

## OMB APPROVAL

OMB Number: 3235-0045  
 Estimated average burden  
 hours per response.....38

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 47	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4	File No.* SR - 2013 - * 013 Amendment No. (req. for Amendments *)
Filing by C2 Options Exchange, Incorporated Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934		
Initial * <input checked="" type="checkbox"/> Amendment * <input type="checkbox"/> Withdrawal <input type="checkbox"/>	Section 19(b)(2) * <input checked="" type="checkbox"/> Section 19(b)(3)(A) * <input type="checkbox"/> Section 19(b)(3)(B) * <input type="checkbox"/>	
Pilot <input type="checkbox"/> Extension of Time Period for Commission Action * <input type="checkbox"/> Date Expires *	Rule <input type="checkbox"/> 19b-4(f)(1) <input type="checkbox"/> 19b-4(f)(4) <input type="checkbox"/> 19b-4(f)(2) <input type="checkbox"/> 19b-4(f)(5) <input type="checkbox"/> 19b-4(f)(3) <input type="checkbox"/> 19b-4(f)(6)	
Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010 Section 806(e)(1) <input type="checkbox"/> Section 806(e)(2) <input type="checkbox"/>		Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934 Section 3C(b)(2) <input type="checkbox"/>
Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>	
<b>Description</b> Provide a brief description of the action (limit 250 characters, required when Initial is checked *). <div style="border: 1px solid black; padding: 5px; margin-top: 10px;">           The Exchange is proposing to modify its rules to address certain option order handling procedures and quoting obligations on the Exchange after the implementation of the market wide equity Plan to Address Extraordinary Market Volatility.         </div>		
<b>Contact Information</b> Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.		
First Name * Megan R. Last Name * Malone Title * Attorney E-mail * malone@cboe.com Telephone * (312) 786-7304 Fax (312) 786-7919		
<b>Signature</b> Pursuant to the requirements of the Securities Exchange Act of 1934, has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized. <div style="text-align: right;">(Title *)</div> <div style="display: flex; justify-content: space-between; margin-top: 10px;"> <div>           Date 03/06/2013            By Megan R. Malone            (Name *)         </div> <div style="border: 1px solid black; padding: 5px; width: 300px;">           Attorney  <div style="border: 1px solid black; padding: 2px; text-align: center; margin-top: 5px;">             Megan R. Malone, malone@cboe.com           </div> </div> </div> <p style="font-size: small; margin-top: 10px;">NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.</p>		

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFT website.

**Form 19b-4 Information \***

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies**

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

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Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

**Item 1.        Text of the Proposed Rule Change**

(a)        C2 Options Exchange, Incorporated (the “Exchange” or “C2”) proposes to modify its rules to address certain option order handling procedures and quoting obligations on the Exchange after the implementation of the market wide equity Plan to Address Extraordinary Market Volatility (the “Plan”). The text of the proposed rule change is provided below and in Exhibit 5.

(additions are underlined; deletions are [bracketed])

\* \* \* \* \*

**C2 Options Exchange, Incorporated****Rules**

\* \* \* \* \*

**Rule 6.10. Order Types Defined**

One or more of the following order types may be made available on a class-by-class basis. Certain order types may not be made available for all Exchange systems. The classes and/or systems for which the order types shall be available will be as provided in the Rules, as the context may indicate, or as otherwise specified via Regulatory Circular.

(a) - (k) No change.

**... Interpretations and Policies:**

**.01** Certain order types may be handled in a different manner when the underlying security is in a limit up-limit down state, as defined in Rule 6.39.

**A. Market Order.** A market order shall be returned by the System if the underlying security is in a limit up-limit down state. As an exception, market orders submitted to initiate an Automated Improvement Mechanism Auction will be accepted.

**B. Market-on-close order.** A market-on-close order shall not be elected if the underlying security is in a limit up-limit down state, as defined in Rule 6.39. If, near the conclusion of trading, the underlying security exits the limit up-limit down state, the system will attempt to re-evaluate, elect, and execute the order.

**C. Stop (stop-loss) order.** A stop order will not be triggered if the underlying security is in a limit up-limit down state. Such order will be held until the end of the limit up-limit

down state, at which point the order will become eligible to be triggered if the market for the particular option contract reaches the specified contract price.

\* \* \* \* \*

**Rule 6.11. Openings (and sometimes Closings)**

\* \* \* \* \*

*... Interpretations and Policies:*

\* \* \* \* \*

.03 Limit Up Limit Down States: If the underlying security for an option class is in a limit up- limit down state as defined in Rule 6.3A when the class moves to a Rotation Period, then all market orders in the system will be cancelled.

\* \* \* \* \*

**Rule 6.13. Complex Order Execution.**

(a) – (b) No change.

(c) Process for Complex Order RFR Auction: Prior to routing to the COB, eligible complex orders may be subject to an automated request for responses ("RFR") auction process.

(1) – (8) No change.

(9) Limit Up-Limit Down States. If during a COA of a market order, the underlying security of an option in a complex order of a COA-eligible order enters a limit up-limit down state, as defined in Rule 6.39, the COA will end upon the entering of the limit up-limit down state and the remaining portion of the order will be cancelled.

*... Interpretations and Policies:*

\* \* \* \* \*

**.06 Special Provisions Applicable to Stock-Options Orders:** Stock-option orders may be executed against other stock-option orders through the COB and COA. Stock-option orders will not be legged against the individual component legs, except as provided in paragraph (d) below.

(a) – (e) No change.

(f) Limit up-Limit Down States. When the underlying security on a Stock-option order is in a limit up-limit down state as defined in Rule 6.39, such order will only execute if the calculated stock price is within the permissible price bands as defined in the Plan. If the

calculated price is not within the permissible price bands, the Stock-option order will be cancelled.

\* \* \* \* \*

### **Rule 6.15. Obvious Error and Catastrophic Errors**

The Exchange shall either bust a transaction or adjust the execution price of a transaction that results from an Obvious Error or Catastrophic Error (collectively “Errors”) as provided in this Rule. [In limited circumstances, the Exchange may nullify transactions, pursuant to Interpretation and Policy .08 below.]

(a) – (d) No change.

#### ***... Interpretations and Policies:***

**.01 - .05** No change.

.08 For purposes of the obvious pricing error provision in paragraph (a)(1) of this Rule, executions will not be adjusted or nullified if they occurred while the underlying security was in a limit up-limit down state, as defined in Rule 6.39. Nothing in this provision shall prevent such executions to be reviewed on an Exchange motion. This provision will be on a one year pilot basis to coincide with the Plan as defined in Rule 6.39. The Exchange will provide the Commission with data and analysis during the duration of this pilot as requested.

\* \* \* \* \*

### **Rule 6.18. HAL**

This Rule governs the operation of the HAL system. HAL is a feature within the System that provides automated order handling in designated classes for qualifying electronic orders that are not automatically executed by the System.

(a) – (c) No change.

(d) *Early Termination of Exposure Period.* In addition to the receipt of a response to trade the entire exposed order at the NBBO or better, the exposure period will also terminate early under the following circumstances:

(i) – (iii) No change.

(iv) If during the exposure period of a market order the underlying security enters a limit up-limit down state, as defined in Rule 6.39, then the exposure period shall terminate and any unexecuted portion of the exposed order shall cancelled.

\* \* \* \* \*

### **Rule 6.39. Equity Market Plan to Address Extraordinary Market Volatility**

This Rule shall be in effect during a pilot period to coincide with the pilot period for the Regulation NMS Plan to Address Extraordinary Market Volatility (the “Limit Up-Limit Down Plan” or the “Plan”).

The Exchange shall modify option order processing during a limit up-limit down state. For purposes of this rule, a “limit up-limit down state” shall mean the period of time when the underlying security of an option enters a limit or straddle state as defined in the Plan.

**(a) Exchange Order Types.** The following order types will be handled specially during a limit up-limit down state: market orders, market-on-close orders, stop orders, and stock-option orders. Refer to Rule 6.10 and 6.13 for descriptions of how such orders will be handled during a limit up-limit down state.

**(b) Order Handling.** The following order handling features shall operate differently during a limit up-limit down state:

(1) *Openings.* Refer to Rule 6.11 for a description of how Openings will behave during a limit up-limit down state.

(2) *Hybrid Agency Liaison.* Refer to Rule 6.18 for a description of how HAL will operate during a limit up-limit down state.

(3) *Complex Order Request for Responses Auction.* Refer to Rule 6.13 for a description of how a complex order request for responses auction (referred to as “COA”) will operate during a limit up-limit down state.

