

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-78200; File No. SR-NASDAQ-2016-091]

### Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Professionals Order Counting

June 30, 2016.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 17, 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 the NASDAQ Options Market LLC (“NOM”) Rules at Chapter I, Section 1, entitled “Definitions,” to add specificity to the definition of a Professional with respect to the manner in which the volume threshold will be calculated by the Exchange.

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 proposes to amend the definition of “Professional” at Chapter I, Section 1(49) to specify the manner in which the Exchange calculates orders to determine if an order should be treated as Professional.

##### Background

The definition of the term Professional at Chapter I, Section 1(48), currently states, “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).” In order to properly represent orders entered on the Exchange Participants are required to indicate whether Public Customer<sup>3</sup> orders are “Professional” orders.”<sup>4</sup> To comply with this requirement, Participants are required to review their Public Customers’ activity on at least a quarterly basis to determine whether orders that are not for the account of a broker-dealer should be represented as Public Customer orders or Professional orders.<sup>5</sup>

The Exchange accepts orders routed from other markets that are marked Professional. The designation of Professional or Professional order does not result in any different treatment of such orders for purposes of Exchange rules concerning away market protection. That is, all non-broker or dealer orders, including those that meet the definition of Professional orders, are treated equally for purposes of Exchange away market protection rules.<sup>6</sup> The Exchange continues to believe that identifying Professional accounts based

upon the average number of orders entered in qualified accounts is an appropriately objective approach to reasonably distinguish such persons and entities from retail investors or market participants.

##### Proposal

The Exchange proposes to count each order entered by a Professional toward the number of orders, regardless of the options exchange to which the order was routed in determining Professional orders.<sup>7</sup>

##### Cancel and Replace

A cancel and replace order is a type of order that replaces a prior order. The Exchange believes that the second order (the replacement order) should be counted as a new order. With respect to “single-strike algorithms,” which are a series of cancel and replace orders in an individual strike which track the NBBO, these orders shall be counted as new orders.<sup>8</sup> The Exchange believes that because the Public Customer is specifically instructing the executing broker in the “single-strike algorithm” scenario to cancel and replace these orders. This type of activity is akin to market making in a Public Customer account and should be counted, as a new order.

##### Parent/Child Orders

An order that converts into multiple subordinate orders to achieve an execution strategy<sup>9</sup> shall be counted as one order per side and series, even if the order is routed away. An order that cancels and replaces a resulting subordinate order and results in multiple sides/series shall be counted as a new order on each side and series. For purposes of counting Public Customer orders, the manner in which the Public Customer submitted the order and whether the order was on the same side and series will determine if the order will count as one order. If one Public Customer order on the same side and series is subsequently broken-up by a broker into multiple orders for purposes of execution or routed away, this order will count as one order. The Exchange believes that the proposed amendment will provide more certainty to market participants in determining the manner in which the Exchange will compute the

<sup>3</sup> The term “Public Customer” means a person that is not a broker or dealer in securities. See Chapter I, Section 1(49).

<sup>4</sup> The Exchange utilizes a special order origin code for Professional orders.

<sup>5</sup> Orders for any Public Customer that had an average of more than 390 orders per day during any month of a calendar quarter must be represented as Professional orders for the next calendar quarter. Members are required to conduct a quarterly review and make any appropriate changes to the way in which they are representing orders within five days after the end of each calendar quarter. While members are only required to review their accounts on a quarterly basis, if during a quarter the Exchange identifies a Public Customer for which orders are being represented as Public Customer orders but that has averaged more than 390 orders per day during a month, the Exchange will notify the member and the member will be required to change the manner in which it is representing the Public Customer’s orders within five days.

<sup>6</sup> See Exchange Rules at Chapter VI, Section 11, Chapter XII, Sections 2 and 3.

<sup>7</sup> All order types count toward the 390 orders on average per day.

<sup>8</sup> Cancel messages do not count as an order.

<sup>9</sup> An order which is placed for the beneficial account(s) of a person or entity that is not a broker or dealer in securities that is broken into multiple parts by a broker or dealer or by an algorithm housed at a broker or dealer or by an algorithm licensed from a broker or dealer. Strategies include volatility orders, for example.

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

number of orders in listed options per day on average during a calendar month for its own beneficial account(s) to determine the Professional designation.

In order to make clear when orders will count as new orders, the Exchange offers the following scenarios as examples.

