For the Nuclear Regulatory Commission.

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## SECURITIES AND EXCHANGE COMMISSION

**[Release No. 34–79244; File No. SR–CBOE–2016–053]**

## Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, Relating to Price Protection Mechanisms and Risk Controls

November 4, 2016.

### I. Introduction

On September 1, 2016, Chicago Board Options Exchange, Incorporated (''CBOE'' or ''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 current and adopt new price protection mechanisms and risk controls for orders and quotes. The Commission published the proposed rule change for comment in the **Federal Register** on September 20, 2016.[3] On September 21, 2016, the Exchange filed Amendment No. 1 to the proposed rule change.[4] The Commission received no comments on the proposal. This order provides notice of filing of Amendment No. 1 and approves the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

### II. Description of the Proposed Rule Change [5]

The Exchange currently has in place various price check mechanisms and risk controls that are designed to prevent incoming orders and quotes from automatically executing at potentially erroneous prices or to assist TPHs with managing their risk.[6] The Exchange proposed to amend CBOE Rules 6.12(a)(3), 6.13(b)(v), 6.14 and 8.18 to add new, as well as amend current, price protection mechanisms and risk controls to further assist brokers in their efforts to prevent errors and avoid trading activity that could potentially be unwanted or even disruptive to the market.[7]

*A. Limit Order Price Parameter for Simple Orders*

The Exchange proposed to amend the limit order price parameter for simple orders in Rule 6.12(a)(3). Currently, a simple limit order is routed directly from an order entry firm to an order management terminal (''OMT'') designated by the order entry firm if a limit order to buy (sell) is more than an acceptable tick distance (''ATD'') [8] above (below): (i) The Exchange's previous day's closing price prior to the opening of a series, or (ii) the disseminated Exchange offer (bid) once a series has opened.[9]

The Exchange has now proposed to amend CBOE Rule 6.12(a)(3) to reject a simple limit order to buy (sell) generally when it is more than an ATD above (below) the last disseminated national best offer (''NBO'') (national best bid (''NBB'')).[10] According to the Exchange, using the NBBO or NBO (NBB), if available, will more accurately reflect the then current market, rather than the previous day's closing price or Exchange BBO.[11] The Exchange, however, will continue to use the previous day's closing price or Exchange BBO in certain instances, such as when the NBBO is locked or crossed, or when there is no NBO (NBB) and the closing price does not cross the disseminated NBB (NBO).[12]

CBOE also proposed to apply the limit order price parameter to immediate-or-cancel orders. According to the Exchange, such orders also are at risk of execution at extreme and potentially erroneous prices and thus will benefit from applicability of these checks.[13] However, the limit order price parameter will not apply to orders routed from a PAR workstation or OMT. According to the Exchange, orders routed from a PAR workstation or OMT are subject to manual handling, and therefore, the Exchange believes the PAR or OMT operator will have evaluated the price of an order based on then-existing market conditions prior to submitting the order for electronic execution.[14] Thus, there is minimal risk of execution at an erroneous price. The limit order price parameter also will not apply to orders with a stop contingency.[15] According to the Exchange, buy orders with a stop contingency are generally submitted at a triggering price that is above the NBO, and sell orders with a stop contingency are generally submitted at a triggering price that is below the NBB.[16] As a result, the Exchange believes these orders are expected to be priced outside the NBBO.[17]

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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. 78839 (September 14, 2016), 81 FR 64521 (September 20, 2016) (''Notice'').

[4] In Amendment No. 1, the Exchange conformed the text of proposed Rule 6.13(b)(v)(B) to CBOE's description in the Notice of the drill through price check parameter. Specifically, the amendment added detail into the rule to reflect that, pursuant to the drill through price check parameter, CBOE will expose the unexecuted portion of an order via HAL at the better of the NBBO and the drill through price. In addition, CBOE also proposed to amend its discussion of existing quote risk monitor functionality to accurately match the existing rule text (which involved background discussion of functionality that CBOE did not propose to amend in the current proposal). To promote transparency of its proposed amendment, when CBOE filed Amendment No. 1 with the Commission, it also submitted Amendment No. 1 as a comment letter to the file, which the Commission posted on its Web site and placed in the public comment file for SR–CBOE–2016–053 (available at *https://www.sec.gov/comments/sr-cboe-2016-053/cboe2016053-1.pdf*). The Exchange also posted a copy of its Amendment No. 1 on its Web site (*http://www.cboe.com/aboutcboe/legal/submittedsecfilings.aspx*) when it filed the amendment with the Commission.

