

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–88599; File No. SR–CboeBZX–2020–006]

### Self-Regulatory Organizations; Cboe BZX Exchange, Inc.; Order Approving a Proposed Rule Change To Provide Members Certain Optional Risk Settings Under Proposed Interpretation and Policy .03 of Rule 11.13

April 8, 2020.

#### I. Introduction

On February 12, 2020, Cboe BZX Exchange, Inc. (the “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) <sup>1</sup> and Rule 19b–4 thereunder, <sup>2</sup> a proposed rule change to provide members certain optional risk settings under proposed Interpretation and Policy .03 of Rule 11.13. The proposed rule change was published for comment in the **Federal Register** on February 27, 2020. <sup>3</sup> The Commission received no comment letters on the proposed rule change. This order approves the proposed rule change.

#### II. Description of the Proposal

The Exchange proposes to offer two optional credit risk settings that would authorize the Exchange to take automated action if a designated limit for a member is breached. Specifically, the Exchange proposes to offer: (i) The “Gross Credit Risk Limit,” a pre-established maximum daily dollar amount for purchases and sales across all symbols, where both purchases and sales are counted as positive values, and (ii) the “Net Credit Risk Limit,” a pre-established maximum daily dollar amount for purchases and sales across all symbols, where purchases are counted as positive values and sales are counted as negative values. <sup>4</sup>

The Exchange also proposes to provide that if a member does not self-clear, the member may allocate the responsibility for establishing and adjusting the Gross Credit and Net Credit risk settings to a clearing member that clears transactions on behalf of the member, if designated in a manner

prescribed by the Exchange. <sup>5</sup> A member that allocates this responsibility to its clearing member would be able to view any risk setting established by the clearing member and would be notified of any action taken by the Exchange with respect to the member’s trading activity. <sup>6</sup> However, the member would cede all control and ability to establish and adjust the risk settings to its clearing member, <sup>7</sup> but the member would retain the ability to revoke the responsibility allocated to its clearing member at any time, if designated in a manner prescribed by the Exchange. <sup>8</sup>

Pursuant to the proposal, any specified limits for the risk settings applicable to the Gross Credit or Net Credit Risk Limits may only be set at the MPID level and may be established or adjusted before the beginning of a trading day or during the trading day. <sup>9</sup> Both the member and the clearing member may enable alerts to signal when the member is approaching the designated limits. <sup>10</sup> These alerts would generate when a member breaches certain percentage thresholds of its designated risk limit, which would send an email message to the recipients designated by the member or clearing member. <sup>11</sup> According to the Exchange, it anticipates initially setting the thresholds at fifty, seventy, or ninety percent of the designated risk limit. <sup>12</sup>

The proposed rule change would also specify that if a risk setting is breached, the Exchange would automatically block new orders submitted and cancel open orders until the applicable risk control is adjusted to a higher limit by the member or clearing member with the responsibility of establishing and adjusting the risk settings. <sup>13</sup> Finally, the

<sup>5</sup> See proposed Interpretation and Policy .03(c) of Rule 11.13. The Exchange notes that all members are required to either clear their own transactions or to have in place a relationship with a clearing member that has agreed to clear transactions on their behalf in order to conduct business on the Exchange. See Notice, *supra* note 3, at 11422.

<sup>6</sup> See proposed Interpretation and Policy .03(c) of Rule 11.13.

<sup>7</sup> See Notice, *supra* note 3, at 11422.

<sup>8</sup> See proposed Interpretation and Policy .03(c) of Rule 11.13.

<sup>9</sup> See proposed Interpretation and Policy .03(b) of Rule 11.13.

<sup>10</sup> See proposed Interpretation and Policy .03(d) of Rule 11.13. The Exchange notes that a clearing member would have the ability to enable alerts regardless of whether it was allocated responsibilities pursuant to proposed Interpretation and Policy .03(c) of Rule 11.13. See Notice, *supra* note 3, at 11423 n.11.

<sup>11</sup> See Notice, *supra* note 3, at 11423.

<sup>12</sup> See *id.*

<sup>13</sup> See proposed Interpretation and Policy .03(e) of Rule 11.13. The Exchange notes, however, that orders entered for participation in the opening or closing auction cannot be canceled or modified after the applicable “cut-off” time, but will be

Exchange proposes to amend Rule 11.15(f) to specify that the Exchange may share any of a member’s risk settings specified in Interpretation and Policy .03 of Rule 11.13 with the clearing member that clears transactions on behalf of the member.

#### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange. <sup>14</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act, <sup>15</sup> which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The Commission believes that the proposed rule change is reasonably designed to provide members with an optional tool to manage their credit risk. The Commission notes that other exchanges have established risk protection controls that are similar in many respects to the Exchange’s proposal. <sup>16</sup> The Commission also notes that the Exchange currently provides credit controls that measure gross and net exposure, similar to the proposed risk limits. <sup>17</sup> Unlike the proposed risk limits, however, the Exchange’s existing credit controls apply at the logical port level, rather than by MPID, and are applied based on a combination of

marked for cancellation. See Notice, *supra* note 3, at 11423 n.13. Similarly, the Exchange notes that orders entered for participation in the Cboe Market Close (“CMC”) will be matched for execution at the applicable cut-off time, and cannot be canceled or modified after such time. See *id.* According to the Exchange, therefore, if a risk setting breach occurs after the applicable cut-off time for an opening or closing auction, or the CMC, the auction orders or CMC auction orders would not be canceled or modified. See *id.* See also Rule 11.23(b)(1)(B) and (c)(1)(B) and Rule 11.28(a) and (b).

