



## EDGX Regulatory Circular RC19-024

**Date:** October 15, 2019 (Updated 11/15/2019)

**To:** Members

**From:** Legal and Regulatory Divisions

**RE:** Retail Priority Orders

On October 2, 2019, the Securities and Exchange Commission (“SEC” or “Commission”) approved Cboe EDGX Exchange, Inc. (the “Exchange” or “EDGX”) Rule Filing [SR-CboeEDGX-2019-012](#), as modified by [Amendment No. 1](#), which introduces order book priority for equity orders submitted on behalf of retail investors (referred to as “Retail Priority Orders”).<sup>1</sup> Changes associated with the rule filing will be implemented on November 1, 2019.<sup>2</sup>

This Regulatory Circular includes a set of Frequently Asked Questions (“FAQs”) regarding Retail Priority Orders, and provides further clarification as to how retail customer orders should be counted pursuant to the Rules.

### Retail Priority Order Designation

- **Retail Order Defined:** The Commission’s approval of Rule Filing SR-CboeEDGX-2019-012 does not change the definition of “Retail Order” in the Exchange Rules. Under Rule 11.21(a)(2), a “Retail Order” is an “agency or riskless principal order that meets the criteria of FINRA Rule 5320.03 that originates from a natural person and is submitted to the Exchange by a Retail Member Organization [(‘RMO’)], provided that no change is made to the terms of the order with respect to price or side of market and the order does not originate from a trading algorithm or any other computerized methodology.”
- **Retail Priority Orders Defined:** As adopted pursuant to Rule Filing SR-CboeEDGX-2019-012, Interpretation and Policy .01 to Rule 11.9 defines a “Retail Priority Order” as a “Retail Order... that is entered on behalf of a person that does not place more than 390 equity orders per day on average during a calendar month for its own beneficial account(s).” Note that the count applies to all orders entered for the beneficial account(s) of such customer, regardless of whether such orders are entered on the Exchange or routed to another venue, and regardless of whether or not such orders are entered as Retail Orders or Retail Priority Orders.

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<sup>1</sup> See Securities Exchange Act Release No. 87200 (October 2, 2019), 84 FR 53788 (October 8, 2019) (SR-CboeEDGX-2019-012) ([Approval Order](#)).

<sup>2</sup> Based on a review of activity during third quarter 2019.

- **Counting of Orders for Retail Priority Order Purposes:** Paragraphs (a) and (b) of Interpretation and Policy .01 to Rule 11.9 set forth how orders should be counted for Retail Priority Order designation purposes with respect to parent/child orders and cancel/replace orders.
  - **“Parent”/”Child” Orders:** A “parent” order that is broken into multiple “child” orders 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, but which is housed with the customer, counts as one order even if the “child” orders are routed across multiple exchanges.
- **Cancel/Replace Orders:** Any order that cancels and replaces an existing order counts as a separate order; except that an order that cancels and replaces any “child” order resulting from a “parent” order that is broken into multiple “child” orders, does not count as a new order.

### Retail Member Organization Responsibilities

- **RMO Policies and Procedures:** Use of the Retail Priority Order designation by RMOs is optional. As adopted pursuant to Rule Filing SR-CboeEDGX-2019-012, Interpretation and Policy .02 to Rule 11.9 requires that those RMOs that elect to enter Retail Priority Orders must have reasonable policies and procedures in place to ensure that such orders are appropriately represented on the Exchange. Such policies and procedures should provide for a review of retail customers’ activity on at least a quarterly basis.
- **RMO Quarterly Reviews:** Retail Orders for any retail customer that had an average of more than 390 orders per day during *any month* of a calendar quarter would not be eligible to be entered as Retail Priority Orders for the next calendar quarter. RMOs 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 quarter.
- **Exchange Reviews and RMO Response:** While RMOs would only be required to review their accounts on a quarterly basis, if during a quarter the Exchange identifies a retail customer for which orders are being represented as Retail Priority Orders but that has averaged more than 390 orders per day during a month, the Exchange would notify the RMO, and the RMO would be required to change the manner in which it is representing the retail customer’s orders within five business days.

### Additional Information

Answers to some frequently asked questions regarding Retail Priority Orders are included below. For additional questions, please contact the Regulatory Interpretations team at [reginterps@cboe.com](mailto:reginterps@cboe.com) or (312) 786-8141. Technical details, including how to enter Retail Priority Orders on the Exchange, can also be found in the following [Trade Desk Notice](#).

## Frequently Asked Questions (FAQs)

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### Retail Orders / Retail Priority Order

**Question 1:** Does the SEC's approval of Rule Filing SR-CboeEDGX-2019-012 change the definition of the term "Retail Order" under the Exchange Rules?

*Answer:* No. The Commission's approval of Rule Filing SR-CboeEDGX-2019-012 does not change the definition of the term "Retail Order" in Exchange Rules. Rather, it further defines Retail Priority Order as a Retail Order that is entered on behalf of a person that does not place more than 390 equity orders per day on average during a calendar month for its own beneficial account(s).

