable Tier 2 rebates described above. As discussed above, the proposed alternative will be based on the member meeting a certain percentage threshold of total national Customer volume in multiply-listed options classes, reaching the Monthly Firm Fee Cap, and meeting the MARS System Eligibility requirements. Specifically, the Exchange proposes to add the following language at the end of Options 7, Section 1, Part B: "The Exchange will pay the applicable Tier 2 rebates to qualifying members or member organizations, qualifying affiliates under Common Ownership, or qualifying Affiliated Entities, provided they: (1) execute a Percentage Threshold of National Customer Volume in Multiply-Listed Equity and ETF Options Classes, excluding SPY Options (monthly), of above 0.25%; (2) reach the Monthly Firm Fee Cap as defined in Options 7, Section 4; and (3) meet the MARS System Eligibility requirements as provided in Options 7, Section 6, Part E."

Applicability to and Impact on Participants

The proposed change is designed to incentivize members who reach the Monthly Firm Fee Cap and have MARS System Eligibility to increase their electronic Customer volume to qualify for the applicable Tier 2 rebates. The proposal may correspondingly encourage members

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18 The term "Affiliated Entity" is a relationship between an Appointed MM and an Appointed OFP for purposes of qualifying for certain pricing specified in the Pricing Schedule. Members under Common Ownership may not qualify as a counterparty comprising an Affiliated Entity. Each member may qualify for only one (1) Affiliated Entity relationship at any given time. See Options 7, Section 1.

to qualify for the Monthly Firm Fee Cap and the MARS System Eligibility requirements (which should increase Firm floor volume and Firm QCC volume as well as electronic Firm, Broker-Dealer, JBO and Professional volume). The Exchange notes that all market participants stand to benefit from increased volume, which facilitates tighter spreads and enhances price discovery, and may lead to a corresponding increase in order flow from other market participants.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,[19] in general, and furthers the objectives of Sections 6(b)(4) and 6(b)(5) of the Act,[20] in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Proposal is Reasonable

The Exchange believes that the proposed alternative method to qualify for the applicable Tier 2 rebates in the Customer Rebate Program is reasonable for several reasons. As a threshold matter, the Exchange is subject to significant competitive forces in the market for options transaction services that constrain its pricing determinations in that market. The fact that this market is competitive has long been recognized by the courts. In NetCoalition v. Securities and Exchange Commission, the D.C. Circuit stated as follows: "[n]o one disputes that competition for order flow is 'fierce.' … As the SEC explained, '[i]n the U.S. national market system, buyers and sellers of securities, and the broker-dealers that act as their order-routing agents, have a wide range of choices of where to route orders for execution'; [and] 'no exchange can afford to take

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19 15 U.S.C. 78f(b).

20 15 U.S.C. 78f(b)(4) and (5).

its market share percentages for granted' because 'no exchange possesses a monopoly, regulatory or otherwise, in the execution of order flow from broker dealers'…."[21]

Numerous indicia demonstrate the competitive nature of this market. For example, clear substitutes to the Exchange exist in the market for options transaction services. The Exchange is only one of sixteen options exchanges to which market participants may direct their order flow. Competing options exchanges offer similar tiered pricing structures to that of the Exchange, including tiered rebates that apply based upon members achieving certain volume thresholds.[22] Within this environment, market participants can freely and often do shift their order flow among the Exchange and competing venues in response to changes in their respective pricing schedules.

Within the foregoing context, the proposal represents a reasonable attempt by the Exchange to increase its liquidity and market share relative to its competitors. The Exchange's proposal is designed to attract additional liquidity and order flow to the Exchange, similar to other exchange programs with competitive pricing programs,[23] thereby promoting market depth, price discovery and improvement, and enhancing order execution opportunities for market participants. As discussed above, the proposed changes provide an additional opportunity for

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21 NetCoalition v. SEC, 615 F.3d 525, 539 (D.C. Cir. 2010) (quoting Securities Exchange Act Release No. 59039 (December 2, 2008), 73 FR 74770, 74782-83 (December 9, 2008) (SR-NYSEArca-2006-21)).

22 See, e.g., NYSE American Options Fee Schedule, Section I.E (setting forth the American Customer Engagement ("ACE") Program that provides tiered customer credits on customer electronic volume, provided the member achieves certain total industry customer equity and ETF option average daily volume percentage thresholds), Section I.H (setting forth the Professional Step-Up Incentive that provides discounted rates or credits, as applicable, to professional customer, broker-dealer, non-NYSE American Options market maker, and firm ranges, and also ties some of these benefits to the ACE Program), and Section I.I (setting forth the Firm Monthly Fee Cap that caps at $100,000 per month the fees associated with Firm Manual transactions, and also lowers the firm fee cap for members that achieve the applicable ACE Program tiers).

23 Id.

members to earn the applicable Tier 2 Customer rebates if they execute a percentage threshold of national Customer volume in multiply-listed equity and ETF options classes, excluding SPY options, of above 0.25% on the Exchange, reach the Monthly Firm Fee Cap, and have MARS System Eligibility. Today, the Exchange provides the same Tier 2 rebates to members that execute a percentage threshold of national Customer volume in multiply-listed equity and ETF options classes, excluding SPY options, of above 0.60% to 1.10% on the Exchange. This proposal would offer members an alternative route to earn the same Tier 2 rebates, provided they meet the lower percentage threshold of above 0.25% and also qualify for both the Monthly Firm Fee Cap and the MARS System Eligibility requirements. The Exchange believes that the proposed percentage threshold is set at an appropriate level that would encourage members to bring more Customer order flow to the Exchange to qualify for the applicable Tier 2 rebates. While the Exchange cannot predict with certainty whether any members would avail themselves of the proposed incentive given that this incentive is new, assuming historical behavior can be predictive of future behavior, the Exchange believes that at present participation rates, almost 30% of active firms on the Exchange have comparable trading volume in the Customer category. The Exchange also believes that the proposed lower percentage threshold (i.e., above 0.25% versus the current Tier 2 threshold of above 0.60% to 1.10%) is reasonable because members must meet additional qualifications (i.e., reach the Monthly Firm Fee Cap and have MARS System Eligibility) under the proposed alternative method to receive the Tier 2 rebates on Customer transactions.