(4) *Canceling/Replacing Orders.* If a request to replace a limit order with a market order is received while the underlying security is in a limit up-limit down state, then the market order and the original limit order will be returned.

**(c) Obvious Error.** Refer to Rule 6.15 for a description of how the Exchange will handle potential obvious error executions during a limit up-limit down state.

**(d) Market-Maker Quoting Obligations.** Subject to certain limitations specified in the rules identified below, the Exchange will not require Market-Makers to quote in series of options when the underlying security is in a limit up-limit down state. Market-Maker participation entitlements will continue to apply during a limit up-limit down state. For the particular limitations, refer to the specific Market-Maker category, and corresponding obligations.

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## **Rule 8.5. Obligations of Market-Makers**

(a) In registering as a Market-Maker, a Participant commits itself to various obligations. Transactions of a Market-Maker in its market making capacity must constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market, and Market-Makers should not make bids or offers or enter into transactions that are

inconsistent with such course of dealings. Ordinarily, Market Makers are expected to adhere to the following obligations:

- (1) During trading hours a Market-Maker must maintain a continuous two-sided market in 60% of the non-adjusted option series of each registered class that have a time to expiration of less than nine months. For purposes of this subparagraph, “continuous” means 90% of the time. If a technical failure or limitation of the System prevents a Market-Maker from maintaining, or from communicating to the Exchange, timely and accurate quotes in a series, the duration of such failure shall not be considered in determining whether that Market-Maker has satisfied the 90% quoting standard with respect to that series. An “adjusted option series” is an option series wherein, as a result of a corporate action by the issuer of the underlying security, one option contract in the series represents the delivery of other than 100 shares of underlying stock or Units. This obligation does not apply to intra-day add-on series on the day during which such series are added for trading. The Exchange may consider other exceptions to this obligation based on demonstrated legal or regulatory requirements or other mitigating circumstances.
  - (2) – (6) No changes.
- (b) – (d) No changes.

**... Interpretations and Policies:**

**.01 When the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, Market-Makers shall have no quoting obligations in the class.**

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**Rule 8.17. DPM Obligations**

(a) *Dealer Transactions.* Each DPM shall fulfill all of the obligations of a Market-Maker under the Rules, and shall satisfy each of the following requirements in respect of each of the securities allocated to the DPM. To the extent that there is any inconsistency between the

specific obligations of a DPM set forth in this Rule 8.17 and the general obligations of a Market-Maker under the Rules, this Rule 8.17 shall govern. Each DPM shall:

- (1) provide continuous quotes in at least the lesser of 99% of the non-adjusted option series (as defined in Rule 8.5(a)(1)) or 100% of the non-adjusted option series minus one call-put pair of each option class allocated to it, with the term “call-put pair” referring to one call and one put that cover the same underlying instrument and have the same expiration date and exercise price, and assure that its disseminated market quotations are accurate. This obligation does not apply to intra-day add-on series on the day during which such series are added for trading. For purposes of this subparagraph (a)(1), “continuous” means 90% of the time. If a technical failure or limitation of the System prevents a DPM from maintaining, or from communicating to the Exchange, timely and accurate quotes in a series, the duration of such failure shall not be

considered in determining whether that DPM has satisfied the 90% quoting standard with respect to the series;

\* \* \* \* \*

*... Interpretations and Policies:*

**.01** No changes.

**.02** When the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, DPMs shall have no quoting obligations in the class.

\* \* \* \* \*

### **Rule 8.19. Participation Entitlement of DPMs**

(a) No changes.

(b) The participation entitlement for DPMs shall operate as follows:

(1) *Generally.*

(A) To be entitled to a participation entitlement, the DPM must be quoting at the BBO.

(B) A DPM may not be allocated a total quantity greater than the quantity that the DPM is quoting at the BBO.

(C) The participation entitlement is based on the number of contracts remaining after all public customer orders in the Book at the BBO have been satisfied.

(2) *Participation Rates Applicable to DPMs.* The collective DPM participation entitlement shall be: 50% when there is one Market-Maker also quoting at the BBO and 40% when there are two or more Market-Makers also quoting at the BBO. If only the DPM is quoting at BBO (with no Market-Makers quoting at the BBO), the participation entitlement shall not be applicable and the allocation procedures under Rule 6.12 shall apply.

(3) *Participation Entitlement in Instances Where a Preferred Market-Maker Receives a Participation Entitlement Pursuant to Rule 8.13.* A DPM will not receive its participation entitlement set forth in this Rule in trades for which a Preferred Market Maker receives a participation entitlement pursuant to Rule 8.13, based on the order priority determined by the Exchange under Rule 6.12.

*... Interpretations and Policies:*

**.01 - .02** No changes.



.03 Where the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, DPMs shall have no quoting obligations in the class. However, a DPM may receive a participation entitlement in series of such a class when the underlying security has entered a limit up-limit down state if it elects to quote in such series and otherwise satisfies the requirements set forth in Rule 8.19(b).

\* \* \* \* \*

(b) Not applicable.

(c) Not applicable.

**Item 2. Procedures of the Self-Regulatory Organization**

(a) The Exchange's President (or designee officer) pursuant to delegated authority approved the proposed rule change on March 6, 2013.

(b) Please refer questions and comments on the proposed rule change to Joanne Moffic-Silver, (312) 786-7462, or Megan R. Malone, (312) 786-7304, C2 Options Exchange, Incorporated, 400 South LaSalle, Chicago, Illinois 60605.

**Item 3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change**

(a) Purpose

The Exchange is proposing to update Exchange rules to correspond with the Plan. Specifically, the Exchange is proposing to make proposed changes to Exchange Rules Rule 6.10, "Order Types Defined," 6.11, "Openings (and sometimes Closings)," Rule 6.13, "Complex Order Execution," Rule 6.15, "Obvious Error and Catastrophic Errors," Rule 6.18, "HAL," Rule 6.39, "Equity Market Plan to Address Extraordinary Market Volatility," Rule 8.5, "Obligations of Market-Makers, Rule 8.17, "DPM Obligations," and Rule 8.19, "DPM Participation Entitlements." The Exchange believes these modifications will protect investors because when an underlying security is in a limit or

straddle state (collectively referred to in this filing as a “limit up-limit down state”), there will not be a reliable price for the security to serve as a benchmark for the price of the option. In addition, the width of the markets might be compromised and, thus, the quality of execution for retail customers. The Plan is more fully explained below.

In an attempt to address extraordinary market volatility in NMS Stock, and, in particular, events like the severe volatility on May 6, 2010, the Exchange, in conjunction with the other national securities exchanges and the Financial Industry Regulatory Authority, Inc. (collectively, “Participants”) drafted the Plan pursuant to Rule 608 of Regulation NMS and under the Securities Exchange Act of 1934 (the “Act”).<sup>1</sup> The Plan is primarily designed to, among other things, address extraordinary market volatility in NMS stocks, protect investors, and promote fair and orderly markets. The Plan provides for market-wide limit up-limit down requirements that prevent trades in individual NMS Stocks from occurring outside of specified price bands, as defined in Section I(N) of the Plan. These requirements would be coupled with trading pauses, as defined in Section I(Y) of the Plan, to accommodate more fundamental price moves (as opposed to erroneous trades or monetary gaps of liquidity).

The Plan was filed on April 5, 2011 by the Participants for publication and comment.<sup>2</sup> The Participants requested the Commission approve the Plan as a one-year pilot. On May 24, 2012, the Participants filed an amendment to the Plan which clarified, among other things, the calculation of the reference price, as defined in Section I(T) of

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<sup>1</sup> See Securities Exchange Act Release No. 64547 (May 25, 2011), 76 FR 31647 (June 1, 2011)(File No. 4-631).

<sup>2</sup> Id.

the Plan, potential for order type exemption, and the creation of an Advisory Committee.<sup>3</sup> On May 31, 2012, the Commission approved the Plan, as amended, on a one-year pilot basis.<sup>4</sup>

Under the Plan, Participants are required to adopt certain rules in order to comply. Specifically, Section VI of the Plan sets forth the limit up-limit down requirements of the Plan, and in particular, that all trading centers in NMS Stocks, including both those operated by the Participants and those operated by member of Participants, shall establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trades at prices that are below the lower price band or above the upper price band for an NMS Stock, consistent with the Plan. Price Bands will be calculated by Securities Information Processors (“SIPs”) responsible for consolidation of information for an NMS Stock pursuant to Rule 603(b) of Regulation NMS under the Act. As proposed, and approved, the Plan would be implemented, as a one year pilot program, in two phases.<sup>5</sup> Phase I would become effective on April 8 and apply to Tier I NMS Stock per Appendix A of the Plan, and Phase II would become effective six months later, or earlier if announced by the SIPs 30 days prior, and would apply to all NMS Stocks.