[5] A more detailed description of the proposed rule change appears in the Notice. *See supra* note 3.

[6] *See, e.g.,* CBOE Rules 6.12(a)(3) through (5) (limit order price parameters), 6.13(b)(v) (market-width and drill through price check parameters), 6.14 (price protections), 6.53C, Interpretation and Policy .08 (price check parameters for complex orders), and 8.18 (QRM Mechanism).

[7] The proposed rule change also made conforming changes to CBOE Rules 6.2B, 6.13A, and 6.14A. A full discussion of those changes may be found in the Notice. *See supra* note 3.

[8] Currently, the Exchange determines the ATD, which may be no less than 5 minimum increment ticks, on a series-by-series and premium basis. Under the proposed rule change, the ATD, which may be no less than two minimum increment ticks, will be determined on a class-by-class and premium basis. In addition, different ATDs may be applied to orders entered during the pre-opening, a trading rotation, a trading halt, or Extended Trading Hours. *See* proposed CBOE Rule 6.12(a)(3) and Notice, *supra* note 3, at 64523 n. 8

[9] *See* CBOE Rule 6.12(a)(3).

[10] Specifically, CBOE will reject the order if it is more than the ATD above (below): (i) prior to the opening of a series, (A) the last disseminated national best offer (''NBO'') (national best bid (''NBB'')), if a series is open on another exchange, or (B) the Exchange's previous day's closing price, if a series is not yet open on any other exchange; if the NBBO is locked, crossed, or unavailable; or if there is no NBO (NBB) and the previous day's closing price is greater (less) than or equal to the NBB (NBO); (ii) intraday, the last disseminated NBO (NBB), or the Exchange's best offer (bid) if the NBBO is locked, crossed or unavailable; or (iii) during a trading halt, the last disseminated NBO (NBB).

[11] *See* Notice, *supra* note 3 at 64522.

[12] *See id.*

[13] *See id.* at 64523.

[14] *See id.*

[15] *See* CBOE Rule 6.53. A stop contingency is triggered for a buy order if there is a last sale or bid at or above the stop price and for a sell order if there is a last sale or offer at or below the stop price.

[16] *See* Notice, *supra* note 3 at 64523.

[17] *See id.*

*B. Drill Through Price Check Parameter*

The Exchange proposed to amend the drill through price check parameter in CBOE Rule 6.13(b)(v). Currently, the Exchange's trading system (''System'') will not automatically execute a market or marketable limit order[18] if the execution would follow an initial partial execution on the Exchange at a price not within an ATD[19] from the initial execution. Instead, the remaining unexecuted portion of a HAL-eligible order will be exposed pursuant to the HAL process in CBOE Rule 6.14A using the ATD as the exposure price and any remainder will route via the order handling system pursuant to CBOE Rule 6.12.[20]

The Exchange now has proposed to amend CBOE Rule 6.13(b)(v) to add detail to the rule describing how the System will handle orders that were not exposed prior to trading up to the drill through price and orders that traded up to the drill through price following exposure. In particular, orders not previously exposed would be exposed via HAL and orders previously exposed via HAL or SAL would rest in the book for a period of time and thereafter be cancelled if they do not execute.[21]

Buy (sell) orders (or any unexecuted portion) that are not eligible for HAL or SAL and do not otherwise cancel by their terms will route via the order handling system pursuant to Rule 6.12. In addition, the drill through price check parameter at the open will be handled pursuant to the separate process set forth in Rule 6.2B, Interpretation and Policy .03.[22]

*C. TPH-Designated Risk Settings*

The Exchange proposed to amend CBOE Rule 6.14 to authorize it to share TPH-designated risk settings with a TPH's Clearing TPH. The risk settings that the Exchange may share with Clearing TPHs include, but are not limited to, settings under Rule 8.18 (related to QRM) and proposed CBOE Rule 6.14(d) (related to order entry and execution rate checks) and (e) (related to maximum contract size). The Exchange represented that other options exchanges have similar rules permitting them to share member-designated risk settings with other members that clear transactions on the member's behalf.[23]

*D. Put Strike Price/Call Underlying Value Checks*

The Exchange proposed to amend the put strike price and call underlying value checks in CBOE Rule 6.14(a). Currently, the System rejects back to the TPH a quote or buy limit order for (i) a put if the price of the quote bid or order is greater than or equal to the strike price of the option, or (ii) a call if the price of the quote bid or order is greater than or equal to the consolidated last sale price of the underlying security, with respect to equity and exchange-traded fund options, or the last disseminated value of the underlying index, with respect to index options. The Exchange proposed to extend this check to apply to market orders (and any remaining size after a partial execution).[24]