- The Exchange proposes to count multiple orders that were submitted by the member as separate orders as multiple orders.
- The Exchange proposes to count a single order submitted by a member, which was automatically executed in multiple parts by the trading system, as one order, because the member did not intervene to create multiple orders. Another example is where an order was entered in the trading system and only partially filled, the order would count as one order. The subsequent fills, which could be multiple executions, would not count as additional orders in determining the 390 limit. The manner in which the order is ultimately executed, as one order or multiple orders, should not itself determine whether the activity is that of a Professional; also the member did not intervene in that circumstance.
- The Exchange proposes to not count an order which reprices, for example because of a locked and crossed market, as a new order because the member did not intervene.

- The Exchange proposes to count orders, which result in multiple orders due to cancel and replacement orders, as new orders. This is because in this situation the member did intervene to create the subsequent orders.

- The Exchange proposes to count an order submitted by the Public Customer as a single order, on the same side and series, as a single order despite the fact that a broker broke-up the order into multiple orders for purposes of execution.

The Exchange notes that other options exchanges have issued notices which describe the manner in which those Exchanges believe thresholds should be computed for determining if an order qualifies as a Professional order.<sup>10</sup> The Exchange believes that there is industry confusion as to which orders count toward the 390 contract threshold. The Exchange's proposal is intended to provide clarity and to continue to promote consistency in the treatment of orders as Professional orders.

Below are some examples of the calculation of Professional orders.

#### Example #1:

A Public Customer has an order to buy 100 calls at a volatility level of 35. The order then generates a child order resulting in a 1.00 bid for 100 options which is sent to exchange A. After the underlying stock price ticks up 2 cents

the child order is then adjusted to reflect a 35 level volatility which in this case (50 delta) results in a 1.01 bid sent to Exchange A replacing the current 1.00 bid.

In determining the number of orders that attribute to the 390 order count, in this case, because the child order is being canceled and replaced in the "same series" this would only count as one (1) order for purposes of Professional designation calculation.

#### Example #2:

A Public Customer has an order to buy 20k Vega at a 35 volatility level in symbol XYZ. The order then generates 50 child orders across different strikes. Throughout the day those 50 orders are adjusted as the stock moves resulting in the replacement of child orders to the tune of 5 times per order (50 x 5 cancels) resulting in 250 total orders generated to Exchange A.

In determining the number of orders that attribute to the 390 order count, in this case, because the child orders generated are across multiple series it would be necessary to count all 250 orders.

In addition to the above examples, the Exchange provides the below chart to demonstrate the manner in which it will count orders.

Single strike activity	Singular	Multiple
Public Customer order posted to 1 SRO Order Book .....	x	.....
Public Customer order posted to Multiple SRO Order Books simultaneously .....	x	.....
Cancel/Replace Activity .....	.....	x
Cancel/Replace Activity tracking NBBO .....	.....	x

Singular—counts as a single order towards the 390 count

Multiple—each order applies towards the 390 count

The Exchange proposes to implement this rule on July 1, 2016 to provide market participants with advance notice for their quarterly calculations. The Exchange will issue an Options Trader Alert in advance to inform market participants of such date.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>11</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>12</sup> in particular, in that it is designed to promote just and equitable principles of trade, to remove impediments to and

perfect the mechanism of a free and open market and a national market system, and, in general to protect investors and the public interest, by promoting the consistent application of its rules by further defining the manner in which the Exchange will compute the number of orders in listed options per day on average during a calendar month for its own beneficial account(s) for purposes of determining the Professional designation. Furthermore, the Exchange believes that specifying the manner in which the 390 threshold will be calculated within its Rules will provide members with certainty and provide them with insight as they conduct their own quarterly reviews for purposes of designating orders.

The Exchange believes that counting all orders toward the number of orders, regardless of the options exchange to which the order was routed, will promote the consistent application of its rules by making clear that all order types shall be counted as well as all orders for the purpose of determining whether the definition of Professional has been met.

#### Cancel and Replace

With respect to determining the Professional designation, a cancel and replace order that replaces a prior order shall be counted as a second order. An order that is filled partially or in its entirety or is a replacement order that is automatically canceled or reduced by the number of contracts that were

<sup>10</sup> See NYSE Arca, Inc.'s and NYSE MKT LLC's Joint Regulatory Bulletin (RBO-15-03 and RBO-15-06, respectively) dated September 9, 2015; CBOE's Regulatory Circular (RG10-126) dated

December 1, 2010; and the International Securities Exchange LLC's Regulatory Information Circular (2009-179) dated June 23, 2009.

<sup>11</sup> 15 U.S.C. 78f(b).

<sup>12</sup> 15 U.S.C. 78f(b)(5).

executed will not count as second order because it was not replaced.<sup>13</sup> The Exchange believes that counting the replacement order as a second order is consistent with Exchange Rules because the replacement order is viewed as a new order with its own unique identifier.