Under the Plan, when one side of the market for an individual security is outside the applicable price band, the SIPs will be required to disseminate such National Best Bid or National Best Offer with an appropriate flag identifying it as non-executable. When

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<sup>3</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012), 77 FR 33498 (June 6, 2012) (File No. 4-631).

<sup>4</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012) 77 FR 33498 (June 6, 2012).

<sup>5</sup> Id.

the other side of the market reaches the applicable Price Band, the market for an individual security will enter a limit state. Trading for that security will exit the limit state if, within 15 seconds of entering the limit state, all limit state quotations were executed or cancelled. If the market does not exit a limit state within 15 seconds, then the primary listing exchange will declare a five-minute trading pause, which will be applicable to all markets trading the security.

Though the Plan is primarily designed for equity markets, the Exchange believes it will, indirectly, potentially impact the options markets as well. Thus, as stated above, the Exchange is proposing to amend its rules to ensure the option markets are not harmed as a result of the Plan's implementation. As such, the Exchange is proposing to amend various rules to reflect such changes. The Exchange believes such changes will protect participants, the Exchange and investors in general.

First, the Exchange is proposing to add Rule 6.39 to codify the changes throughout the Exchange's rules. The Exchange is proposing to add the title to "Equity Market Plan to Address Extraordinary Market Volatility" and add text. Rule 6.39 will define the Plan as it applies to the Exchange. In addition, the proposed rule change will describe the location of the other rule changes associated with the Plan. In essence, the proposed changes to Rule 6.39 will serve as a roadmap for the Exchange's universal changes due to the implementation of the Plan. The proposed rule changes will list changes to Exchange order types, order handling, obvious error, and market-maker quoting obligations that the Exchange is proposing to make in connection with the implementation of the Plan. These rule changes are more thoroughly described in various sections of the Exchange Rulebook, but having one place referencing all rules associated with the Plan will serve to better protect

investors by making the other rules easily located. The Exchange believes the proposed changes to Rule 6.39 will describe to Trading Permit Holders (“TPHs”), and other participants, where to find the changes associated with the Plan and will, thus, attempt to maintain a more orderly market.

Next, the Exchange is proposing to modify its opening procedures under Rule 6.11, “Openings (and sometimes Closings).” The Exchange is proposing to add an Interpretation and Policy .03 to clarify that if the underlying security for a class of options enters into a limit up-limit down state when the class moves to opening rotation, any market orders entered that trading day currently opening, prior to the opening of that class, will be cancelled. The Exchange believes this change is consistent with cancelling market orders in general during a limit up-limit down period as described in more detail below. The Exchange further believes this proposed change will help the Exchange to protect its TPHs from executing skewed orders during limit up-limit down periods.

Next, the Exchange is proposing to modify Exchange Rule 6.18, “HAL.” Exchange Rule 6.18 currently governs the operation of HAL, a feature within the System that provides automated order handling in designated classes trading on the System for qualifying orders that are not automatically executed by the System. The Exchange determines the eligible order size, eligible order types, eligible origin code (i.e. public customer orders, non-Market-Maker broker-dealer orders and Market-Maker broker-dealer orders), and classes in which HAL is activated.<sup>6</sup> When the Exchange receives a qualifying order that is marketable against the National Best Bid or Offer (“NBBO”) and/or the Exchange’s best

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<sup>6</sup> Rule 6.18.

bid or offer (“BBO”)<sup>7</sup>, HAL electronically exposes the order<sup>8</sup> at the NBBO price to allow Market-Makers appointed in that class, as well as all TPHs acting as agent for orders, at the top of the Exchange’s book in the relevant series (or all TPHs if allowed by the Exchange)<sup>9</sup> to step-up to the NBBO price.

Because the underlying security of the option in HAL affects the pricing of the eventually executed order, the Exchange is proposing to make changes to Rule 6.18 to reflect the implementation of the Plan. More specifically, the Exchange is proposing to amend Rule 6.18 to modify the behavior of HAL of a market order while the underlying security of the option is in a limit up-limit down state. If an underlying security shall enter a limit state while a HAL of a market order is in process, the auction will end early, upon the entering of the state, and any unexecuted portion of a market order shall be cancelled. The Exchange believes the proposed rule changes will best protect the TPH by ensuring it does not receive an executed order with an unanticipated price due to the change in the underlying security. In addition, by ending the auction early, the Exchange is providing a better chance for the TPH to get its order executed as it is in the TPH’s interest for an earlier execution versus a later one.

Next, the Exchange is proposing to modify how an electronic complex order request for responses (“RFR”) auction (“COA”) will operate while the underlying security of at least one of the options has entered a limit state. Exchange Rule 6.13(c)

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<sup>7</sup> HAL will not electronically expose the order if the Exchange’s quotation contains resting orders and does not contain sufficient Market-Maker quotation interest to satisfy the entire order.

<sup>8</sup> The duration of the exposure period may not exceed one second. Rule 6.18(c) describes the manner in which an exposed order is allocated under HAL, and Rule 6.18(d) lists the circumstances in which an exposure period would terminate early.

currently describes the general COA process. Generally, on a class-by-class basis, the Exchange may activate COA, which is a process by which eligible complex orders<sup>10</sup> are given an opportunity for price improvement before being booked in the electronic complex order book (“COB”) or once on a PAR workstation. On receipt of a COA-eligible order and request from a TPH representing the order that it be COA’d, the Exchange will send an RFR message to all TPHs who have elected to receive RFR messages.<sup>11</sup> Each Market-Maker with an appointment in the relevant option class and each TPH acting as agent for orders resting at the top of the COB in the relevant options series may then submit responses to the RFR message during the Response Time Interval.<sup>12</sup> The Exchange is proposing to add to the COA rule that if, during COA, the underlying security of a market order enters a limit up-limit down state, the COA will end upon the entering of that state and the remaining portion of the order will cancel.

Next, the Exchange is proposing to amend Exchange Rule 6.15 relating to the nullification and adjustment of options transactions. Under the current rule, an Obvious

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<sup>10</sup> An eligible complex order, referred to in Rule 6.13 as a “COA-eligible order,” means a complex order that, as determined by the Exchange on a class-by-class basis, is eligible for a COA considering the order’s marketability (defined as a number of ticks away from the current market), size, complex order type and complex order origin type (*i.e.* non-broker-dealer public customer, broker-dealers that are not Market-Makers or specialists on an options exchange, and/or Market-Makers or specialists on an options exchange). All determinations by the Exchange on COA-eligible order parameters are announced to Trading Permit Holders by Regulatory Circular. See Rule 6.18(c)(1)(B) and Interpretation and Policy .01 to Rule 6.18.

<sup>11</sup> See Rule 6.18(c)(3)(B). The RFR message will identify the component series, the size of the COA-eligible order and any contingencies, but will not identify the side of the market.

<sup>12</sup> See Rule 6.18(c)(3). A “Response Time Interval” means the period of time during which responses to the RFR may be entered, the length of which is determined by the Exchange on a class-by-class basis but may not exceed three seconds. See Rule 6.18(c)(3)(B).

Pricing Error occurs when the execution price of an electronic transaction is above or below the Theoretical Price for the series by a specified amount. For purpose of the rule, the “Theoretical Price” of an option series is currently defined, for series traded on at least one other options exchange, as the last national best bid price with respect to an erroneous sell transaction and the last national best offer price with respect to an erroneous buy transaction, just prior to the trade. If there are no quotes for comparison, designated help desk personnel<sup>13</sup> will determine the Theoretical Price.

Because the theoretical price may be unreliable due to the underlying security entering a limit state, the Exchange is proposing to amend the Exchange obvious error rules to provide that the Exchange may not nullify or adjust trades when the underlying security is in a limit up-limit down state. The Exchange is also proposing to add language specifying that transactions in options that overlay a security that is in a limit state may, however, be reviewed on an Exchange motion. The Exchange is also proposing to add language to specify that this provision will be on a one year pilot basis to coincide with the Plan. The Exchange will provide the Commission with data and analysis during the duration of this pilot as requested.<sup>14</sup> The Exchange believes this will best protect the market because it allows limit orders to be executed on the Exchange while the underlying securities are in limit states regardless of the calculated theoretical price.

In addition, the Exchange believes the proposed rule change would protect against TPHs getting a potential second look at transactions that happened during limit states that could be unfair to other participants. The proposed rule change would encourage added

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<sup>13</sup> See Exchange Rule 6.15(a)(3)(B).