*E. Quote Inverting NBBO Check*

The Exchange proposed to amend Rule CBOE 6.14(b) regarding the quote inverting NBBO check. Currently, if the Exchange is at the NBO (NBB), the System rejects a quote back to a Market-Maker if the quote bid (offer) crosses the NBO (NBB) by more than a number of ticks specified by the Exchange. If CBOE is not at the NBO (NBB), the System rejects a quote back to a Market-Maker if the quote bid (offer) locks or crosses the NBO (NBB). If the NBBO is unavailable, locked, or crossed, then this check compares the quote to the BBO (if available). The rule is currently silent on what happens if the BBO is unavailable.

The Exchange has now proposed to amend Rule 6.14(b) to not apply this check to incoming quotes when the BBO is unavailable. The Exchange also proposed to amend the rule to state that it will not apply the check to incoming quotes prior to the opening of a series if the series is not open on another exchange, as well as during a trading halt.[25]

*F. Execution of Quotes That Lock or Cross NBBO*

The Exchange further proposed to amend the provision concerning the execution of quotes that lock or cross the NBBO.[26] The rule currently states that if the System accepts a quote that locks or crosses the NBBO, it executes the quote and either (i) cancels any remainder or (ii) books any remainder if the price of the quote does not lock or cross the price of an away exchange.[27] Further, CBOE currently will not disseminate an internally crossed market, and if a Market-Maker submits a quote that would invert an existing quote, the System will change the

[18] Currently, the Exchange applies the market-width check to market orders and the drill through check to market and marketable limit orders. The Exchange proposed to codify this current practice into the rules. *See* Notice, *supra* note 3, at 64523 n. 12.

[19] Currently, the ATD is determined by the Exchange on a series-by-series and premium basis for market orders and/or marketable limit orders and may be no less than two minimum increment ticks. Under the proposed rule change, the Exchange will determine the ATD on a class and premium basis (which may be no less than two minimum increment ticks), which the Exchange will announce via Regulatory Circular. *See* proposed CBOE Rule 6.13(b)(v)(B)(I).

[20] *See* CBOE Rule 6.13(b)(v).

[21] Specifically, if a buy (sell) order not yet exposed via HAL partially executes, and the System determines the unexecuted portion would execute at a price higher (lower) than the price that is an ATD above (below) the NBO (NBB) (''drill through price''), the System will not automatically execute the remaining portion but will instead expose it via HAL at the better of the NBBO and the drill through price (if eligible for HAL). If a buy (sell) order exposed via HAL (other than pursuant to the previous sentence) or the Solicitation Auction Mechanism (''SAL'') would, following the exposure period, execute at a price higher (lower) than the drill through price, the System will not automatically execute the order (or unexecuted portion). These orders (or unexecuted portions) will rest in the book (based on the time at which they enter the book for priority purposes) for a time period in milliseconds (which the Exchange will determine and announce via Regulatory Circular and will not exceed three seconds—the Exchange will initially set the time at two seconds) with a price equal to the drill through price. If the order (or any unexecuted portion) does not execute during that time period, the System cancels it. In classes in which SAL is activated, an order eligible for SAL will be exposed immediately and would not partially execute prior to being exposed via SAL. For this reason, SAL is not included in proposed CBOE Rule 6.13(v)(B)(I). *See* Notice, *supra* note 3, at 64523 n. 15. Any order (or unexecuted portion) that by its terms cancels if it does not execute immediately (including immediate-or-cancel, fill-or-kill, intermarket sweep, and market-maker trade prevention orders) will be cancelled rather than rest in the book for this time period in accordance with the definition of those order types. *See* proposed CBOE Rule 6.13(b)(v)(B)(III).

[22] The proposed rule change also amended the market width price check parameter in CBOE Rule 6.13(b)(v) (proposed CBOE Rule 6.13(b)(v)(A)) to be determined on a class-by-class basis rather than series-by-series, as well as made additional non-substantive changes to Rule 6.13(b)(v), such as separating the provisions regarding the market-width price check parameter from those regarding the drill through price check parameter.

[23] *See* Notice, *supra* note 3 at 64525. *See also, e.g.,* Miami International Securities Exchange, LLC (''MIAX'') Rule 500; NASDAQ OMX BX, Inc. (''BX'') Chapter VI, Section 20; NYSE Arca, Inc. (''Arca'') Rule 6.2A(a); NYSE MKT LLC (''MKT'') Rule 902.1NY(a); and NASDAQ OMX PHLX LLC (''PHLX'') Rule 1016.