The Exchange believes that counting cancel and replace orders with “single-strike algorithms,” which are a series of cancel and replace orders in an individual strike which track the NBBO, as new orders is consistent with the Act because the Public Customer is specifically instructing the executing broker in the “single-strike algorithm” scenario to cancel and replace these orders. Tracking the NBBO<sup>14</sup> is akin to market making on the Exchange in a Public Customer account and should be counted as new orders. The Exchange believes that the Public Customers order designation should be reserved for retail Public Customers.

#### Parent/Child Orders

The Exchange’s adoption of the Professional order was to treat orders in listed options per day on average during a calendar month in his or her own beneficial account differently from Public Customer orders for purposes of pricing.<sup>15</sup> For this reason, the Exchange is adopting rules concerning the computation of orders which convert into multiple subordinate orders for the purpose of determining the Professional designation. The Exchange’s proposal to count multiple subordinate orders that achieve an execution strategy as one order per side and series and count an order that cancels and replaces a resulting subordinate order and results in multiple sides/series as a new order is consistent with the Act, because the Exchange is distinguishing where the member is actively entering orders that result in multiple orders and canceling and replacing orders that result in multiple orders versus where the

member had no control of the resulting executions. Allowing orders on the same side of the market to be counted as a single order is consistent with the original intent of the Professional order designation. The same side of market distinction protects retail Public Customers. This practice is typically the type of transaction Public Customers execute versus a Professional trader. Multiple related orders resulting from a large order filled in part, or an order which is cancelled and replaced several times are considered part of a related order. The Exchange does not desire to count large orders filled in part as multiple orders because the member did not intervene in the outcome of the execution. An order that results in several separate and unrelated orders would be counted as multiple orders because the member intervened in this circumstance.

The Exchange believes that the proposed amendment will provide more certainty to market participants in determining the computation of the number of orders in listed options per day on average during a calendar month for its own beneficial account(s) to determine the Professional designation. The Exchange notes that other options exchanges have issued notices describing the manner in which they believe that Professional order should be counted when determining if an order qualifies as a Professional order.<sup>16</sup> The Exchange believes that there is confusion as to which orders count toward the 390 contract threshold. The Exchange proposes to provide clarity to its Rules with specific guidance as to the computation of Professional orders, which it believes will promote consistency in the treatment of orders as Professional orders. The Exchange believes that this proposed guidance will promote consistency and permit the proper calculation of options orders to prevent members with high volume from receiving benefits reserved for Public Customer orders. The Professional designation focuses specifically on the number of orders generated.

NOM’s System executes order based on Price-Time priority, however, a marketplace advantage afforded to Public Customer orders on the Exchange is that members are generally not assessed transaction fees for the

execution of Public Customer orders. The purpose of these marketplace advantages is to attract retail order flow to the Exchange by leveling the playing field for retail investors over market Professionals.<sup>17</sup> The Exchange believes that permitting certain types of orders to be counted as a single order and other types of orders to be counted as multiple orders is consistent with the original intent of the Professional designation which was to continue to provide Public Customer accounts with marketplace advantages and distinguish those accounts non-Professional retail investors from the Professionals accounts some non-broker-dealer individuals and entities have access to information and technology that enables them to Professionally trade listed options in the same manner as a broker or dealer in securities.<sup>18</sup>

Finally, the proposed guidance is being issued to stem confusion as to the manner in which options exchanges compute the Professional order volume. The Exchange’s Rules may be similar to notices issued by NYSE Arca, Inc, NYSE MKT LLC (“NYSE MKT”) and International Securities Exchange LLC (“ISE”).

#### *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 because the Exchange will uniformly apply the rules to calculate volume on all members in determining Professional orders. The designation of Professional orders would not result in any different treatment of such orders for purposes of the Exchange’s Rules concerning order protection or routing to away exchanges. Also, SIFMA supports the guidance issued by NYSE Arca and NYSE MKT. The guidance is being issued to stem confusion as to the manner in which options exchanges compute the Professional order volume.

The Exchange is adopting similar counting methods the Exchange believes is currently being utilized by NYSE

<sup>13</sup> See Exchange Rules at Chapter VI, Section 1(e)(1). Cancel-replacement order shall mean a single message for the immediate cancellation of a previously received order and the replacement of that order with a new order with new terms and conditions. If the previously placed order is already filled partially or in its entirety, the replacement order is automatically canceled or reduced by the number of contracts that were executed. The replacement order will not retain the priority of the cancelled order except when the replacement order reduces the size of the order and all other terms and conditions are retained.