<sup>14</sup> Finally, as an administrative change, the Exchange is proposing to eliminate a sentence referring to an Interpretation and Policy (.08) that no longer exists. The proposed provision will be the new Interpretation and Policy (.08) to Rule 6.15.



liquidity on the Exchange as the proposed changes would help to ensure that limit orders that are filled during a limit up-limit down state would have certainty of execution. By allowing the Exchange to continue to review such transactions on their own motion, the Exchange is further attempting to protect investors and maintain an orderly market. The Exchange believes that the combination of encouraging TPHs to participate on the market and allowing a safeguard to erroneous trades will provide the best solution during the pilot of the Plan.

Next, the Exchange is proposing to modify Rule 6.10 and 6.13 and, more specifically, how certain Exchange order types will be handled while the underlying security of such orders enters into a limit up-limit down state. The proposed rule change will, among other things, address how market orders<sup>15</sup>, market-on-close<sup>16</sup>, stop orders<sup>17</sup>, and stock option orders<sup>18</sup> will function on the Exchange upon the implementation of the Plan. More specifically, the Exchange is proposing to add language to clarify that: (a) market orders will be returned during limit up-limit down states, (b) market-on-close orders will not be elected if the underlying security is in a limit up-limit down state, (c) stop orders will be held while the underlying security is in a limit up-limit down state, and

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<sup>15</sup> See Exchange Rule 6.10 which defines a market order as “an order to buy or sell a stated number of options contracts at the best price available at the time of execution.”

<sup>16</sup> See Exchange Rule 6.10(c)(2) which defines a market-on-close order designation as an order “to be executed as close as possible to the closing bell, or during the closing rotation, and should be near to or at the closing price for the particular series of option contracts.

<sup>17</sup> See Exchange Rule 6.10(c)(3) which defines a stop order contingency to an order as one that “to buy or sell when the market for a particular option contract reaches a specified price on the Exchange.”

<sup>18</sup> See Exchange Rule 6.13(a)(2) which defines a stock-option order as “an order to buy or sell a stated number of units of an underlying stock or a security convertible into the underlying stock . . . coupled with the purchase or sale of options contract(s) on the opposite side of the market.”

(d) stock-option orders will only execute if the calculated stock price is within the permissible Price Bands.<sup>19</sup> In addition, during a limit up-limit down state, if a message is sent to replace a limit order with a market order, the resting limit order will be cancelled and the replaced market order will also be cancelled.

When a stock is in a limit or straddle state, while options trading will continue, there will not be a reliable price for a security to serve as a benchmark for the price of the option. In addition, without a reliable underlying stock price, there is an enhanced risk of errors and improper executions. With these concerns in mind, the Exchange believes that adding a level of certainty for TPHs will encourage participation on the Exchange whilst the underlying securities are in limit up-limit down states. Thus, the Exchange believes handling these certain orders in this way will best protect the investor after the implementation of the Plan by not allowing execution at unreasonable prices due to the shift in the stock prices.

Finally, the Exchange is proposing to eliminate all market maker obligations for options in which the underlying security is in a limit state while the underlying security is in the limit up-limit down state. Currently, Exchange Rules 8.5 and 8.17 impose certain obligations on Market-Makers and DPMs, respectively, including obligations to provide continuous quotes as follows<sup>20</sup>:

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<sup>19</sup> If the calculated price of a stock-option order is not within the permissible Price Bands, the stock-option order will be routed for manual handling.

<sup>20</sup> For purposes of Rules 8.5(a)(1), and 8.17(a)(1), “continuous” means 90% of the time. If a technical failure or limitation of the System prevents a Market-Maker from maintaining timely and accurate quotes in a series, the duration of such failure will not be included in the 90% determination.

- Rule 8.5 requires that Market-Makers provide a continuous two-sided market in 60% of the non-adjusted option series of the Market-Maker's appointed class that have a time to expiration of less than nine months;
- Rule 8.17(a)(1) requires DPMs to provide continuous quotes in at least the lesser of 99% or 100% minus one call-put pair<sup>21</sup> of the non-adjusted option series of each class allocated to it.

Exchange Rule 8.19 provides that DPMs generally will receive the participation entitlements in their assigned classes when quoting at the best price if they satisfy their obligations and other conditions set forth in the rules. Specifically, Rule 8.19 provides that the DPM participation entitlement will be 50% when there is one Market-Maker also quoting at the best price on the Exchange and 40% when there are two Market-Makers also quoting at the best price on the Exchange.<sup>22</sup>

Because prices may be skewed due to the underlying security being in a limit up-limit down state, the Exchange is proposing to eliminate all Market-Maker quoting obligations in series of options that the underlying security is currently in a limit up-limit down state. Because of the direct relationship between an options price and the price of the associated underlying security, the Exchange believes eliminating all Market-Maker obligations in connection with the implementation of the Plan is the most effective way to ensure the options markets will not be compromised. Because a bid or offer of an

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<sup>21</sup> See Rule 8.17(a)(1) which defines a "call-up pair" as "one call and one put that cover the same underlying instrument and have the same expiration date and exercise price."

<sup>22</sup> The participation entitlements of DPMs are based on the number of contracts remaining after all public customer orders in the book at the best price on the Exchange have been satisfied. Additionally, a DPM may not be allocated a total quantity greater than the quantity for which the DPM is quoting at the best price. See Rules 8.19(b)(1)(B) and (C).

underlying security may not be executable due to a limit or straddle state, the ability to hedge the purchase or sale of an option may not be possible or, in the least, is at risk. Because of this reason, the Exchange is anticipating that Exchange Market-Makers will be forced to change behaviors. In addition, the Exchange believes other options markets will be implementing similar changes. In an effort to protect the investors in the options market while the underlying security is in a limit up-limit down state, the Exchange believes that eliminating quoting obligations is the more effective way for this protection.

The Exchange, however, is proposing that Market-Makers may still receive participation entitlements pursuant to the proposed rules in all series in their assigned classes in which they are quoting, even in series in which they are not required to provide continuous electronic quotes under the Exchange Rules. Market-Makers already receive participation entitlements in series they are not required to quote. For example, a DPM is currently required to provide continuous quotes in at least 99% of the non-adjusted option series or 100% of the non-adjusted series minus one call-put pair of each option class allocated to it for 90% of the trading day.<sup>23</sup> If the DPM elects to quote in 100% of the non-adjusted series in an option class allocated to it, it will receive a participation entitlement in all of those series when quoting at the best price, including the 1% of the series in which it is not required to quote in. Thus, under the proposed rule change, the market would continue to function as it does now. The Exchange believes this benefit is appropriate, as it incentivizes Market-Makers to quote in as many series as possible in their appointed classes, even those series in which the Rules do not require them to continuously quote. Thus, under the proposed rule change, the market would continue to

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<sup>23</sup> See Rule 8.17(a).

function as it does now with respect to how entitlements are allocated to Market-Makers. The Exchange believes this benefit is appropriate, as it incentivizes Market-Makers to quote in as many series as possible in their appointed classes, even those series in which the underlying security has entered into a limit up-limit down state. The Exchange is attempting to better encourage Market-Makers to quote though they will not be obligated to. If they do choose to quote, the Exchange believes they should be entitled to receive the Entitlement for such quoting as appropriate.

The Exchange believes the combination of these modifications will protect investors because when an underlying security is in a limit or straddle state, there will not be a reliable price for the security to serve as a benchmark for the price of the option. In addition, the width of the markets might be compromised and, thus, the quality of execution for retail customers. At the same time, the Exchange believes the proposed rule change will create more certainty on the options markets encouraging more investors to participate despite the changes associated with the Plan.

(b) Statutory Basis

The Exchange believes the proposed rule change is consistent with the Securities Exchange Act of 1934 (the “Act”) and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.<sup>24</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>25</sup> 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,

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<sup>24</sup> 15 U.S.C. 78f(b).

<sup>25</sup> 15 U.S.C. 78f(b)(5).

clearing, settling, processing information with respect to, and facilitation 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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>26</sup> requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes the proposed changes will be in accordance with the Act as they are merely intended to ensure the options markets will continue to remain just and equitable with the implementation of the Plan which is intended to reduce the negative impacts of a sudden, unanticipated price movement in NMS stocks. The proposed rule changes would promote this intention in the options markets while protecting investors participating there. In addition, similar rule changes will be adopted by other markets in the national market system in a coordinated manner promoting the public interest. Creating a more orderly market will promote just and equitable principles of trade by allowing investors to feel more secure in their participation in the national market system after the implementation of the Plan.