[24] The Exchange will not apply these checks to market orders that execute during the opening process, however, in order to avoid impacting the determination of the opening price. According to the Exchange, separate price protections apply during the opening process, including the drill through protection in CBOE Rule 6.2B. *See* Notice, *supra* note 3, at 64525. The Exchange also proposed to amend CBOE Rule 6.14(a) to eliminate discretion afforded to the Exchange to determine to apply the call check to a class during Extended Trading Hours. The Exchange represented that it currently does not apply the check during Extended Trading Hours and is eliminating its ability to do so in the future. *See id.*

[25] *See* proposed CBOE Rule 6.14(ii) and (iii).

[26] The Exchange proposed to move this provision from current CBOE Rule 6.14(b)(iii) to proposed CBOE Rule 6.14(c).

[27] If a quote inverts another quote, it is subject to CBOE Rules 6.45A(d)(ii) or 6.45B(d)(ii).

incoming quote so it locks the existing quote.[28] The Exchange then disseminates the locked market, and both quotes will be deemed firm. When the market locks, a counting period will begin during which Market-Makers may update those quotes (provided a Market-Maker will be obligated to execute orders eligible for automatic execution at its disseminated quote). If at the end of the counting period the quotes remain locked, the locked quotes will automatically execute against each other.

Under current CBOE Rule 6.14(b)(iii), any counting period under the quote lock rule may cause the Exchange to disseminate a quote that locks that of an away exchange. The Exchange has now proposed to amend the rule to no longer disseminate a lock, and instead will reject an incoming Market-Maker quote (or unexecuted portion thereof) that locks or crosses a resting Market-Maker quote at the NBBO.[29]

### *G. Order Entry, Execution, and Price Parameter Checks*

The Exchange proposed to adopt the following four mandatory activity-based risk protections under proposed CBOE Rule 6.14(d):[30]

(i) the total number of orders (of all order types) and auction responses entered and accepted by the System (''orders entered'');

(ii) the total number of contracts (from orders and auction responses) executed on the System, which does not count executed contracts from orders submitted from a PAR workstation or an OMT or stock contracts executed as part of stock-option orders (''contracts executed'');

(iii) the total number of orders the System books or routes via the order handling system [31] pursuant to the drill through price check parameter (as amended by this proposed rule change) in proposed Rule 6.13(b)(v)(B) (''drill through events''); and

(iv) the total number of orders the System cancels or routes via the order handling system pursuant to the limit order price parameter in Rule 6.12(a)(3) through (5) (''price reasonability events'').

When a TPH exceeds a parameter within one of the time intervals set by CBOE, the System will (i) reject all subsequent incoming orders and quotes, (ii) cancel all resting quotes, and (iii) for the orders entered and contracts executed checks, if the TPH requests, cancel resting orders in the manner specified by the TPH (either all orders, orders with time-in-force of day, or orders entered on that trading day).[32]

The System will not accept new orders or quotes from a restricted acronym or login until the Exchange receives the TPH's manual notification to reactivate its ability to send orders and quotes. While an acronym or login is restricted, a TPH may continue to interact with any resting orders (*i.e.,* orders not cancelled pursuant to this protection) entered prior to its acronym or login becoming restricted, including receiving trade execution reports and canceling resting orders.

### *H. Maximum Contract Size*

The Exchange proposed to adopt a maximum contact size risk control pursuant to which the System will reject a TPH's incoming order or quote (including both sides of a two-sided quote) if its size exceeds the TPH's designated maximum contract size parameter.[33] Each TPH must provide a maximum contract size for each of simple orders, complex orders, and quotes applicable to an acronym or, if the TPH requests, a login.[34]

### **I. Kill Switch**

The Exchange further proposed to adopt a kill switch, which will be on optional tool allowing a TPH to send a message to the System to, or contact the Exchange Help Desk to request that, the Exchange cancel all its resting quotes, resting orders (either all orders, orders with time-in-force of day, or orders entered on that trading day), or both, and thereafter reject all subsequent incoming quotes and/or orders.[35] The System will send a TPH an automated message when it has processed a kill switch request and thereafter will not accept new orders or quotes from a restricted acronym or login until the Exchange receives the TPH's manual notification to reactivate its ability to send orders and quotes.