<sup>14</sup> Tracking the NBBO shall mean any parent order that consumes any self-regulatory organization order book data feed, or the OPRA feed, to generate automated child orders, and move with, or follow the Bid or Offer of the series in question.

<sup>15</sup> See NOM Rules at Chapter VI, Section 10 and Chapter XV, Section 2.

<sup>16</sup> See NYSE Arca, Inc.’s and NYSE MKT LLC’s Joint Regulatory Bulletin (RBO-15-03 and RBO-15-06, respectively) dated September 9, 2015; The Chicago Board Options Exchange, Incorporated’s Regulatory Circular (RG10-126) dated December 1, 2010; and the International Securities Exchange LLC’s Regulatory Information Circular (2009-179) dated June 23, 2009.

<sup>17</sup> Market Professionals have access to sophisticated trading systems that contain functionality not available to Public Customers, including things such as continuously updated pricing models based upon real-time streaming data, access to multiple markets simultaneously and order and risk management tools.

<sup>18</sup> For example, some broker-dealers provided their Professional customers with multi-screened trading stations equipped with trading technology that allows the trader to monitor and place orders on all six options exchanges simultaneously. These trading stations also provide compliance filters, order managements tools, the ability to place orders in the underlying securities, and market data feeds.

MKT, NYSE ARCA and ISE related to designation of Professional orders.

#### Counting All Orders

The Exchange believes that counting all orders entered by a Professional toward the number of orders, regardless of the options exchange to which the order was routed, does not create an undue burden on intra-market competition because this proposed rule change will be consistently applied to all members in determining Professional orders.

#### Cancel and Replace

The Exchange believes that its application of cancel and replace orders does not create an undue burden on intra-market competition because this application is consistent with Exchange Rules, where the replacement order is viewed as a new order. This treatment is consistent with the manner in which this order type is applied today within the Order Book.

#### Parent/Child Orders

The Exchange's treatment of subordinate orders does not create an undue burden on intra-market competition because allowing orders on the same side of the market to be counted as a single order is consistent with the original intent of the Professional order designation which is to count distinct orders and focus on the number of orders generated.

The Exchange does not believe that the proposed rule change will impose an undue burden on inter-market competition because other exchanges have announced the intent to adopt similar guidance.<sup>19</sup> The Exchange believes that disparate rules regarding Professional order designation, and a lack of uniform application of such rules, does not promote the best regulation and may, in fact, encourage regulatory arbitrage. The Exchange believes that it is therefore prudent and necessary to conform its rules to that of other options exchanges for purposes of calculating the threshold volume of orders to be designated as a Professional. This is particularly true where the Exchange's third-party routing broker-dealers are members of several exchanges that have rules requiring Professional order designations.

#### *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**

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>20</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>21</sup> A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative prior to 30 days after the date of filing.<sup>22</sup> Rule 19b-4(f)(6)(iii), however, permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest.<sup>23</sup>

The Exchange has requested that the Commission waive the 30-day operative delay. The Commission notes that it has considered a substantially similar proposed rule change filed by CBOE and PHLX which it approved after a notice and comment period.<sup>24</sup> This proposed rule change does not raise any new or novel issues from those considered in the CBOE and PHLX proposals. Based on the foregoing, the Commission believes that it is consistent with the protection of investors and the public interest to waive the 30-day operative date so that the proposal may take effect upon filing.<sup>25</sup>

At any time within 60 days of the filing of such proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such

action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings under Section 19(b)(2)(B) of the Act<sup>26</sup> to determine whether the proposed rule change 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
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR-NASDAQ-2016-091 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 No. SR-NASDAQ-2016-091. 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 such filing will also 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

<sup>20</sup> 15 U.S.C. 78s(b)(3)(a)(iii).

<sup>21</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

<sup>22</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>23</sup> *Id.*

<sup>24</sup> See Securities Exchange Act Release Nos. 77450 (March 25, 2016) (Order Approving SR-CBOE-2016-005); 77449 (March 25, 2016), 81 FR 18665, (March 31, 2016) (Order Approving SR-Phlx-2016-10).

