



NYSE ARCA OPTIONS REGULATORY BULLETIN

NYSE Arca Options RB-16-04

February 19, 2016

TO: NYSE ARCA OTP HOLDERS & OTP FIRMS

FROM: NYSE REGULATION

SUBJECT: RULES OF PRIORITY AND ORDER PROTECTION IN OPEN OUTCRY TRADING

NYSE Regulation is issuing this bulletin to remind OTP Holders and OTP Firms of certain rules and procedures that must be followed when trading in open outcry on the Options Floor. This bulletin addresses rules pertaining to order announcement, order priority and order protection, and will cover the proper procedures that must be followed in order to help ensure compliance with these rules. OTP Holders are encouraged to review relevant rules and previously issued regulatory guidance referenced in this bulletin.

Priority and Order Allocation Procedures – Open Outcry (Rule 6.75)

When executing trades in open outcry, OTP Holders must comply with the rules of priority. Specifically, as outlined in Rule 6.75, open outcry orders must yield priority to all better-priced orders in the Consolidated Book, equal-priced Customer orders in the Consolidated Book and any non-Customer Orders ranked ahead of equal priced Customer orders.

Rule 6.75 provides that where two or more bids (offers) for the same option contract represent the best price and one such bid (offer) is for the account of a Customer displayed on the Consolidated Book, such Customer bid (offer) and any non-Customer bids (offers) on the Consolidated Book ranked ahead of such Customer bid (offer) shall have priority over any other bid (offer) in the Trading Crowd. For purposes of Rule 6.75, Customer interest also includes any orders placed in the Consolidated Book on behalf of a Professional Customer as defined in Rule 6.1A(a)(4A). Generally speaking, this means that OTP Holders may not trade at, or through, the price of any priority interest on the Consolidated Book without satisfying such interest.

Priority is established at the time an open outcry order is executed, as determined by the time an order is released in Liquid Point¹ by the Trading Official (“TO timestamp”) signifying that a consummated trade has taken place, subject to the limited exceptions (discussed later).² Floor Brokers should be aware that any trade negotiations involving members of the trading crowd or communications with their firm’s desk or off-floor customers should be finalized prior to requesting a Trading Official to release their order. Once a Trading Official releases an order,

¹ Floor Broker Workstation or BLAZE terminal, collectively “Liquid Point”.

² See NYSE Arca RBO-12-07 (Book Priority and NBBO Trade Throughs at the Time of Execution)

thus signifying that an execution has taken place, any priority interest present on the Consolidated Book at the time of the TO timestamp must then be honored.

Floor Brokers may inquire with the Trading Official at the post as to the amount of any priority interest in the Consolidated Book prior to executing an order; however this information is for advisory purposes only and is provided on a best efforts basis. Floor Brokers are required to clear all priority interest actually present at the time of the TO timestamp, regardless of whether that number is less than or greater than the amount indicated by the Trading Official at the time of the Floor Broker's inquiry.

Floor Brokers may seek to satisfy their obligation to clear priority interest in a few ways. Floor Brokers may use Liquid Point to send a Clear-the-Book ("CTB") order for the full size of the initiating order, at the same price as the priority interest in the Consolidated Book that they need to clear, and on the appropriate side of the market. By sending a CTB order contemporaneous with the execution of a trade in open outcry, the CTB order will trade with only those contracts that had priority as of the time of the trade, based on the TO timestamp.

There may be times when using the CTB order is not possible or appropriate. For example, if a Floor Broker is executing an order where (s)he is buying at the same price as the Exchange Best Bid, a CTB order will default to an order to buy and cannot be changed to an order to sell, in order to satisfy the priority interest represented within the Exchange best bid.

Trading Officials may release an order using CTB override³ in certain situations where it is warranted, such as when there is a system or other issue that prevented the Trading Official from releasing the order contemporaneous with the open outcry trade at which time there was no priority interest at the execution price(s). There may also be instances where a Floor Broker may request to have an order released with an override of CTB functionality. In such instances, the broker must always continue to comply with the rules of priority as if (s)he was using CTB functionality. Compliance with the rules of priority in these situations may be achieved if the Floor Broker, or employee of a Floor Brokerage firm, were to contemporaneously route an Intermarket Sweep Order ("ISO")⁴, to the Exchange for the full size of his or her order, at the same price as the priority interest in the Consolidated Book that they need to clear and on the appropriate side of the market. Any delays in the routing of an order intended to clear priority interest would be considered a violation of a Floor Broker's obligation to comply with the terms of Rule 6.75. All instances involving CTB overrides involving priority interest are documented and are subject to regulatory review. Floor Brokerage firms must maintain records of all orders sent to the Exchange to satisfy priority interest on the Consolidated Book.⁵ Record retention requirements apply regardless of whether an order was actually executed.

Split Price Priority

Rule 6.75(h) provides that the minimum order size required to achieve priority over any priority interest in the Consolidated Book is 100 contracts. For example, if an OTP Holder executing a 100 contract order buys 50 or more option contracts at a price, the OTP Holder has priority in purchasing up to the equivalent number of option contracts at the next lower price provided the OTP Holder's bid is made promptly and both purchases represent the contra side to the

³ An order released by a Trading Official using CTB override will not generate a CTB order.

