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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-89768; File No. SR-CBOE-2020-060]

Self-Regulatory Organizations; Cboe Exchange, Inc.; Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, to Permanently Adopt the Related Futures Cross Order Type

September 4, 2020.

I. Introduction

On July 1, 2020, Cboe Exchange, Inc. (the "Exchange" or "Cboe Options") 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 permanently adopt the Related Futures Cross ("RFC") order type. The proposed rule change was published for comment in the Federal Register on July 21, 2020.[3] On August 13, 2020, the Exchange filed Amendment No. 1 to the proposed rule change.[4] The Commission received one comment on the proposed rule change.[5] This order approves the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 89325 (July 15, 2020), 85 FR 44125.

4 Amendment No. 1 is publicly available on the Commission's website at: https://www.sec.gov/comments/sr-cboe-2020-060/srcboe2020060-7640381-222308.pdf.

5 See Letter from Joyana Pilquist, CFA, dated August 24, 2020. The Commission believes this comment, which relates to FLEX options, is outside the scope of this proposed rule change as CBOE is not proposing to change the substantive terms of FLEX options transactions. Accordingly, the Commission does not believe this comment can be

II. Summary of the Proposal, as Modified by Amendment No. 1

From March 16 to June 12, 2020, the Exchange closed its trading floor in response to the coronavirus pandemic. As a result, the Exchange operated in an all-electronic configuration. Because the trading floor was closed during this time, floor brokers could not execute crosses of option combos (i.e., synthetic futures) on the trading floor on behalf of market participants who were exchanging futures contracts in either VIX or SPX for related options positions in order to swap related exposures,[6] and there was no means to electronically pair and execute the options legs of these transactions on the Exchange.

To enable Trading Permit Holders ("TPHs") to execute the options part of these transactions when the floor was closed, the Exchange adopted the electronic RFC order type under Rule 5.24(e)(1)(D).[7] RFCs under Rule 5.24(e)(1)(D) were automatically executed without exposure to

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appropriately addressed through this proposal.

6 In the Notice, the Exchange provides the following example of such a transaction: If a market participant has positions in VIX options but would prefer to hold a corresponding position in VIX futures (such as, for example, to reduce margin or risk related to the option positions), that market participant may swap its VIX options positions with another market participant(s)'s VIX futures positions that have corresponding risk exposure. See Notice, supra note 3, at 44125. The Exchange explains that the transaction between the market participants for the futures positions occurs in accordance with the rules of the applicable designated contract market that lists the futures. See id., n.3 (citing Cboe Futures Exchange LLC Rule 414). The Exchange further explains that these are riskless transactions that carry no profit or loss for the market participants that are party to the transactions, but rather are intended to provide a seamless method for market participants to reduce margin and capital requirements while maintaining the same risk exposure within their portfolios. See Notice, supra note 3, at 44125.

7 See Securities Exchange Act Release No. 88447 (March 20, 2020), 85 FR 17129 (March 26, 2020) (CBOE-2020-023).

open outcry due to the all-electronic environment at the time.[8] These RFCs were also required to execute in accordance with the same priority principles that apply to all complex orders on CBOE.[9] Specifically: (i) each option leg must have executed at a price that complies with Rule 5.33(f)(2), provided that no option leg executes at the same price as a Priority Customer Order in the Simple Book; (ii) each option leg must have executed at a price at or between the national best bid or offer (''NBBO'') for the applicable series; and (iii) the execution price must have been better than the price of any complex order resting in the complex order book, unless the RFC Order was a Priority Customer Order and the resting complex order is a non-Priority Customer Order, in which case the execution price may be the same as or better than the price of the resting complex order.[10] If an RFC could not have executed in accordance with these requirements, the CBOE System would have cancelled the order.[11] When the CBOE trading floor reopened on June 15, 2020, RFC Orders were no longer available,[12] though, the RFC rule text in Rule 5.24(e)(1)(D) remains in the CBOE rulebook. Accordingly, under CBOE's current rules with an operable trading floor, TPHs no longer have the option to submit electronic RFC Orders for automatic execution.

