

Regulatory Circular RG15-087

Date: May 29, 2015

To: Trading Permit Holders

From: Business Development Division

Re: Re-activation of the Solicitation Auction Mechanism (SAM) and Qualified Contingent Cross (QCC)

Updates RG08-53, RG13-102, RG14-076 and RG14-121

Effective June 1, 2015, Chicago Board Options Exchange, Incorporated ("CBOE") will re-activate the Solicitation Auction Mechanism ("SAM") and Qualified Contingent Cross ("QCC") functionality for both simple and complex orders in all CBOE non-exclusive option classes.¹

Summary details on SAM and QCC are as follows:

SAM

- SAM is an auction mechanism that a Trading Permit Holder ("TPH") may use to electronically execute orders it represents as agent ("Agency Orders") against solicited orders.
- SAM utilizes the same FIX/CMI2 formats as Automated Improvement Mechanism ("AIM," see Rule 6.74A; see also Regulatory Circular RG08-53 for information on the formats) except that Agency Orders and solicited orders submitted for SAM auction processing must contain an all-or-none ("AON") contingency and be for a size not less than 500 standard option contracts (5,000 mini-option contracts).
- Agency Orders submitted for SAM auction processing must be stopped with a solicited order priced at or within the NBBO.
- The Exchange has determined that the minimum price increment for SAM auction initiation and responses will be \$0.01 for simple and complex orders in all classes where SAM is activated.
- TPHs may submit responses during the auction period, which shall be one second, except responses may not be entered for the account of an options Market-Maker from another options exchange.
- TPHs may not use SAM to circumvent Rules 6.45A.01, 6.45B.01 and 6.74A limiting principal transactions. This may include, but is not limited to, TPHs entering contra orders that are solicited from (a) affiliate broker-dealers, or (b) broker-dealers with which the TPH has an arrangement that allows the TPH to realize similar economic benefits from the solicited transaction as it would achieve by executing the customer order in whole or in part as principal. These restrictions are generally not systematically enforced -- TPHs are responsible for ensuring compliance with these requirements. The system does enforce the following: If an Agency Order submitted into SAM is paired against a contra-side order from the same executing clearing firm and the order origin code on the contra-side order is "F",² then both orders will be cancelled.
- Solicited contra orders entered by TPHs to trade against Agency Orders may not be for the account of a CBOE Market-Maker assigned to the options class.³ An Agency Order may

¹ Exclusive classes include DJX, XSP, MXEA, MXEF, and classes of options listed in Underlying Symbol List A of the CBOE Fees Schedule, footnote 34.

² Origin Code "F" is used for OCC clearing member firm proprietary account orders. See CBOE Regulatory Circular RG13-038.

execute against a solicited order priced at or within the NBBO (as of the time that the Agency Order was received) if (i) the cumulative size of any marketable resting orders, quotes, and responses cannot satisfy the entire Agency Order at an improved price(s) and (ii) there are no public customer orders resting in the book on the opposite side of the Agency Order at the proposed execution price.

- If there is sufficient size to execute the Agency Order at an improved price, then the Agency Order will execute against resting orders, electronic quotes, and auction response interests and the solicited order will be cancelled.

Under Rule 6.74B.02, prior to submitting an Agency Order for SAM auction processing on behalf of customers, TPHs must deliver to the customer written notification informing the customer that discloses the terms and conditions of SAM in a form approved by CBOE. The following text may be used by TPHs to satisfy this requirement:

When handling an order of 500 contracts or more on your behalf, [firm] may solicit other parties to execute against your order and may thereafter execute your order using the Chicago Board Options Exchange's Solicitation Auction Mechanism. This functionality provides a single-priced execution, unless the order results in price improvement for the entire quantity, in which case multiple prices may result. For further details on the operation of the Solicitation Auction Mechanism, please refer to Chicago Board Options Exchange Rule 6.74B, which is available at www.cboe.org/Legal.

TPHs may submit alternative forms of notification for approval. Questions regarding the SAM customer notification process may be directed to the Regulatory Interpretations and Guidance team at RegInterps@cboe.com or (312) 786-8141.

For additional information regarding SAM auction and solicitation requirements, please refer to Rule 6.74B.