**Item 4. Self-Regulatory Organization's Statement on Burden on Competition**

C2 does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Specifically, the Exchange believes the proposed changes will not impose any burden on intramarket competition because it applies to all TPHs equally. The Exchange does not believe the proposed changes will impose any burden on intermarket competition as the changes are merely being made to protect investors with the implementation of the Plan.

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<sup>26</sup> Id.

In addition, the propose changes will provide certainty of treatment and execution of options orders during periods of extraordinary market volatility.

**Item 5. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others**

The Exchange neither solicited nor received comments on the proposed rule change.

**Item 6. Extension of Time Period for Commission Action**

C2 does not consent to an extension of the time period for Securities and Exchange Commission (the “Commission”) action on the proposed rule change specified in Section 19(b)(2) of the Act.<sup>27</sup>

**Item 7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)**

- (a) Not applicable.
- (b) Not applicable.
- (c) Not applicable.

(d) The proposed rule change is filed for accelerated effectiveness pursuant to Section 19(b)(2) of the Act.<sup>28</sup> The Exchange requests that the Commission approve the proposed rule change on an accelerated basis pursuant to Section 19(b)(2) of the Act so that it may be operative as soon as practicable. The Exchange believes there is good cause for accelerated approval of the proposed rule change as the Plan will become operative on April 8, 2013. Accelerated approval of the proposed rule change is in the public interest because

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<sup>27</sup> 15 U.S.C. 78s(b)(2).

<sup>28</sup> 15 U.S.C. 78s(b)(2).

it will assure that the Exchange will have rules that comply with the Plan and the other changes to the various national securities exchanges.

**Item 8.        Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

The proposed rule change is not based on a rule either of another self-regulatory organization or of the Commission.

**Item 9.        Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act**

Not applicable.

**Item 10.       Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act**

Not applicable.

**Item 11.       Exhibits**

Exhibit 1.       Completed Notice of Proposed Rule Change for publication in the Federal Register.

Exhibit 5.       Proposed rule text if not included under Item 1(a).



EXHIBIT 1

**SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34- ; File No. SR-C2-2013-013]

[Insert date]

Self-Regulatory Organizations; C2 Options Exchange, Incorporated; Notice of Filing of a Proposed Rule Change Relating to the Regulation NMS Plan to Address Extraordinary Market Volatility

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 [insert date], C2 Options Exchange, Incorporated (the “Exchange” or “C2”) filed with the Securities and Exchange Commission (the “Commission”) the proposed rule change as described in Items I, II, and III 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 modify its rules to address certain option order handling procedures and quoting obligations on the Exchange after the implementation of the market wide equity Plan to Address Extraordinary Market Volatility (the “Plan”).

The text of the proposed rule change is available on the Exchange’s website (<http://www.c2exchange.com/Legal/>), at the Exchange’s Office of the Secretary, and at the Commission’s Public Reference Room.

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

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

**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 proposing to update Exchange rules to correspond with the Plan. Specifically, the Exchange is proposing to make proposed changes to Exchange Rules Rule 6.10, "Order Types Defined," 6.11, "Openings (and sometimes Closings)," Rule 6.13, "Complex Order Execution," Rule 6.15, "Obvious Error and Catastrophic Errors," Rule 6.18, "HAL," Rule 6.39, "Equity Market Plan to Address Extraordinary Market Volatility," Rule 8.5, "Obligations of Market-Makers, Rule 8.17, "DPM Obligations," and Rule 8.19, "DPM Participation Entitlements." The Exchange believes these modifications will protect investors because when an underlying security is in a limit or straddle state (collectively referred to in this filing as a "limit up-limit down state"), there will not be a reliable price for the security to serve as a benchmark for the price of the option. In addition, the width of the markets might be compromised and, thus, the quality of execution for retail customers. The Plan is more fully explained below.

In an attempt to address extraordinary market volatility in NMS Stock, and, in particular, events like the severe volatility on May 6, 2010, the Exchange, in conjunction with the other national securities exchanges and the Financial Industry Regulatory

Authority, Inc. (collectively, “Participants”) drafted the Plan pursuant to Rule 608 of Regulation NMS and under the Securities Exchange Act of 1934 (the “Act”).<sup>3</sup> The Plan is primarily designed to, among other things, address extraordinary market volatility in NMS stocks, protect investors, and promote fair and orderly markets. The Plan provides for market-wide limit up-limit down requirements that prevent trades in individual NMS Stocks from occurring outside of specified price bands, as defined in Section I(N) of the Plan. These requirements would be coupled with trading pauses, as defined in Section I(Y) of the Plan, to accommodate more fundamental price moves (as opposed to erroneous trades or monetary gaps of liquidity).

The Plan was filed on April 5, 2011 by the Participants for publication and comment.<sup>4</sup> The Participants requested the Commission approve the Plan as a one-year pilot. On May 24, 2012, the Participants filed an amendment to the Plan which clarified, among other things, the calculation of the reference price, as defined in Section I(T) of the Plan, potential for order type exemption, and the creation of an Advisory Committee.<sup>5</sup> On May 31, 2012, the Commission approved the Plan, as amended, on a one-year pilot basis.<sup>6</sup>

Under the Plan, Participants are required to adopt certain rules in order to comply. Specifically, Section VI of the Plan sets forth the limit up-limit down requirements of the Plan, and in particular, that all trading centers in NMS Stocks, including both those operated by the Participants and those operated by member of Participants, shall

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<sup>3</sup> See Securities Exchange Act Release No. 64547 (May 25, 2011), 76 FR 31647 (June 1, 2011)(File No. 4-631).

<sup>4</sup> Id.

<sup>5</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012), 77 FR 33498 (June 6, 2012) (File No. 4-631).

<sup>6</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012) 77 FR 33498 (June 6, 2012).

establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trades at prices that are below the lower price band or above the upper price band for an NMS Stock, consistent with the Plan. Price Bands will be calculated by Securities Information Processors (“SIPs”) responsible for consolidation of information for an NMS Stock pursuant to Rule 603(b) of Regulation NMS under the Act. As proposed, and approved, the Plan would be implemented, as a one year pilot program, in two phases.<sup>7</sup> Phase I would become effective on April 8 and apply to Tier I NMS Stock per Appendix A of the Plan, and Phase II would become effective six months later, or earlier if announced by the SIPs 30 days prior, and would apply to all NMS Stocks.

Under the Plan, when one side of the market for an individual security is outside the applicable price band, the SIPs will be required to disseminate such National Best Bid or National Best Offer with an appropriate flag identifying it as non-executable. When the other side of the market reaches the applicable Price Band, the market for an individual security will enter a limit state. Trading for that security will exit the limit state if, within 15 seconds of entering the limit state, all limit state quotations were executed or cancelled. If the market does not exit a limit state within 15 seconds, then the primary listing exchange will declare a five-minute trading pause, which will be applicable to all markets trading the security.

Though the Plan is primarily designed for equity markets, the Exchange believes it will, indirectly, potentially impact the options markets as well. Thus, as stated above, the Exchange is proposing to amend its rules to ensure the option markets are not harmed as a result of the Plan’s implementation. As such, the Exchange is proposing to amend various

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<sup>7</sup> Id.

rules to reflect such changes. The Exchange believes such changes will protect participants, the Exchange and investors in general.

First, the Exchange is proposing to add Rule 6.39 to codify the changes throughout the Exchange's rules. The Exchange is proposing to add the title to "Equity Market Plan to Address Extraordinary Market Volatility" and add text. Rule 6.39 will define the Plan as it applies to the Exchange. In addition, the proposed rule change will describe the location of the other rule changes associated with the Plan. In essence, the proposed changes to Rule 6.39 will serve as a roadmap for the Exchange's universal changes due to the implementation of the Plan. The proposed rule changes will list changes to Exchange order types, order handling, obvious error, and market-maker quoting obligations that the Exchange is proposing to make in connection with the implementation of the Plan. These rule changes are more thoroughly described in various sections of the Exchange Rulebook, but having one place referencing all rules associated with the Plan will serve to better protect investors by making the other rules easily located. The Exchange believes the proposed changes to Rule 6.39 will describe to Trading Permit Holders ("TPHs"), and other participants, where to find the changes associated with the Plan and will, thus, attempt to maintain a more orderly market.

Next, the Exchange is proposing to modify its opening procedures under Rule 6.11, "Openings (and sometimes Closings)." The Exchange is proposing to add an Interpretation and Policy .03 to clarify that if the underlying security for a class of options enters into a limit up-limit down state when the class moves to opening rotation, any market orders entered that trading day currently opening, prior to the opening of that class, will be cancelled. The Exchange believes this change is consistent with cancelling market orders in

general during a limit up-limit down period as described in more detail below. The Exchange further believes this proposed change will help the Exchange to protect its TPHs from executing skewed orders during limit up-limit down periods.