In this proposal, the Exchange seeks to adopt electronic RFC Orders on a permanent basis.[13] The Exchange explains that the need to reduce risk is prevalent in VIX and SPX, particularly when the markets are volatile, and that customers often have corresponding futures

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8 See id., at 17131.

9 See id., at 17131.

10 See id., at 17131.

11 See id., at 17131.

12 See Notice, supra note 3, at 44126.

13 See Notice, supra note 3, at 44126-27 for a more detailed description of the proposal.

that could make these transactions possible.[14] The Exchange further explains that it is necessary for both the option and future legs of the transactions that would be subject to RFC to occur between the same market participants in order to successfully swap the related exposures; while in-crowd market participants have the opportunity to bid or offer to participate on the trade on the floor (i.e., to break up the options cross between the two parties), the Exchange represents that other TPHs on the floor generally declined on a voluntary basis to do so upon hearing that the cross was part of an exchange of related futures contracts.[15]

To facilitate this proposed rule change, the Exchange first proposes to delete Rule 5.24(e)(1)(D). Second, the Exchange proposes to add RFC Orders to its list of complex orders under Rule 5.33(b)(5). For purposes of electronic trading, RFC Orders would be identical to the current definition in Rule 5.24(e)(1)(D) and defined as an SPX or VIX complex order comprised of an option combo order coupled with a contra-side order or orders totaling an equal number of option combo orders. For purposes of open outcry trading, an RFC order is an SPX or VIX complex order comprised of an option combo that may execute against a contra-side RFC order or orders totaling an equal number of option combo orders. Furthermore, an RFC order must be identified to the Exchange as being part of an exchange of option contracts for related futures positions. Rule 5.33(m) would be adopted to add the same priority protection principles that were adopted under Rule 5.24(e)(1)(D),[16] and if an RFC Order under Rule 5.33 cannot be executed in accordance with these priority principles, it will be cancelled. Finally, the Exchange proposes to amend Rules 5.83 and 5.85 to permit RFC Orders to be handled by a floor broker for execution

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14 See Notice, supra note 3, at 44125.

15 See id. at 44125-26.

16 See supra note 10 and accompanying text; see also Notice, supra note 3, 44126.

on the floor without representation on the floor rather than submitted for automatic execution electronically.

III. Discussion and Commission Findings

After careful review and consideration, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange.[17] In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,[18] which requires, among other things, that the rules of a national securities exchange be 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, and that the rules of a national securities exchange not be designed to permit unfair discrimination between customers, issuers, brokers or dealers.

This proposal has two components. First, the Exchange seeks to make electronic RFC Orders permanent, even when the trading floor of the Exchange is operable. The electronic RFC order type is designed to allow market participants trading SPX and VIX options to more efficiently execute risk mitigating transactions on the Exchange, as explained above.[19] The Exchange represents that it received feedback from customers regarding the benefits of

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17 In approving this proposed rule change, as amended, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

18 15 U.S.C. 78f(b)(5).

19 See also Notice, supra note 3, at 44125-26, 44127-28.

electronic RFC Orders when its floor was closed – including the efficiency this order type provided with respect to the execution of these crosses – which is what prompted it to file this proposal.[20] Second, when the trading floor is operative, amended Rules 5.83 and 5.85 would permit RFC Orders to be handled by a floor broker for execution without representation on the trading floor as an alternative to automatic electronic execution.

In Amendment No. 1, the Exchange further reiterates that there is a mutual understanding among TPHs on the floor to not break up the options leg of transactions that would qualify for the proposed RFC order type due to the necessity of keeping the terms of the hedging transactions unchanged through execution. The Exchange asserts that this understanding among TPHs contributes to smoother operations on the trading floor. The Exchange further argues that while the electronic RFC order type would preclude the options component of these hedging transactions to be broken up going forward, the benefits of permitting RFC Orders to execute as clean crosses greatly outweigh any detriments, if there are even any, that may result from exposing these orders for potential break up. The Exchange believes that the benefits of requiring a broker to expose an order on the trading floor generally flow to that order, which include the potential of price improvement for the order and to locate liquidity against which to execute the order. In the case of orders that would qualify to use the RFC order type, the Exchange asserts that the representing broker has already located the necessary liquidity to execute the order, as that is necessary given the nature of these transactions.