<sup>25</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>26</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>19</sup> See *supra* note 16.

information that you wish to make available publicly. All submissions should refer to File No. SR–NASDAQ–2016–091 and should be submitted on or before July 28, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>27</sup>

**Robert W. Errett,**  
Deputy Secretary.

[FR Doc. 2016–16027 Filed 7–6–16; 8:45 am]

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–78221; File No. SR–BatsEDGX–2016–28]

### Self-Regulatory Organizations; Bats EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Add Interpretation and Policy .01 to Rule 16.1 To Specify the Calculation Methodology for Counting Professional Orders

July 1, 2016.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),<sup>1</sup> and Rule 19b–4 thereunder,<sup>2</sup> notice is hereby given that on June 30, 2016, Bats EDGX Exchange, Inc. (the “Exchange” or “EDGX”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Exchange has designated this proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b–4(f)(6)(iii) thereunder,<sup>4</sup> which renders it effective upon filing with the Commission. 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 add Interpretation and Policy .01 to Rule 16.1 to specify the manner in which the Exchange calculates average daily order submissions for purposes of counting Professional orders, as further described below.

The text of the proposed rule change is available at the Exchange’s Web site at [www.batstrading.com](http://www.batstrading.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 parts of such statements.

##### A. Self-Regulatory Organization’s Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

The Exchange proposes to add Interpretation and Policy .01 to Rule 16.1 to specify the methodology for counting average daily order submissions in listed options to determine whether a person or entity meets the definition of a Professional (“Professional order counting”). The proposed rule change is designed to harmonize Professional order counting with the recently adopted rules of competing options exchanges—specifically the Chicago Board of Options Exchange, Inc. (“CBOE”) and NASDAQ OMX PHLX LLC (“PHLX”).<sup>5</sup>

Rule 16.1(a)(46) defines a Professional “as any person or entity that (A) is not a broker or dealer in securities; and (B) places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s).” In adopting Rule 16.1(a)(46), the Exchange believed that identifying Professional accounts based upon the average number of orders entered in qualified accounts is an appropriate, objective approach that will reasonably distinguish such

persons and entities from non-professional, retail investors or market participants. In order to properly represent orders entered on the Exchange, Options Members are required to indicate whether Customer orders are “Professional” orders.<sup>6</sup> To comply with this requirement, Options Members are required to review their Customers’ activity on at least a quarterly basis to determine whether orders that are not for the account of a broker-dealer should be represented as Customer orders or Professional orders.<sup>7</sup>

The advent of new multi-leg spread products and the proliferation of the use of complex orders and algorithmic execution strategies by both institutional and retail market participants has raised questions as to what should be counted as an “order” for Professional order counting purposes. The proposed changes would specifically address the counting of multi-leg spread products, algorithm generated orders, and complex orders for purposes of determining Professional status. In addition, the proposal is intended to provide guidance regarding the methodology used by the Exchange when calculating average daily orders for Professional order counting purposes.<sup>8</sup>

As proposed, the rule would provide that an order would count as one order for Professional counting purposes, unless one of the exceptions enumerated in the proposed rule stipulates otherwise (each an “Exception”). The first Exception relates to the treatment of complex orders for purposes of computing orders for Professional order counting purposes. Specifically, the proposed rule provides that a complex order of eight (8) option legs or less would count as one order, whereas a complex order comprised of nine (9) option legs or more counts as

<sup>6</sup> See e.g., Rule 18.2(a)(6) (Conduct and Compliance with the Rules) (requiring that accurate information is input into the System, including but not limited to, the Options Member’s capacity).

<sup>7</sup> Orders for any customer that had an average of more than 390 orders per day during any month of a calendar quarter must be represented as Professional orders for the next calendar quarter. Option Members would be required to conduct a quarterly review and make any appropriate changes to the way in which they are representing orders within five business days after the end of each calendar quarter. While Option Members only would be required to review their accounts on a quarterly basis, if during a quarter the Exchange identifies a customer for which orders are being represented as Customer orders but that has averaged more than 390 orders per day during a month, the Exchange would notify the Option Member would be required to change the manner in which it is representing the customer’s orders within five business days.

<sup>8</sup> This proposal is consistent with CBOE and PHLX’s approved rules. See *supra* note 5.

<sup>27</sup> 17 CFR 200.30–3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b–4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b–4(f)(6)(iii).

<sup>5</sup> See Securities Exchange Act Release Nos. 77450 (March 25, 2016), 81 FR 18668, (March 31, 2016) (SR–CBOE–2016–005); 77449 (March 25, 2016), 81 FR 18665, (March 31, 2016) (SR–Phlx–2016–10) (approval orders). The Exchange notes that it recently issued guidance regarding Professional order counting. See e.g., Bats BZX Exchange, Inc. and Bats EDGX Exchange Inc., Regulatory Circular (RC–2015–012, respectively) dated December 21, 2015. This proposal codifies that guidance in a manner that is consistent with CBOE and PHLX’s approved rules. The Exchange notes that various other options exchanges refer to Professionals as “Professional Customers.” The Exchange has proposed to continue to use the term Professional, as is currently the case in Exchange rules.