According to the Exchange, the kill switch message will be accepted by the System in the order of receipt in the queue and will be processed in that order so that interest already in the System will be processed prior to the kill switch message.[36] Moreover, a Market-Maker's utilization of the kill switch, and subsequent removal of its quotes, will not diminish or relieve the Market-Maker of its obligation to provide continuous two-sided quotes. Market-Makers will continue to be required to provide continuous two-sided quotes on a daily basis, and a Market-Maker's utilization of the kill switch will not prohibit the Exchange from taking disciplinary action against the Market-Maker for failing to meet the continuing quoting obligation each trading day.[37]

### *J. Quote Risk Monitor Mechanism*

Lastly, the Exchange proposed to amend the QRM Mechanism in CBOE Rule 8.18. Pursuant to the QRM mechanism, a Market-Maker may establish a (i) maximum number of contracts, (ii) a maximum cumulative percentage of the original quoted size of

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[28] *See* CBOE Rules 6.45A(d)(ii) and 6.45B(d)(ii).

[29] The Exchange also proposed to amend the rule to not apply the check when the NBBO is locked, crossed, or unavailable. In addition, the Exchange proposed to authorize a senior official at the Exchange's Help Desk to determine not to apply this check in the interest of maintaining a fair and orderly market. For example, the Exchange believes it is appropriate to disable this check in response to a market event or market volatility to avoid inadvertently cancelling quotes not erroneously priced but rather priced to reflect potentially rapidly changing prices. *See* Notice, *supra* note 3, at 64526. The Exchange represented that, pursuant to Exchange procedures, any decision to not apply the check and the reason for such decision will be documented, retained, and periodically reviewed. *See id.*

[30] Other exchanges maintain similar activity-based risk protections. *See, e.g.,* International Securities Exchange, LLC (''ISE'') Rule 714(d) and MIAX Rule 519A.

[31] As discussed above, orders (or unexecuted portions) that by their terms cancel if they do not execute immediately will be cancelled rather than rest in the book for a period of time (as proposed in this filing) pursuant to the drill through price check parameter if triggered. According to the Exchange, because these orders will not book or route pursuant to the drill through price check parameter, these orders will not be included in the count for the drill through event check. *See* Notice, *supra* note 3, at 64527 n. 33.

[32] The Exchange expects the initial time intervals for all these checks to be set at one and five minutes. The time intervals set by the Exchange will apply to all TPHs, who will not be able to change these time intervals. *See* Notice, *supra* note 3, at 64527 n. 34.

[33] *See* proposed CBOE Rule 6.14(e). The Exchange represented that other options exchanges have adopted similar functionality. *See* Notice, *supra* note 3, at 64528 n. 40; MIAX Rule 519(b).

[34] For purposes of determining the contract size of an incoming order or quote, the proposed rule states the contract size of a complex order will equal the contract size of the largest option leg of the order (*i.e.,* if the order is a stock-option order, this check will not apply to the stock leg of the order). *See* proposed CBOE Rule 6.14(e). If a TPH enters an order or quote to replace a resting order or update a resting quote, and the System rejects the incoming order or quote because it exceeds the applicable maximum contract size, the System also will cancel the resting order or any resting quote in the same series. In addition, the Exchange proposed to apply this check to paired orders submitted to AIM, SAM or as a QCC order. Further, the Exchange proposed that for an A:AIR order, if the System rejects the agency order, then the System rejects the contra-side order; however, if the System rejects the contra-side order, the System still accepts the agency order. *See* proposed CBOE Rule 6.14(e)(ii).

[35] *See* proposed CBOE Rule 6.14(f). The Exchange represented that other options exchanges have adopted similar kill switches. *See* Notice, *supra* note 3, at 64529; BOX Options Exchange LLC (''BOX'') Rule 7280 and PHLX Rule 1019(b).

[36] *See* Notice, *supra* note 3 at 64532.

[37] *See id.*

each side of each series, and (iii) the maximum number of series for which either side of its quote is fully traded, that may trade within a rolling time period in milliseconds also established by the Market-Maker. When these parameters are exceeded within the time interval, the System cancels the Market-Maker's quotes in the class and other classes with the same underlying on the same trading platform. In addition, CBOE Rule 8.18 allows Market-Makers or TPH organizations to specify a maximum number of QRM incidents across all classes on an Exchange-wide basis. When the Exchange determines that a Market-Maker or TPH organization has reached its QRM incident limit during the rolling time interval, the System will cancel all of the Market-Maker's electronic quotes and Market-Maker orders resting in the book in all option classes on the Exchange and prevent the Market-Maker or TPH organization from sending additional quotes or orders to the Exchange until the Market-Maker reactivates its ability to send quotes or orders.