Next, the Exchange is proposing to modify Exchange Rule 6.18, “HAL.” Exchange Rule 6.18 currently governs the operation of HAL, a feature within the System that provides automated order handling in designated classes trading on the System for qualifying orders that are not automatically executed by the System. The Exchange determines the eligible order size, eligible order types, eligible origin code (i.e. public customer orders, non-Market-Maker broker-dealer orders and Market-Maker broker-dealer orders), and classes in which HAL is activated.<sup>8</sup> When the Exchange receives a qualifying order that is marketable against the National Best Bid or Offer (“NBBO”) and/or the Exchange’s best bid or offer (“BBO”),<sup>9</sup> HAL electronically exposes the order<sup>10</sup> at the NBBO price to allow Market-Makers appointed in that class, as well as all TPHs acting as agent for orders, at the top of the Exchange’s book in the relevant series (or all TPHs if allowed by the Exchange)<sup>11</sup> to step-up to the NBBO price.

Because the underlying security of the option in HAL affects the pricing of the eventually executed order, the Exchange is proposing to make changes to Rule 6.18 to reflect the implementation of the Plan. More specifically, the Exchange is proposing to amend Rule 6.18 to modify the behavior of HAL of a market order while the underlying security of the option is in a limit up-limit down state. If an underlying security shall

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<sup>8</sup> Rule 6.18.

<sup>9</sup> HAL will not electronically expose the order if the Exchange’s quotation contains resting orders and does not contain sufficient Market-Maker quotation interest to satisfy the entire order.

<sup>10</sup> The duration of the exposure period may not exceed one second. Rule 6.18(c) describes the manner in which an exposed order is allocated under HAL, and Rule 6.18(d) lists the circumstances in which an exposure period would terminate early.

enter a limit state while a HAL of a market order is in process, the auction will end early, upon the entering of the state, and any unexecuted portion of a market order shall be cancelled. The Exchange believes the proposed rule changes will best protect the TPH by ensuring it does not receive an executed order with an unanticipated price due to the change in the underlying security. In addition, by ending the auction early, the Exchange is providing a better chance for the TPH to get its order executed as it is in the TPH's interest for an earlier execution versus a later one.

Next, the Exchange is proposing to modify how an electronic complex order request for responses ("RFR") auction ("COA") will operate while the underlying security of at least one of the options has entered a limit state. Exchange Rule 6.13(c) currently describes the general COA process. Generally, on a class-by-class basis, the Exchange may activate COA, which is a process by which eligible complex orders<sup>12</sup> are given an opportunity for price improvement before being booked in the electronic complex order book ("COB") or once on a PAR workstation. On receipt of a COA-eligible order and request from a TPH representing the order that it be COA'd, the Exchange will send an RFR message to all TPHs who have elected to receive RFR messages.<sup>13</sup> Each Market-Maker with an appointment in the relevant option class and each TPH acting as agent for orders resting at the top of the COB in the relevant options series may then submit responses to the RFR message during the Response Time

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<sup>12</sup> An eligible complex order, referred to in Rule 6.13 as a "COA-eligible order," means a complex order that, as determined by the Exchange on a class-by-class basis, is eligible for a COA considering the order's marketability (defined as a number of ticks away from the current market), size, complex order type and complex order origin type (*i.e.* non-broker-dealer public customer, broker-dealers that are not Market-Makers or specialists on an options exchange, and/or Market-Makers or specialists on an options exchange). All determinations by the Exchange on COA-eligible order parameters are announced to Trading Permit Holders by Regulatory Circular. See Rule 6.18(c)(1)(B) and Interpretation and Policy .01 to Rule 6.18.

<sup>13</sup> See Rule 6.18(c)(3)(B). The RFR message will identify the component series, the size of the COA-eligible order and any contingencies, but will not identify the side of the market.

Interval.<sup>14</sup> The Exchange is proposing to add to the COA rule that if, during COA, the underlying security of a market order enters a limit up-limit down state, the COA will end upon the entering of that state and the remaining portion of the order will cancel.

Next, the Exchange is proposing to amend Exchange Rule 6.15 relating to the nullification and adjustment of options transactions. Under the current rule, an Obvious Pricing Error occurs when the execution price of an electronic transaction is above or below the Theoretical Price for the series by a specified amount. For purpose of the rule, the “Theoretical Price” of an option series is currently defined, for series traded on at least one other options exchange, as the last national best bid price with respect to an erroneous sell transaction and the last national best offer price with respect to an erroneous buy transaction, just prior to the trade. If there are no quotes for comparison, designated help desk personnel<sup>15</sup> will determine the Theoretical Price.

Because the theoretical price may be unreliable due to the underlying security entering a limit state, the Exchange is proposing to amend the Exchange obvious error rules to provide that the Exchange may not nullify or adjust trades when the underlying security is in a limit up-limit down state. The Exchange is also proposing to add language specifying that transactions in options that overlay a security that is in a limit state may, however, be reviewed on an Exchange motion. The Exchange is also proposing to add language to specify that this provision will be on a one year pilot basis to coincide with the Plan. The Exchange will provide the Commission with data and analysis during the

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<sup>14</sup> See Rule 6.18(c)(3). A “Response Time Interval” means the period of time during which responses to the RFR may be entered, the length of which is determined by the Exchange on a class-by-class basis but may not exceed three seconds. See Rule 6.18(c)(3)(B).

<sup>15</sup> See Exchange Rule 6.15(a)(3)(B).



duration of this pilot as requested.<sup>16</sup> The Exchange believes this will best protect the market because it allows limit orders to be executed on the Exchange while the underlying securities are in limit states regardless of the calculated theoretical price.

In addition, the Exchange believes the proposed rule change would protect against TPHs getting a potential second look at transactions that happened during limit states that could be unfair to other participants. The proposed rule change would encourage added liquidity on the Exchange as the proposed changes would help to ensure that limit orders that are filled during a limit up-limit down state would have certainty of execution. By allowing the Exchange to continue to review such transactions on their own motion, the Exchange is further attempting to protect investors and maintain an orderly market. The Exchange believes that the combination of encouraging TPHs to participate on the market and allowing a safeguard to erroneous trades will provide the best solution during the pilot of the Plan.

Next, the Exchange is proposing to modify Rule 6.10 and 6.13 and, more specifically, how certain Exchange order types will be handled while the underlying security of such orders enters into a limit up-limit down state. The proposed rule change will, among other things, address how market orders<sup>17</sup>, market-on-close<sup>18</sup>, stop orders<sup>19</sup>, and stock option orders<sup>20</sup> will function on the Exchange upon the implementation of the

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<sup>16</sup> Finally, as an administrative change, the Exchange is proposing to eliminate a sentence referring to an Interpretation and Policy (.08) that no longer exists. The proposed provision will be the new Interpretation and Policy (.08) to Rule 6.15.

<sup>17</sup> See Exchange Rule 6.10 which defines a market order as “an order to buy or sell a stated number of options contracts at the best price available at the time of execution.”

<sup>18</sup> See Exchange Rule 6.10(c)(2) which defines a market-on-close order designation as an order “to be executed as close as possible to the closing bell, or during the closing rotation, and should be near to or at the closing price for the particular series of option contracts.

<sup>19</sup> See Exchange Rule 6.10(c)(3) which defines a stop order contingency to an order as one that “to buy or sell when the market for a particular option contract reaches a specified price on the Exchange.”

<sup>20</sup> See Exchange Rule 6.13(a)(2) which defines a stock-option order as “an order to buy or sell a

Plan. More specifically, the Exchange is proposing to add language to clarify that: (a) market orders will be returned during limit up-limit down states, (b) market-on-close orders will not be elected if the underlying security is in a limit up-limit down state, (c) stop orders will be held while the underlying security is in a limit up-limit down state, and (d) stock-option orders will only execute if the calculated stock price is within the permissible Price Bands.<sup>21</sup> In addition, during a limit up-limit down state, if a message is sent to replace a limit order with a market order, the resting limit order will be cancelled and the replaced market order will also be cancelled.

When a stock is in a limit or straddle state, while options trading will continue, there will not be a reliable price for a security to serve as a benchmark for the price of the option. In addition, without a reliable underlying stock price, there is an enhanced risk of errors and improper executions. With these concerns in mind, the Exchange believes that adding a level of certainty for TPHs will encourage participation on the Exchange whilst the underlying securities are in limit up-limit down states. Thus, the Exchange believes handling these certain orders in this way will best protect the investor after the implementation of the Plan by not allowing execution at unreasonable prices due to the shift in the stock prices.