Furthermore, the Exchange believes that its proposal will encourage members to increase the amount of Customer order flow directed to the Exchange. In addition, because members will also be required to reach the Monthly Firm Fee Cap and have MARS System Eligibility to receive the applicable Tier 2 Customer rebates, the proposed program may encourage members to direct Firm floor and QCC order flow as well as electronic Firm, Broker-Dealer, JBO and Professional order flow, in addition to electronic Customer order flow. The Exchange notes that all market participants stand to benefit from increased order flow – whether Customer, Firm, Broker-Dealer, JBO or Professional, and whether floor or electronic – as such increase promotes market depth, facilitates tighter spreads, enhances price discovery, and may lead to an increase in order flow from other market participants that would not otherwise qualify for the proposed alternative route to the Tier 2 Customer rebates.

The Proposal is an Equitable Allocation of Rebates

The Exchange believes that its proposal is an equitable allocation of the applicable Tier 2 rebates. The proposal is based on the amount and type of business transacted on the Exchange, and members can opt to avail themselves of these rebates or not. Furthermore, this proposal is designed to encourage members to bring and execute their order flow (particularly electronic Customer volume and, in turn, Firm floor, QCC, and electronic Firm, Broker-Dealer, JBO and Professional volume) to the Exchange. To the extent at the proposed changes attract such additional volume to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for, among other things, order execution. Thus, the Exchange believes the proposed changes would improve market quality for all market participants on the Exchange, and increase its attractiveness to existing and prospective members.

The Proposal is not Unfairly Discriminatory

The Exchange believes that its proposal is not unfairly discriminatory. As an initial matter, the Exchange believes that nothing about its volume-based tiered pricing model is inherently unfair; instead, it is a rational pricing model that is well-established and ubiquitous in today's economy among firms in various industries – from co-branded credit cards to grocery stores to cellular telephone data plans – that use it to reward the loyalty of their best customers that provide high levels of business activity and incent other customers to increase the extent of their business activity. It is also a pricing model that the Exchange and its competitors have long employed with the assent of the Commission. It is fair because it incentivizes customer activity that increases liquidity, enhances price discovery, and improves the overall quality of the options market.

As discussed above, the proposal is based on the amount and type of business transacted on the Exchange, and members are not obligated to try to achieve the proposed alternative route to the Tier 2 Customer rebates. Rather, the proposal is designed to encourage these members to bring additional order flow (particularly electronic Customer volume and, in turn, Firm floor, QCC, and electronic Firm, Broker-Dealer, JBO and Professional volume) to the Phlx market, improving market quality and price discovery. The Exchange believes that the proposed qualification for the Tier 2 Customer rebates is not unfairly discriminatory because to the extent the proposed changes attract more volume to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for order execution, among other things. As noted above, all market participants stand to benefit from increased order flow – whether Customer, Firm, Broker-Dealer, JBO or Professional, and whether floor or electronic – as such increase promotes market depth, facilitates tighter spreads, enhances price discovery, and may lead to an increase in order flow from other market participants that would not otherwise qualify for the proposed alternative route to the Tier 2 Customer rebates. Thus, the Exchange believes the proposed changes will help to improve market quality and the attractiveness of the Exchange's options market to all existing and prospective members.

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.

Intramarket Competition

The proposed amendments to the Exchange's Customer Rebate Program described above do not impose an undue burden on intra-market competition. By fortifying participation in this program, the proposed changes are designed to attract additional order flow (particularly electronic Customer volume and, in turn, Firm floor, QCC, and electronic Firm, Broker-Dealer, JBO and Professional volume) to the Exchange. The Exchange believes that its proposal would incentivize market participants to direct additional volume to the Exchange. As noted above, all market participants stand to benefit from increased order flow as such increase promotes market depth, facilitates tighter spreads, enhances price discovery, and may attract additional liquidity and volume to the Exchange. For these reasons, the Exchange does not believe that its proposal will place any category of Exchange market participant at a competitive disadvantage.

Inter-market Competition

The Exchange operates in a highly competitive market in which market participants can readily favor one of 16 competing options exchanges if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. In such an environment, the Exchange must continually adjust its fees and rebates to remain competitive with other exchanges and to attract order flow to the Exchange. Because competitors are free to modify their own fees and rebates in response, the Exchange believes that the degree to which pricing changes in this market may impose any burden on competition is extremely limited.

Moreover, as noted above, price competition between exchanges is fierce, with liquidity and market share moving freely between exchanges in reaction to fee and rebate changes. In sum, if the changes proposed herein are unattractive to market participants, it is likely that the Exchange will lose market share as a result. Accordingly, the Exchange does not believe that the proposed changes will impair the ability of members or competing order execution venues to maintain their competitive standing in the financial markets.

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act.[24]

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

[24] 15 U.S.C. 78s(b)(3)(A)(ii).

- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-Phlx-2019-48 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-2019-48. 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-2019-48 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.[25]

Jill M. Peterson
Assistant Secretary

[25] 17 CFR 200.30-3(a)(12).

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