Currently, use of the QRM is optional. The Exchange proposed to amend CBOE Rule 8.18 to make it mandatory for Market-Makers to enter values for each parameter for all classes in which they quote.[38]

## III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of Section 6 of the Act [39] and the rules and regulations thereunder applicable to the Exchange.[40] Specifically, the Commission finds that the proposed rule change is consistent with the Section 6(b)(5) [41] requirements that the rules of an 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 regulating, clearing, settling, processing information with respect to, and 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. The Commission believes that the proposed rule change is designed to mitigate the likelihood of orders trading at potentially erroneous prices, clarify when certain price/risk controls will apply, avoid locking an away market, and assist TPHs in managing their risk exposure to avoid potentially harmful and disruptive trading.

As discussed above, CBOE is proposing to amend its limit order price parameter for simple orders to use the NBBO when available in lieu of the Exchange's previous day's closing price or BBO. To the extent that the use of the NBBO, when available, rather than the Exchange's previous day's closing price or BBO, may better reflect the then current market, it should provide a suitable measure for purposes of determining the reasonability of the prices of orders. Moreover, the Commission believes that it is reasonable for CBOE to exclude orders with a stop contingency or orders routed from a PAR workstation or OMT from the limit order price check parameter. In particular, application of the limit order price check parameter to stop contingency orders may interfere with the application of the stop contingency, and orders routed from a PAR workstation or OMT may be less likely to execute at an erroneous price since they are manually reviewed and processed.

The Commission believes that the proposed rule change to expand the applicability of the put strike price and call underlying value checks to market orders [42] may help TPHs mitigate risks associated with orders trading at prices that exceed a corresponding benchmark, which may indicate an execution at a price that is potentially erroneous. Furthermore, the Commission believes the proposed rule change to eliminate the flexibility to not apply this check to orders entered during Extended Trading Hours will provide market participants with increased certainty regarding the inapplicability of this check.

The proposed changes to the drill through price checks provide additional detail to the rule regarding how the System handles certain orders that were not exposed prior to trading up to the drill through price and orders that traded up to the drill through price following exposure. In addition, allowing the remainder of orders to rest in the book for a brief time period at the drill through price may benefit investors by providing an additional opportunity for execution of their orders. Furthermore, clarifying that an order exposed via HAL pursuant to the drill through price check will not be exposed at a price worse than the NBBO is consistent with the current treatment of other orders exposed via HAL at the NBBO.[43]

The Commission also believes that the proposed amendments to the quote inverting NBBO check will provide market participants with greater clarity that CBOE will not apply the check in the absence of an NBBO and BBO. In addition, the proposed rule change eliminates the Exchange's flexibility to apply the check prior to the opening of a series as well as during a trading halt. Removing this flexibility and clearly stating when CBOE will not apply the check considerably enhances the transparency of the functionality.

With respect to CBOE's proposed changes regarding the execution of quotes that lock or cross the NBBO (Proposed Rule 6.14(c)), the Commission believes that the proposed rule change is consistent with the Act as it is reasonably designed to prevent the dissemination of a quote that locks or crosses an away market. Moreover, to the extent the Exchange determines to temporarily deactivate the check in the interest of maintaining a fair and orderly market, CBOE has represented that all such decisions by CBOE will be adequately justified, documented, retained, and periodically reviewed.[44]

Further, the Commission believes that the Exchange's proposed risk protection parameters and mechanisms for orders and quotes are reasonably designed to provide TPHs with additional tools to assist them in managing their risk exposure. Specifically, the order entry, execution, and price parameter rate checks, maximum contract size risk control, and mandatory use of the QRM may help TPHs to mitigate the potential risks associated with entering too many orders or quotes, executing too many contracts, having too many orders rejected because of price protection parameters, and entering orders or quotes with size that may be potentially erroneous that may result from, for example, technology issues with the broker's electronic trading system. To this extent, these TPH-customizable settings may help act as a backstop to the TPH's own controls and provide an additional layer of protection customized to the TPH's self-selected parameters. Moreover, the Commission notes that other exchanges have

[38] The Exchange represented that other options exchanges have made similar functionality mandatory for all Market-Makers. *See* Notice, *supra* note 3, at 64529; ISE Rule 804(g).

[39] 15 U.S.C. 78f(b).

[40] In approving these proposed rule changes, the Commission has considered the proposed rules' impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[41] 15 U.S.C. 78f(b)(5).

[42] The checks will not apply to market orders during an opening rotation since separate price protections will apply during the opening process. *See* Notice, *supra* note 3, at 64525.

[43] *See* current and proposed CBOE Rule 6.14A(b).