Finally, the Exchange is proposing to eliminate all market maker obligations for options in which the underlying security is in a limit state while the underlying security is in the limit up-limit down state. Currently, Exchange Rules 8.5 and 8.17 impose

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stated number of units of an underlying stock or a security convertible into the underlying stock . . . coupled with the purchase or sale of options contract(s) on the opposite side of the market.”

<sup>21</sup> If the calculated price of a stock-option order is not within the permissible Price Bands, the stock-option order will be routed for manual handling.

certain obligations on Market-Makers and DPMs, respectively, including obligations to provide continuous quotes as follows<sup>22</sup>:

- Rule 8.5 requires that Market-Makers provide a continuous two-sided market in 60% of the non-adjusted option series of the Market-Maker's appointed class that have a time to expiration of less than nine months;
- Rule 8.17(a)(1) requires DPMs to provide continuous quotes in at least the lesser of 99% or 100% minus one call-put pair<sup>23</sup> of the non-adjusted option series of each class allocated to it.

Exchange Rule 8.19 provides that DPMs generally will receive the participation entitlements in their assigned classes when quoting at the best price if they satisfy their obligations and other conditions set forth in the rules. Specifically, Rule 8.19 provides that the DPM participation entitlement will be 50% when there is one Market-Maker also quoting at the best price on the Exchange and 40% when there are two Market-Makers also quoting at the best price on the Exchange.<sup>24</sup>

Because prices may be skewed due to the underlying security being in a limit up-limit down state, the Exchange is proposing to eliminate all Market-Maker quoting obligations in series of options that the underlying security is currently in a limit up-limit down state. Because of the direct relationship between an options price and the price of the associated underlying security, the Exchange believes eliminating all Market-Maker

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<sup>22</sup> For purposes of Rules 8.5(a)(1), and 8.17(a)(1), "continuous" means 90% of the time. If a technical failure of limitation of the System prevents a Market-Maker from maintaining timely and accurate quotes in a series, the duration of such failure will not be included in the 90% determination.

<sup>23</sup> See Rule 8.17(a)(1) which defines a "call-up pair" as "one call and one put that cover the same underlying instrument and have the same expiration date and exercise price."

<sup>24</sup> The participation entitlements of DPMs are based on the number of contracts remaining after all public customer orders in the book at the best price on the Exchange have been satisfied. Additionally, a DPM may not be allocated a total quantity greater than the quantity for which the DPM is quoting at the best price. See Rules 8.19(b)(1)(B) and (C).

obligations in connection with the implementation of the Plan is the most effective way to ensure the options markets will not be compromised. Because a bid or offer of an underlying security may not be executable due to a limit or straddle state, the ability to hedge the purchase or sale of an option may not be possible or, in the least, is at risk. Because of this reason, the Exchange is anticipating that Exchange Market-Makers will be forced to change behaviors. In addition, the Exchange believes other options markets will be implementing similar changes. In an effort to protect the investors in the options market while the underlying security is in a limit up-limit down state, the Exchange believes that eliminating quoting obligations is the more effective way for this protection.

The Exchange, however, is proposing that Market-Makers may still receive participation entitlements pursuant to the proposed rules in all series in their assigned classes in which they are quoting, even in series in which they are not required to provide continuous electronic quotes under the Exchange Rules. Market-Makers already receive participation entitlements in series they are not required to quote. For example, a DPM is currently required to provide continuous quotes in at least 99% of the non-adjusted option series or 100% of the non-adjusted series minus one call-put pair of each option class allocated to it for 90% of the trading day.<sup>25</sup> If the DPM elects to quote in 100% of the non-adjusted series in an option class allocated to it, it will receive a participation entitlement in all of those series when quoting at the best price, including the 1% of the series in which it is not required to quote in. Thus, under the proposed rule change, the market would continue to function as it does now. The Exchange believes this benefit is appropriate, as it incentivizes Market-Makers to quote in as many series as possible in their appointed classes, even those series in which the Rules do not require them to

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<sup>25</sup> See Rule 8.17(a).

continuously quote. Thus, under the proposed rule change, the market would continue to function as it does now with respect to how entitlements are allocated to Market-Makers. The Exchange believes this benefit is appropriate, as it incentivizes Market-Makers to quote in as many series as possible in their appointed classes, even those series in which the underlying security has entered into a limit up-limit down state. The Exchange is attempting to better encourage Market-Makers to quote though they will not be obligated to. If they do choose to quote, the Exchange believes they should be entitled to receive the Entitlement for such quoting as appropriate.

The Exchange believes the combination of these modifications will protect investors because when an underlying security is in a limit or straddle state, there will not be a reliable price for the security to serve as a benchmark for the price of the option. In addition, the width of the markets might be compromised and, thus, the quality of execution for retail customers. At the same time, the Exchange believes the proposed rule change will create more certainty on the options markets encouraging more investors to participate despite the changes associated with the Plan.

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Securities Exchange Act of 1934 (the “Act”) and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.<sup>26</sup> Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>27</sup> requirements that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles

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<sup>26</sup> 15 U.S.C. 78f(b).

<sup>27</sup> 15 U.S.C. 78f(b)(5).

of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitation 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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)<sup>28</sup> requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes the proposed changes will be in accordance with the Act as they are merely intended to ensure the options markets will continue to remain just and equitable with the implementation of the Plan which is intended to reduce the negative impacts of a sudden, unanticipated price movement in NMS stocks. The proposed rule changes would promote this intention in the options markets while protecting investors participating there. In addition, similar rule changes will be adopted by other markets in the national market system in a coordinated manner promoting the public interest. Creating a more orderly market will promote just and equitable principles of trade by allowing investors to feel more secure in their participation in the national market system after the implementation of the Plan.

B. Self-Regulatory Organization's Statement on Burden on Competition

C2 does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Specifically, the Exchange believes the proposed changes will not impose any burden on intramarket competition because it applies to all TPHs equally. The Exchange does not believe the proposed changes will impose any burden on intermarket competition as the

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<sup>28</sup>

Id.

changes are merely being made to protect investors with the implementation of the Plan. In addition, the propose changes will provide certainty of treatment and execution of options orders during periods of extraordinary market volatility.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Exchange neither solicited nor received comments on the proposed rule change.

**III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

- A. by order approve or disapprove such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be 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 e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-C2-2013-013 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-C2-2013-013. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, D.C. 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-C2-2013-013 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>29</sup>

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<sup>29</sup> 17 CFR 200.30-3(a)(12).



Secretary

## EXHIBIT 5

(additions are underlined; deletions are [bracketed])

\* \* \* \* \*

**C2 Options Exchange, Incorporated****Rules**

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**Rule 6.10. Order Types Defined**

One or more of the following order types may be made available on a class-by-class basis. Certain order types may not be made available for all Exchange systems. The classes and/or systems for which the order types shall be available will be as provided in the Rules, as the context may indicate, or as otherwise specified via Regulatory Circular.

(a) - (k) No change.

. . . Interpretations and Policies:

.01 Certain order types may be handled in a different manner when the underlying security is in a limit up-limit down state, as defined in Rule 6.39.

A. Market Order. A market order shall be returned by the System if the underlying security is in a limit up-limit down state. As an exception, market orders submitted to initiate an Automated Improvement Mechanism Auction will be accepted.

B. Market-on-close order. A market-on-close order shall not be elected if the underlying security is in a limit up-limit down state, as defined in Rule 6.39. If, near the conclusion of trading, the underlying security exits the limit up-limit down state, the system will attempt to re-evaluate, elect, and execute the order.

C. Stop (stop-loss) order. A stop order will not be triggered if the underlying security is in a limit up-limit down state. Such order will be held until the end of the limit up-limit down state, at which point the order will become eligible to be triggered if the market for the particular option contract reaches the specified contract price.

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**Rule 6.11. Openings (and sometimes Closings)**

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. . . Interpretations and Policies:

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.03 Limit Up Limit Down States: If the underlying security for an option class is in a limit up- limit down state as defined in Rule 6.3A when the class moves to a Rotation Period, then all market orders in the system will be cancelled.

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### **Rule 6.13. Complex Order Execution.**

(a) – (b) No change.

(c) Process for Complex Order RFR Auction: Prior to routing to the COB, eligible complex orders may be subject to an automated request for responses ("RFR") auction process.

(1) – (8) No change.