QCC

- A qualified contingent cross ("QCC") order is an order to buy (sell) at least 1,000 standard option contracts (or 10,000 mini-option contracts), that is identified as being part of a qualified contingent trade coupled with a contra-side order to sell (buy) an equal number of contracts. Please note that transactions that are subject to the QCC order designation must consist of only two orders/parties (one order/party on each side of the trade). Multiple parties are not allowed, even if two or more contra-parties on one side of the trade can meet the threshold amount of at least 1,000 contracts (or 10,000 in the case of mini-option contracts). (See Regulatory Circular RG13-041.)
- Complex QCC orders must be for a minimum of 1,000 contracts per leg (10,000 minimum per leg in mini options). Note that CBOE systems will not systematically enforce minimum leg quantities

³ Note, however, that pending regulatory approval, the Exchange is proposing to remove this restriction from Rule 6.74B to allow Market-Makers orders to be the solicited contra-side order, subject to certain order entry conditions and order modification prohibitions. See Securities and Exchange Release No. 74862 (March 17, 2015) (Notice of Filing of a Proposed Rule Change Relating to Rules 6.74A and 6.74B) (SR-CBOE-2015-026); see also Securities and Exchange Release No. 74862 (May 4, 2015) (Notice of Designation of Longer Period for Commission Action on Proposed Rule Change Relating to Rules 6.74A and 6.74B).

for complex orders -- TPHs are responsible for ensuring compliance with these minimum leg quantity requirements.

- Single-leg QCC orders may only be entered in the standard price increments applicable to simple orders in the option class as specified under Rule 6.42. Multi-leg complex QCC orders may be entered in \$0.01 increments.
- In order to satisfy QCC transaction requirements, a qualified contingent trade must consist of two or more component orders, executed as agent or principal, where:
 - (1) at least one component is an NMS stock, as defined in Rule 600 of Regulation NMS under the Exchange Act;
 - (2) all components are effected with a product or price contingency that either has been agreed to by all the respective counterparties or arranged for by a broker-dealer as principal or agent;
 - (3) the execution of one component is contingent upon the execution of all other components at or near the same time;
 - (4) the specific relationship between the component orders (e.g., the spread between the prices of the component orders) is determined by the time the contingent order is placed;
 - (5) the component orders bear a derivative relationship to one another, represent different classes of shares of the same issuer, or involve the securities of participants in mergers or with intentions to merge that have been announced or cancelled; and
 - (6) the transaction is fully hedged (without regard to any prior existing position) as a result of other components of the contingent trade.

Qualified contingent cross orders may execute without exposure provided the execution (1) is not at the same price as a public customer order resting in the electronic book and (2) is at or between the NBBO. A qualified contingent cross order will be cancelled if it cannot be executed.

Information regarding QCC transaction fees is available in the CBOE fee schedule at <http://www.cboe.com/publish/feeschedule/CBOEFeeSchedule.pdf>.

QCC Order Entry Mechanics:

QCC Orders may be submitted electronically from on or off the CBOE trading floor using PULSe, FBW, OMT, or directly via the FIX and CMI APIs. QCC Order senders should insert "A:AIQ" in FIX tag 9324 using the FIX paired order format or a "3" in the Paired Order message field in a CMI2 Paired Order. API message specifications and testing are available through the API Group at 312-786-7300/api@cboe.com.

In order to effect proprietary orders (including QCC Orders) electronically from on the floor of the Exchange, TPHs must ensure that they qualify for an exemption from Section 11(a)(1) of the Exchange Act. In general, Section 11(a)(1) restricts any member of a national securities exchange (which are referred to as "Trading Permit Holders" or "TPHs" in the CBOE Rules) from effecting any transaction on such exchange for (i) the member's own account, (ii) the account of a person associated with the member, or (iii) an account over which the member or a person associated with the member exercises discretion, unless a specific exemption is available. For additional information regarding Section 11(a)(1), including examples of common statutory exemptions, please refer to Regulatory Circular RG11-079.⁴

⁴ TPHs should pay particular attention to footnote 3 regarding the QCC order type and the "G Order" exemption, indicating that TPHs that intend to rely on the "G Order" exemption must price QCC orders at

**Reporting Requirement:**

For each QCC that is executed at the CBOE, the executing TPH must provide the Regulatory Division with a spreadsheet containing the following stock and option information:

<u>Stock information:</u>	<u>Option Information:</u>
Symbol	Class Symbol & Series Information
Share Quantity	Contract Quantity
Execution Date & Time	Execution Date & Time
Execution Price	Execution Price
Exchange of execution	Correspondent firm code
Buy & Sell Clearing Firm	Branch ID & Sequence number
	Executing Firm
	CMTA (if applicable)
	Indicate whether the QCC was entered from on or off the CBOE trading floor

The information must be submitted to the Regulatory Division via email at gcctrade@cboe.com no later than the opening of trading on the day following the execution date.

Additional Information:

- Questions regarding operational matters related to this circular may be directed to the CBOE Help Desk at helpdesk@cboe.com or 866-728-2263.
- For any additional information on regulatory matters related to this circular, please contact the Regulatory Interpretations and Guidance team at RegInterps@cboe.com or (312) 786-8141.

a price that improves the Exchange's best bid or offer on the same side of the market in order to effectively yield to non-member interests.