**Question 2:** Who can enter Retail Priority Orders?

*Answer:* Only Retail Member Organizations or "RMOs" that are approved to enter Retail Orders pursuant to Rule 11.21 are permitted to enter Retail Priority Orders.

**Question 3:** How does a Member become an RMO?

*Answer:* A "Retail Member Organization" or "RMO" is a Member (or a division thereof) that has been approved by the Exchange under Exchange Rule 11.21 to submit Retail Orders. Pursuant to Exchange Rule 11.21(b), which describes the qualification and application process for becoming a Retail Member Organization, any member may qualify as a Retail Member Organization if it conducts a retail business or routes retail orders on behalf of another broker-dealer. The RMO application is available at: [https://cdn.cboe.com/resources/membership/EDGX\\_Retail\\_Member\\_Organization\\_Application.pdf](https://cdn.cboe.com/resources/membership/EDGX_Retail_Member_Organization_Application.pdf).

**Question 4:** What if a Member does not submit Retail Priority Orders?

*Answer:* Rule Filing SR-CboeEDGX-2019-012 only imposes new obligations on RMOs that elect to submit Retail Priority Orders that are eligible for order book priority. If a Member does not enter Retail Priority Orders, it does not have to comply with the requirements described in the Rule for entering such orders.

**Question 5:** How does an RMO that conducts a retail business comply with the rule?

*Answer:* Interpretation and Policy .02 to Rule 11.9 requires that RMOs that elect to enter Retail Priority Orders have reasonable policies and procedures in place to ensure that such orders are appropriately represented on the Exchange. An RMO that conducts a retail business would be required to review its retail customers' activity each calendar quarter to determine whether such customers are priority eligible. For example, an RMO could use an exception report to identify retail customers with trading activity that falls at/below or exceeds the 390 order per day threshold for entering Retail Priority Orders.

**Question 6:** My firm is an RMO that routes Retail Orders to the Exchange on behalf of another broker-dealer. Who is responsible for designating orders as Retail Priority Orders?

*Answer:* The RMO is responsible. As mentioned above, Interpretation and Policy .02 to Rule 11.9 requires that RMOs that enter Retail Priority Orders have reasonable policies and procedures in place to ensure that such orders are appropriately represented on the Exchange. If reasonably designed, such policies and procedures may allow the RMO to rely on the broker-dealer on whose behalf such orders are entered.

Please note that RMOs that enter Retail Priority Orders on the Exchange, but do not carry or clear those accounts, are required to take steps to track and identify orders they represent, but they are not expected to take action to track orders that they do not represent or of which they are otherwise unaware.

**Question 7:** Does an RMO that routes retail orders on behalf of another broker-dealer need to obtain an attestation from that broker-dealer related to the Retail Priority Order designation?

*Answer:* No, but it may be reasonable to do so. Pursuant to Rule 11.21(b)(6), an RMO that does not itself conduct a retail business but routes Retail Orders on behalf of another broker-dealer must obtain an annual written representation from each other broker-dealer that sends the RMO orders to be designated as Retail Orders that entry of such orders as Retail Orders will be in compliance with the requirements of Rule 11.21, and monitor whether Retail Order flow routed on behalf of such broker-dealers meets applicable requirements. A similar written representation and monitoring process is not required for RMOs electing to submit Retail Priority Orders, but would be appropriate for complying with the new requirements for Retail Priority Orders, provided that the broker-dealer on whose behalf the orders are entered has itself implemented policies and procedures consistent with the requirements for marking such orders as Retail Priority Orders.

### **Fees**

**Question 8:** Will Retail Orders that are not entered as Retail Priority Orders continue to benefit from fees and rebates currently applicable to those orders?

*Answer:* Yes. Although only Retail Priority Orders would be eligible for priority, Retail Orders – whether or not entered with the Retail Priority Order designation – will retain other benefits, including applicable fees and rebates currently applicable to such orders. Please see the [Cboe EDGX U.S. Equities Exchange Fee Schedule](#) for information.

### **Counting of Orders**

**Question 9:** Does the 390 average daily order requirement only apply to orders entered on the Exchange? (Updated 11/15/2019)

*Answer:* No. In determining the average daily number of orders entered on behalf of a retail customer, all orders for NMS stocks entered for the beneficial account(s) of such customer should be considered without regard to the venue where the order is routed. Orders for OTC securities are not contemplated by the Rule.

**Question 10:** Do only Retail Orders need to be counted? Do only Retail Priority Orders need to be counted?

*Answer:* No and no. As mentioned above, all orders entered for the beneficial account(s) of a retail customer should be counted in determining the average daily number of orders entered. This would include orders that are not entered as Retail Orders or Retail Priority Orders. Please note that although all orders must be counted for purposes of determining whether the 390 order per day threshold has been exceeded, any order entered as a Retail Priority Order must qualify as a Retail Order pursuant to Rule 11.21(a)(2).