[44] *See supra* note 29 and accompanying text.

established similar risk protection mechanisms.[45] The Commission notes that the proposed functionality, including the cancellation of any resting interest, must be processed in sequence with other interest in the System and comply with the firm quote obligations in Rule 602 of Regulation NMS.

CBOE will require TPHs and Market-Makers to utilize these risk protection parameters and mechanisms. However, TPHs and Market-Makers will have discretion to customize the parameters in accordance with their respective risk management needs. In light of this flexibility, the Commission reminds TPHs to be mindful of their obligations, to among others, seek best execution of orders they handle on an agency basis and consider their best execution obligations when establishing parameters for the order entry, execution, price parameter rate checks, maximum contract size risk control, and QRM.[46] For example, an abnormally low order entry parameter should be carefully scrutinized, particularly if a TPH's order flow to the Exchange contains agency orders. To the extent that a TPH chooses sensitive parameters and those parameters apply to connections over which it transmits customer orders to the Exchange, a TPH should consider the effect of its chosen settings on its ability to receive a timely execution on marketable agency orders that it sends to the Exchange in various market conditions. The Commission cautions brokers considering their best execution obligations to be aware that an agency order they represent may be rejected as a result of these risk protections.

In addition, in light of the Exchange's decision not to set maximum or minimum values, or default values, the Commission expects CBOE to periodically assess whether these risk protection measures are operating in a manner that is consistent with the promotion of fair and orderly markets, including whether not utilizing maximum and minimum parameters or default values continues to be appropriate and in accordance with the Act and the rules thereunder.

Further, the Commission believes that Proposed Rule 6.14(f), which creates an optional kill switch mechanism, is consistent with the Act as it may further enhance risk management capabilities of TPHs by providing them with the ability to manage their risk exposure if they experience a significant system failure. To the extent that the kill switch mechanism provides TPHs with an appropriate backstop in this manner, it may encourage firms to provide liquidity on CBOE and thus contribute to fair and orderly markets in a manner that protects investors and the public interest. The Commission notes that the Exchange represented in its proposal that the kill switch will operate consistently with a broker-dealer's firm quote obligations pursuant to Rule 602 of Regulation NMS,[47] and that the kill switch does not diminish or relieve a Market-Maker of its obligation to provide continuous two-sided quotes.[48] The Exchange also represented that the kill switch message will be accepted by the System in the order of receipt in the queue and will be processed in such order. As such, the System will process interest already in the System prior to receipt of the kill switch message prior to processing the kill switch message.[49] Based on these representations, the Commission believes that the kill switch is reasonably designed to promote just and equitable principles of trade and perfect the mechanism of a free and open market. Lastly, the Commission notes that other exchanges have established kill switches that operate in a manner similar to that proposed by CBOE.[50]

Finally, the Commission believes that the proposal to authorize CBOE to share with Clearing TPHs the risk mitigation settings selected by a TPH for whom the Clearing TPH clears may assist Clearing TPHs manage their clearing risk exposure. The Commission notes that other exchanges have adopted similar rules authorizing the sharing of similar risk settings with clearing members.[51]

## IV. Solicitation of Comments on Amendment No. 1 to the Proposed Rule Change

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 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 email to *rule-comments@sec.gov.* Please include File Number SR–CBOE–2016–053 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–2016–053. This file number should be included on the subject line if email 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 Web site (*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 Web site 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; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–CBOE–2016–053, and should be submitted on or before December 1, 2016.

## 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 thirtieth day after the date of publication of notice of the amended proposal in the **Federal Register**. In Amendment No. 1,[52] CBOE clarified in its drill through rule text the exposure price of an order via HAL as CBOE had described it in the Notice. Amendment

[45] *See* ISE Rules 714(d) & 804(g); MIAX Rules 519(b) & 519A.

[46] *See, e.g.,* Securities Exchange Act Release Nos. 37619A (September 6, 1996), 61 FR 48290 (September 12, 1996) (Order Handling Rules adopting release); 51808 (June 9, 2005), 70 FR 37496, 37537–8 (June 29, 2005) (Regulation NMS adopting release).

[47] *See* Notice, *supra* note 3, at 64532.

[48] *See id.*

[49] *See id.*

[50] *See, e.g.,* BOX Rule 7280(b) and PHLX Rule 1019(b).

[51] *See, e.g.,* MIAX Rule 500; BX Chapter VI, Section 20; NYSE Arca Rule 6.2A(a); NYSE MKT Rule 902.1NY(a); and PHLX Rule 1016.

[52] *See* Amendment No. 1, *supra* note 4.