<sup>14</sup> In approving this proposed rule change, the Commission notes that it has considered the proposed rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

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

<sup>16</sup> See, e.g., Investors Exchange LLC Rule 11.380.

<sup>17</sup> See Interpretation and Policy .01(h) of Rule 11.13.

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

<sup>2</sup> 17 CFR 240.19b–4.

<sup>3</sup> See Securities Exchange Act Release No. 88263 (February 21, 2020), 85 FR 11421 (“Notice”).

<sup>4</sup> See proposed Interpretation and Policy .03(a) of Rule 11.13. For purposes of calculating both the Gross Credit Risk Limit and the Net Credit Risk Limit, only executed orders would be included. See *id.*

outstanding orders on the Exchange's book and notional execution value, rather than based simply on a notional execution value.<sup>18</sup> The Commission believes that the proposed rule change would provide an additional option for members seeking to further tailor their risk management capability while transacting on the Exchange. The Commission also believes that the proposed rule change is reasonably designed to provide clearing members additional opportunity to monitor and manage the potential risks that they assume when clearing for members of the Exchange, as well as to provide clearing members with greater control over their risk tolerance and exposure on behalf of their correspondent members, while also providing an alert system designed to help ensure that both members and clearing members are made aware of developing issues.

The Commission notes that the proposed Gross Credit and Net Credit Risk Limits are optional functionalities. The Commission reminds members electing to use the proposed risk limits to be mindful of their obligations to, among other things, seek best execution of orders they handle on an agency basis. A broker-dealer has a legal duty to seek to obtain best execution of customer orders, and the decision to utilize the proposed risk settings, including the parameters set forth by the member for the risk setting, must be consistent with this duty.<sup>19</sup> For instance, under the proposal, members, or their respective clearing members on their behalf, have discretion to set the Gross Credit Risk Limit or Net Credit Risk Limit. While the Exchange did not affirmatively establish minimum and maximum permissible settings for these limits in its proposed rule change, the Commission expects the Exchange to periodically assess whether the risk limits are operating in a manner that is consistent with the promotion of fair and orderly markets. In addition, the Commission expects that members will consider their best execution obligations when establishing the parameters for the risk limits.<sup>20</sup> For example, to the extent that a member's risk settings are set to overly-sensitive parameters, particularly

if a member's order flow to the Exchange contains agency orders, a member should consider the effect of its chosen settings on its ability to receive a timely execution on marketable agency orders that it sends to the Exchange in various market conditions.<sup>21</sup> The Commission cautions that brokers considering their best execution obligations should be aware that agency orders they represent may be blocked or canceled on account of the Gross Credit and Net Credit Risk Limits.

Based on the foregoing, the Commission finds that the proposed rule change is consistent with the Act.

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>22</sup> that the proposed rule change (SR-ChoeBZX-2020-006) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>23</sup>

**J. Matthew DeLesDernier,**

*Assistant Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-88587; File No. SR-NASDAQ-2020-015]

### Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 4759

April 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 3, 2020, The Nasdaq Stock Market LLC ("Nasdaq" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit

comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Rule 4759 (Data Feeds Utilized) to include the Long-Term Stock Exchange, Inc. ("LTSE") in the list of proprietary and network processor feeds that the Exchange utilizes for the handling, routing, and execution of orders as well as regulatory compliance processes related to those functions.

The text of the proposed rule change is available on the Exchange's website at <http://nasdaq.cchwallstreet.com>, at the principal office of the Exchange, and at the Commission's Public Reference Room.

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

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

###### 1. Purpose

On May 10, 2019, the Commission approved the Long-Term Stock Exchange, Inc. ("LTSE") as a national securities exchange.<sup>3</sup> In anticipation of the planned launch of LTSE,<sup>4</sup> the Exchange proposes to amend and update Rule 4759, which lists the proprietary and network processor feeds that the Exchange utilizes for the handling, routing and execution of orders as well as regulatory compliance processes related to those functions. Specifically, the Exchange proposes to specify that LTSE will be an additional market center source for quotation data

<sup>3</sup> See Securities Exchange Act Release No. 85828 (May 10, 2019), 84 FR 21841 (May 15, 2019) (File No. 10-234) (Order approving LTSE application for registration as a national securities exchange).

<sup>4</sup> LTSE expects to launch on May 15, 2020. See LTSE Update on adjusted phase-in schedule published on March 18, 2020, available at: <https://longtermstockexchange.com/static/MA-2020-006-14f9b362b7bd1103c9545525d246e778.pdf>.

<sup>18</sup> See *id.* See also Notice, *supra* note 3, at 11422.

<sup>19</sup> See Securities Exchange Act Release Nos. 37619A (September 6, 1996), 61 FR 48290 (September 12, 1996) ("Order Handling Rules Release"); 51808 (June 9, 2005), 70 FR 37496, 37537-38 (June 29, 2005).

<sup>20</sup> The Commission reminds broker-dealers that they must examine their procedures for seeking to obtain best execution in light of market and technology changes and modify those practices if necessary to enable their customers to obtain the best reasonably available prices. See Order Handling Rules Release, *supra* note 19, at 48323.

<sup>21</sup> For example, a marketable agency order that would have otherwise executed on the Exchange might be prevented from reaching the Exchange on account of other interest from the member that causes it to exceed the pre-established risk limit and thereby results in the Exchange blocking new orders from the member.

<sup>22</sup> 15 U.S.C. 78s(b)(2).

<sup>23</sup> 17 CFR 200.30-3(a)(12).

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

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