**Question 11:** If a broker breaks a parent order into multiple smaller “child” orders, does the order still count as one order?

*Answer:* Yes. A “parent” order that is broken into multiple “child” orders 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, but which is housed with the customer, counts as one order even if the “child” orders are routed across multiple exchanges under paragraph (a) to Interpretation and Policy .01 to Rule 11.9.

*Example:* Customer A enters an order to buy 10,000 shares of SPY, and the broker-dealer breaks that order down into four orders of 2,500 shares each and routes those orders to EDGX, BZX, Nasdaq, and NYSE. Customer A’s order to buy 10,000 shares only counts as a single order.

The Exchange notes that if an algorithm is used to route a Retail Priority Order to the Exchange such order must meet the definition of “Retail Order” in Rule 11.21(a)(2). Consistent with current requirements applicable to all Retail Orders, if an RMO uses an algorithm to determine to send an existing Retail Priority Order to the Exchange, such order is acceptable and is not deemed to have originated from a trading algorithm strictly as a result of the brokerage firm’s algorithm, provided that the RMO assures that the Retail Priority Order meets the underlying rule requirements for Retail Orders, including that the routing algorithm does not change the terms of the order with respect to price or side of the market.<sup>3</sup>

**Question 12:** If a retail customer places an order with a broker to buy (sell) a security, which results in multiple “child” cancel/replaces, would each replace order need to be counted as a separate order?

*Answer:* No. Although the rule generally requires that any order that cancels and replaces an existing order be counted as a separate order, an order that cancels and replaces any “child” order resulting from a “parent” order that is broken into multiple “child” orders, does not count as a new order pursuant to paragraph (b) to Interpretation and Policy .01 to Rule 11.9.

**Question 13:** If a customer places a reserve order or similar order type that automatically replenishes, does each “replenish” need to be counted?

*Answer:* No. Under paragraph (a) of Interpretation and Policy .01 to Rule 11.9, a “parent” order that is broken into multiple “child” orders 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, but which is housed with the customer, counts as

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<sup>3</sup> Additionally, the Retail Order provision preventing changes to the terms of the order (e.g., price or side) is not meant to prevent an RMO from ensuring a better execution experience for the retail customer, such as by adding a limit to a Retail Order.

one order. Thus, if a customer places a reserve order that automatically replenishes, the original order counts as one order.

**Question 14:** Do orders routed by exchanges count as new orders?

*Answer:* No. Orders routed by exchanges (or exchange outbound routing brokers) in the course of fulfilling their obligations under Rule 611 of Regulation NMS do not need to be counted.

**Question 15:** If a parent order generates child orders that are pegged to the NBBO, do I have to count each cancel/replace of a child order?

*Answer:* No. Under paragraph (a) of Interpretation and Policy .01 to Rule 11.9, a “parent” order that is broken into multiple “child” orders 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, but which is housed with the customer, counts as one order. This rule applies to all parent/child orders, including orders pegged to the NBBO.

### **Review and Aggregation of Customer Accounts/Beneficial Ownership**

**Question 16:** How often must an RMO review orders for the Retail Priority Order designation?

*Answer:* RMOs are required to conduct at least quarterly reviews of retail customers’ monthly activity and make any appropriate changes to the way in which they represent orders within five days after the end of each calendar quarter.

**Question 17:** Is it possible for a customer whose orders are not eligible to be entered as Retail Priority Orders in one quarter to become eligible for such status in a subsequent quarter?

*Answer:* Yes. The Retail Priority Order designation is based on review of a customer’s past activity on at least a quarterly basis. Assuming that a customer’s activity is reviewed at the end of a calendar quarter, if a customer exceeds the 390 average daily order threshold during any month of the quarterly review period, the customer’s orders would not be eligible to be entered as Retail Priority Orders for the next quarter. Thereafter, however, if the customer places 390 orders or fewer per day on average each month during the next quarter, the customer’s orders would be eligible to be entered as Retail Priority Orders during the following quarter.

**Question 18:** If a retail customer places orders for multiple accounts, do the orders need to be aggregated?

*Answer:* Yes. All orders for accounts controlled by the same retail customer must be aggregated when determining whether or not the 390 average daily order threshold has been exceeded.

**Question 19:** Can a customer disaggregate/segregate trading activity for purposes of the 390 average daily order threshold calculation?

*Answer:* No. The rule requires the aggregation of all beneficial accounts of a retail customer when calculating the number of orders placed. A customer cannot maintain priority eligibility by spreading activity over multiple accounts. RMOs should also take note that the rule does not permit the

disaggregation/segregation of a person's or entity's account(s) when calculating the number of orders placed.

*Example:* Customer A is a retail customer that maintains three brokerage accounts with the RMO. All orders placed for the account(s) of Customer A must be aggregated when calculating the number of orders placed for Customer A.