Based on the foregoing, the Commission finds that the proposed rule change 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

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20 See Notice, supra note 3, at 44126.

investors and the public interest. In addition to the above assertions and representations by the Exchange, the Commission notes that the proposed electronic RFC order type contains the same priority protection principles that were adopted under Rule 5.24(e)(1)(D) when the Exchange permitted electronic RFC Orders as clean crosses due to the closure of its trading floor. Furthermore, Rule 5.33(m) provides that: (i) an RFC order may only be entered in the standard increment applicable to the class; (ii) the execution of an RFC order must happen contemporaneously with the execution of the related futures position portion of the exchange; and (iii) the transaction involving the related futures position of the exchange must comply with all applicable rules of the designated contract market on which the futures are listed for trading. With regard to the proposed changes to Rules 5.83 and 5.85, RFC Orders handled by floor brokers would be covered by the same protections.

For the above reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act.

IV. Solicitation of Comments on Amendment No. 1

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether Amendment No. 1 to the proposed rule change is consistent with the Exchange 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-CBOE-2020-060 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-CBOE-2020-060. 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 this filing will also 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-CBOE-2020-060 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1

The Commission finds good cause to approve the proposed rule change, as modified by Amendment No. 1, prior to the 30th day after the date of publication of notice of Amendment No. 1 in the Federal Register.

Amendment No.1 has two main aspects. First, in Amendment No. 1, the Exchange makes certain technical edits to the Exhibit 5 that was initially filed.[21] Second, as stated above, the Exchange expands its statutory basis analysis in Amendment No.1 to provide additional arguments and representations to support its position that allowing RFC Orders to execute automatically without exposure is consistent with the Act. Furthermore, the Exchange also expands the analysis in its request that this filing be approved on an accelerated basis, and it adds an analysis to Item 8 of the filing to assert that the proposed CBOE RFC order type is "virtually identical" to a recently approved RFC order type on Miami International Securities Exchange, LLC.[22]

Amendment No. 1 does not change any substantive provisions of the proposed rule change that were noticed for public comment. It contains only minor, technical revisions to the proposed rule text, and it provides additional justification that the proposal is consistent with the Act. Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,[23] to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

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[21] Specifically, Amendment No. 1: deletes the closing bracket and period from the end of Rule 5.24(e)(1)(C); deletes the opening bracket before Rule 5.24(e)(1)(D); inserts a closing bracket before the semi-colon at the end of Rule 5.24(e)(1)(D)(7), and deletes the closing bracket following the "and" at the end of Rule 5.24(e)(1)(D)(7); proposes to change current Rule 5.24(e)(1)(E) to Rule 5.24(e)(1)(D), and includes the introductory paragraph (with no other proposed changes) of that subparagraph in the Exhibit; and adds the current definition of a "Post Only" order in Rule 5.33(b) (with no proposed changes) to demonstrate where in that paragraph the proposed definition of an RFC order will be located.

[22] See Securities Exchange Act Release No. 89213 (July 1, 2020), 85 FR 41077 (July 8, 2020) (MIAX-2020-11).

[23] 15 U.S.C. 78s(b)(2).

VI. Conclusion

IT IS THEREFORE ORDERED that, pursuant to Section 19(b)(2) of the Act,[24] the proposed rule change, as modified by Amendment No. 1, (SR-CBOE-2020-060) be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[25]

J. Matthew DeLesDernier,

Assistant Secretary

[FR Doc. 2020-20023 Filed: 9/9/2020 8:45 am; Publication Date: 9/10/2020]

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24 15 U.S.C. 78s(b)(2).

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