(9) Limit Up-Limit Down States. If during a COA of a market order, the underlying security of an option in a complex order of a COA-eligible order enters a limit up-limit down state, as defined in Rule 6.39, the COA will end upon the entering of the limit up-limit down state and the remaining portion of the order will be cancelled.

***... Interpretations and Policies:***

\* \* \* \* \*

**.06 Special Provisions Applicable to Stock-Options Orders:** Stock-option orders may be executed against other stock-option orders through the COB and COA. Stock-option orders will not be legged against the individual component legs, except as provided in paragraph (d) below.

(a) – (e) No change.

(f) Limit up-Limit Down States. When the underlying security on a Stock-option order is in a limit up-limit down state as defined in Rule 6.39, such order will only execute if the calculated stock price is within the permissible price bands as defined in the Plan. If the calculated price is not within the permissible price bands, the Stock-option order will be cancelled.

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### **Rule 6.15. Obvious Error and Catastrophic Errors**

The Exchange shall either bust a transaction or adjust the execution price of a transaction that results from an Obvious Error or Catastrophic Error (collectively "Errors") as provided in this Rule. [In limited circumstances, the Exchange may nullify transactions, pursuant to Interpretation and Policy .08 below.]

(a) – (d) No change.

***... Interpretations and Policies:***

**.01 - .05** No change.

**.08** For purposes of the obvious pricing error provision in paragraph (a)(1) of this Rule, executions will not be adjusted or nullified if they occurred while the underlying security was in a limit up-limit down state, as defined in Rule 6.39. Nothing in this provision shall prevent such executions to be reviewed on an Exchange motion. This provision will be on a one year pilot basis to coincide with the Plan as defined in Rule 6.39. The Exchange will provide the Commission with data and analysis during the duration of this pilot as requested.

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## **Rule 6.18. HAL**

This Rule governs the operation of the HAL system. HAL is a feature within the System that provides automated order handling in designated classes for qualifying electronic orders that are not automatically executed by the System.

(a) – (c) No change.

(d) *Early Termination of Exposure Period.* In addition to the receipt of a response to trade the entire exposed order at the NBBO or better, the exposure period will also terminate early under the following circumstances:

(i) – (iii) No change.

(iv) If during the exposure period of a market order the underlying security enters a limit up-limit down state, as defined in Rule 6.39, then the exposure period shall terminate and any unexecuted portion of the exposed order shall cancelled.

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## **Rule 6.39. Equity Market Plan to Address Extraordinary Market Volatility**

This Rule shall be in effect during a pilot period to coincide with the pilot period for the Regulation NMS Plan to Address Extraordinary Market Volatility (the “Limit Up-Limit Down Plan” or the “Plan”).

The Exchange shall modify option order processing during a limit up-limit down state. For purposes of this rule, a “limit up-limit down state” shall mean the period of time when the underlying security of an option enters a limit or straddle state as defined in the Plan.

**(a) Exchange Order Types.** The following order types will be handled specially during a limit up-limit down state: market orders, market-on-close orders, stop orders, and stock-option orders. Refer to Rule 6.10 and 6.13 for descriptions of how such orders will be handled during a limit up-limit down state.

**(b) Order Handling.** The following order handling features shall operate differently during a limit up-limit down state:

(1) *Openings*. Refer to Rule 6.11 for a description of how Openings will behave during a limit up-limit down state.

(2) *Hybrid Agency Liaison*. Refer to Rule 6.18 for a description of how HAL will operate during a limit up-limit down state.

(3) *Complex Order Request for Responses Auction*. Refer to Rule 6.13 for a description of how a complex order request for responses auction (referred to as “COA”) will operate during a limit up-limit down state.

(4) *Canceling/Replacing Orders*. If a request to replace a limit order with a market order is received while the underlying security is in a limit up-limit down state, then the market order and the original limit order will be returned.

(c) **Obvious Error**. Refer to Rule 6.15 for a description of how the Exchange will handle potential obvious error executions during a limit up-limit down state.

(d) **Market-Maker Quoting Obligations**. Subject to certain limitations specified in the rules identified below, the Exchange will not require Market-Makers to quote in series of options when the underlying security is in a limit up-limit down state. Market-Maker participation entitlements will continue to apply during a limit up-limit down state. For the particular limitations, refer to the specific Market-Maker category, and corresponding obligations.

\* \* \* \* \*

## **Rule 8.5. Obligations of Market-Makers**

(a) In registering as a Market-Maker, a Participant commits itself to various obligations. Transactions of a Market-Maker in its market making capacity must constitute a course of dealings reasonably calculated to contribute to the maintenance of a fair and orderly market, and Market-Makers should not make bids or offers or enter into transactions that are inconsistent with such course of dealings. Ordinarily, Market Makers are expected to adhere to the following obligations:

(1) During trading hours a Market-Maker must maintain a continuous two-sided market in 60% of the non-adjusted option series of each registered class that have a time to expiration of less than nine months. For purposes of this subparagraph, “continuous” means 90% of the time. If a technical failure or limitation of the System prevents a Market-Maker from maintaining, or from communicating to the Exchange, timely and accurate quotes in a series, the duration of such failure shall not be considered in determining whether that Market-Maker has satisfied the 90% quoting standard with respect to that series. An “adjusted option series” is an option series wherein, as a result of a corporate action by the issuer of the underlying security, one option contract in the series represents the delivery of other than 100 shares of underlying stock or Units. This obligation does not apply to intra-day add-on series on the day during which such series are added for trading. The Exchange may consider other exceptions to this obligation based on demonstrated legal or regulatory requirements or other mitigating circumstances.

(2) – (6) No changes.

(b) – (d) No changes.

**... Interpretations and Policies:**

**.01** When the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, Market-Makers shall have no quoting obligations in the class.

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**Rule 8.17. DPM Obligations**

(a) *Dealer Transactions.* Each DPM shall fulfill all of the obligations of a Market-Maker under the Rules, and shall satisfy each of the following requirements in respect of each of the securities allocated to the DPM. To the extent that there is any inconsistency between the specific obligations of a DPM set forth in this Rule 8.17 and the general obligations of a Market-Maker under the Rules, this Rule 8.17 shall govern. Each DPM shall:

(1) provide continuous quotes in at least the lesser of 99% of the non-adjusted option series (as defined in Rule 8.5(a)(1)) or 100% of the non-adjusted option series minus one call-put pair of each option class allocated to it, with the term “call-put pair” referring to one call and one put that cover the same underlying instrument and have the same expiration date and exercise price, and assure that its disseminated market quotations are accurate. This obligation does not apply to intra-day add-on series on the day during which such series are added for trading. For purposes of this subparagraph (a)(1), “continuous” means 90% of the time. If a technical failure or limitation of the System prevents a DPM from maintaining, or from communicating to the Exchange, timely and accurate quotes in a series, the duration of such failure shall not be considered in determining whether that DPM has satisfied the 90% quoting standard with respect to the series;

\* \* \* \* \*

**... Interpretations and Policies:**

**.01** No changes.

**.02** When the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, DPMs shall have no quoting obligations in the class.

\* \* \* \* \*

**Rule 8.19. Participation Entitlement of DPMs**

(a) No changes.

(b) The participation entitlement for DPMs shall operate as follows:

(1) *Generally.*

(A) To be entitled to a participation entitlement, the DPM must be quoting at the BBO.

(B) A DPM may not be allocated a total quantity greater than the quantity that the DPM is quoting at the BBO.

(C) The participation entitlement is based on the number of contracts remaining after all public customer orders in the Book at the BBO have been satisfied.

(2) *Participation Rates Applicable to DPMs.* The collective DPM participation entitlement shall be: 50% when there is one Market-Maker also quoting at the BBO and 40% when there are two or more Market-Makers also quoting at the BBO. If only the DPM is quoting at BBO (with no Market-Makers quoting at the BBO), the participation entitlement shall not be applicable and the allocation procedures under Rule 6.12 shall apply.

(3) *Participation Entitlement in Instances Where a Preferred Market-Maker Receives a Participation Entitlement Pursuant to Rule 8.13.* A DPM will not receive its participation entitlement set forth in this Rule in trades for which a Preferred Market Maker receives a participation entitlement pursuant to Rule 8.13, based on the order priority determined by the Exchange under Rule 6.12.

***... Interpretations and Policies:***

**.01 - .02** No changes.

**.03** Where the underlying security for a class is in a limit up-limit down state, as defined in Rule 6.39, DPMs shall have no quoting obligations in the class. However, a DPM may receive a participation entitlement in series of such a class when the underlying security has entered a limit up-limit down state if it elects to quote in such series and otherwise satisfies the requirements set forth in Rule 8.19(b).

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