No. 1 further clarified CBOE's background discussion of how quotes and orders are cancelled pursuant to the QRM Mechanism in order to harmonize the description of the existing rule with the text of Rule 8.18. Both of these changes are consistent with the proposal as initially filed, and simply add detail to the filing to resolve internal inconsistencies. The changes do not introduce material, new, or novel concepts. Accordingly, the Commission finds good cause, pursuant to Section 19(b)(2) of the Act,[53] to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

**VI. Conclusion**

*It is therefore ordered,* pursuant to Section 19(b)(2) of the Act,[54] that the proposed rule change (SR–CBOE–2016–053), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[55]

**Brent J. Fields,**

*Secretary.*

[FR Doc. 2016–27153 Filed 11–9–16; 8:45 am]

**BILLING CODE 8011–01–P**

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## SECURITIES AND EXCHANGE COMMISSION

**[Release No. 34–79240; File No. SR–NASDAQ–2016–146]**

## Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 9400 To Include a Cross-Reference

November 4, 2016.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1], and Rule 19b-4 [2] thereunder, notice is hereby given that, on October 25, 2016, The NASDAQ Stock Market LLC (''Nasdaq'' 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 amend Rule 9400, entitled ''Expedited Client Suspension Proceeding'' to include a cross-reference for clarification.

The text of the proposed rule change is available on the Exchange's Web site at *http://nasdaq.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 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 is filing this proposal to amend Rule 9400, entitled ''Expedited Client Suspension Proceeding'' to include a cross-reference Chapter III, Section 16, entitled ''Disruptive Quoting and Trading Activity Prohibited'' within Rule 9400. The Exchange filed a rule change to adopt an options rule, identical to equities Rule 2170, which relates to disruptive quoting and trading activity.[3] In that rule change, it stated that ''[t]he Exchange will initiate disciplinary action for violations of Chapter III, Section 16, pursuant to Rule 9400.'' [4] At that time, the Exchange inadvertently did not include the cross-references to Chapter III, Section 16 within Rule 9400. The Exchange proposes to add references to Chapter III, Section 16 within Rule 9400 for clarity. This rule change is non-controversial.

Background

The Exchange filed a rule change to adopt an options rule to clearly prohibit disruptive quoting and trading activity on the Exchange and to permit the Exchange to take prompt action to suspend members or their clients that violate such rule pursuant to Rule 9400.[5] The Exchange had previously adopted Rule 9400 to set forth procedures for issuing suspension orders, immediately prohibiting a member from conducting continued disruptive quoting and trading activity on the Exchange.[6] Rule 9400 provides the Exchange the authority to order a member to cease and desist from providing access to the Exchange to a client of the member that is conducting disruptive quoting and trading activity in violation of Rule 2170. The Exchange also previously adopted Rule 2400 to specifically define and prohibit disruptive equities quoting and trading activity on the Exchange.[7] Chapter III, Section 16 is identical to Rule 2400, however applicable to options. Similarly, Chapter III, Section 16 prohibits members from engaging in or facilitating disruptive options quoting and trading activity on the Exchange.

The Exchange proposes to simply add the cross-references for the options rules alongside the equity rule for clarity. This rule change is consistent with the intent of the rule proposal which adopted Chapter III, Section 16.[8]

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 the rules of the Exchange are designed to prevent fraudulent and manipulative acts and practices, it [sic] 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 making clear within Rule 9400 that violations of Chapter III, Section 16 are subject to disciplinary action pursuant to Rule 9400 as stated in the Exchange's rule filing.[11] This cross-reference will provide clarity to members and ease of reference to the

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[53] 15 U.S.C. 78s(b)(2).

[54] *See id.*

[55] 17 CFR 200.30–3(a)(12).

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

[2] 17 CFR 240.19b–4.

[3] *See* Securities and Exchange Release No. 78208 (June 30, 2016), 81 FR 44366 (July 7, 2016) (SR–NASDAQ–2016–092).

[4] *See* Securities and Exchange Release No. 78208 (June 30, 2016), 81 FR 44366, 44370 (July 7, 2016) (SR–NASDAQ–2016–092). Rule 9400 is located within the Code of Procedure rules which apply to both equities and options violations.

[5] *See* note 3.

[6] *See* Securities and Exchange Release No. 77913 (May 25, 2016), 81 FR 35081 (June 1, 2016) (SR–NASDAQ–2016–074).

[7] *See* note 3.

[8] *See* note 3.

[9] 15 U.S.C. 78f(b).

[10] 15 U.S.C. 78f(b)(5).

[11] *See* note 4.