⁴ See NYSE Arca Rule 6.92(a)(8) - Intermarket Sweep Orders

⁵ See NYSE Arca Rule 6.68(a) - Record of Orders

transaction of the same order. If the BBO is \$1.00 bid, offered at \$1.10, 10 x 50, where the \$1.00 bid for 10 contracts represents priority interest, an OTP Holder with an order to buy 100 contracts who also has an order to sell 100 contracts, may execute the order by trading 50 contracts at \$1.05 and 50 contracts at \$1.00. This transaction would allow the OTP Holder to take priority over the priority interest that was bidding \$1.00 for 10 contracts. If instead, the OTP Holder proceeded by executing the order by trading 10 contracts at \$1.05 and 90 contracts at \$1.00, the OTP Holder would be required to satisfy the priority interest that was bidding \$1.00 for 10 contracts before executing the remaining 80 contracts at \$1.00.

Complex Order Priority

Rule 6.75(g) provides a limited exception to standard rules of priority when executing Complex Orders in open outcry. Complex Orders, as defined in Rule 6.62(e), may be executed at a net debit or credit price without yielding priority to equal priced Customer bids (offers) for the individual leg markets in the Consolidated Book, provided that at least one options leg of the order betters the corresponding Customer market in the Consolidated Book for that series by at least \$0.01. Individual legs of a Complex Order, or the option leg of a Stock/Option Order, may never trade at a price that is inferior to any leg market comprising the Complex BBO.

CTB orders are not generated for complex executions; therefore Floor Brokers should send an ISO order(s), for the appropriate size, and side of the market and at the same price as the priority interest in the relevant leg(s) markets in the Consolidated Book that they need to clear.

OTP Holders are also reminded that Complex Orders executed in open outcry must yield priority to all better-priced Electronic Complex Orders and in addition, all same-price Customer and/or Professional Customer Electronic Complex Orders, for the same complex order strategy that may be present in the Consolidated Book at the time of execution. Floor Brokers should determine whether there are any equal or better-priced Electronic Complex Orders by referencing the complex order table displayed in Liquid Point prior to requesting that a Trading Official release their order. Once a Trading Official releases a Complex Order, thus signifying that an execution has taken place, all better-priced Electronic Complex Orders, and all equal-priced Customer and/or Professional Customer Electronic Complex Orders present at the time of the TO timestamp must then be satisfied. Upon release of the order, Floor Brokers should contemporaneously route an Electronic Complex Order to the Exchange for the appropriate size and side of the market and at the same price as any Electronic Complex Order(s) in the Consolidated Book, that they need to clear. Any in the routing of an order intended to clear priority interest will be considered a violation of a Floor Broker's obligation to comply with the terms of Rule 6.75.

Multi-Legged Orders and Stock/Option Order Priority

OTP Holders are reminded that orders involving multiple legs that do not meet the definition of a Complex Order, as defined in Rule 6.62(e), and Stock/Option orders, as defined in Rule 6.62(h), do not have priority over equal priced priority interest in the Consolidated Book.

Order Protection and Avoidance of NBBO Trade-Throughs

OTP Holders must comply with the Exchange rules and the terms of the Options Order Protection and Locked/Crossed Market Plan ("Linkage Plan") by honoring any better-priced

Protected Quotes. The Linkage Plan,⁶ as codified in Exchange Rules 6.92 and 6.94 provides that OTP Holders shall not effect trade-throughs of a Protected Bid or Offer (collectively, a “Protected Quote”), except pursuant to an applicable exception.⁷ A Protected Quote is defined as a bid or offer in an options series that (a) is disseminated pursuant to the OPRA Plan and (b) is the best bid or best offer, respectively, displayed by an eligible exchange. Once a Trading Official releases an order, thus signifying that an execution has taken place, all better-priced Protected Quotes present at the time of the TO timestamp must be satisfied, unless an exemption applies. It is the Floor Broker’s responsibility to ascertain whether there are any better-priced Protected Quotes in the market at the time of execution, and whether an exemption applies. In order to help ensure that Floor Brokers fulfill their obligation to avoid trade-throughs, an ISO should be routed to each exchange displaying a better-priced Protected Quote, for the full size of the Protected Quote, contemporaneous with the execution of the order on NYSE Arca. Floor Brokers should note that simply sending an order to a third party router for the aggregate size of all better-priced Protected Quote(s) may not satisfy the requirements for the trade-through exemption. In order to ensure compliance with the terms of the ISO trade-through exemption, OTP Holders should send individual ISOs, or use other means they deem appropriate to ensure that ISOs are sent for the full size of each Protected Quote, to each eligible exchange.

Limited Exceptions to TO Timestamp

As previously discussed in RBO-12-07, the Exchange is aware that in certain limited circumstances the TO Timestamp may not reflect market conditions at the precise time that an open outcry execution occurred. This may be the case when there are “race conditions” in connection with the Trading Official releasing the order, rapidly flickering quotations, periods of heightened market activity or systems issues affecting the release of an order. Under these limited conditions, Floor Brokers would be required to yield priority to only those orders that were present at the actual time of execution, as determined by the Trading Official at the post. Where these situations are known, the Trading Official will document the actual market conditions that were present at the time of execution.

Relevant NYSE Arca Options Rules

- Rule 6.68 Record of Orders
- Rule 6.73 Manner of Bidding and Offering
- Rule 6.75 Priority and Order Allocation Procedures — Open Outcry
- Rule 6.94 Order Protection and Avoidance of Trade-Throughs

Contact Information

For questions regarding the bulletin and rules governing floor trading, please contact Stewart Courant at (415) 318-1963 or Glenn Gsell at (415) 318-1936

⁶ See <http://www.sec.gov/rules/sro/nms/nmsarchive/nms2007.shtml#4-546>

⁷ See NYSE Arca Rule 6.94(b) - Exceptions to Trade-Through Liability.