NYSE

Information Memo

NYSE IM 21-01

March 16, 2021

TO: ALL MEMBERS AND MEMBER ORGANIZATIONS

FROM: NYSE REGULATION

SUBJECT: QUARTERLY EXPIRATION DAY– March 19, 2021

I. Purpose

March 19, 2021 will be an Expiration Day (the “Expiration Day”) for stock and index options and futures products for which settlement pricing is based upon opening or closing prices that day on the New York Stock Exchange LLC (“NYSE” or “Exchange”). This Information Memorandum reminds members and member organizations of certain NYSE rules and policies regarding order entry requirements; publication of imbalance information; entry and cancellation of market-on-close (“MOC”), limit-on-close (“LOC”) and closing offset (“Closing IO Order”) orders; and printing of Closing Auctions. While these rules and policies are applicable every day, they are especially significant on expiration days.

II. Record of Orders

Members and member organizations are reminded that, except in limited circumstances[1], NYSE Rule 123(e) requires that, immediately following the receipt of an order in an NYSE listed security on the Trading Floor, members and member organizations must record the details of that order (including the prescribed data elements) in an electronic system on the Trading Floor. This recording must occur <u>before</u> the order can be represented on the Trading Floor. All applicable order information should be entered into an Exchange order management system (“OMS”) such as the Broker Booth Support System (“BBSS”). Orders routed to and received on the Floor from a third-party OMS are not compliant with Rule 123 until routed to BBSS or until entered into BBSS via local order entry. The portion of any order being executed verbally must have been entered into an Exchange OMS prior to the order being represented for execution. Members and member organizations are further reminded that held or not held order instructions must be entered in the free-form field (Tag 58).

Additionally, NYSE Rule 123(f) requires that all reports of executions related to such orders be entered into the same database using prescribed data elements.

III. Rules and Policies Relating to the Close

1 Supplementary Material .21 to Rule 123 provides that “[a]ny order executed by a DMM for his or her own account and any orders which by their terms are incompatible for entry in an Exchange system relied on by a Floor member to record the details of the order in compliance with this Rule” are exempt from the order entry requirements of NYSE Rule 123(e). In addition, Supplementary Material .22 to that rule specifies unique order entry requirements that are applicable to bona fide arbitrage orders and orders to offset transactions made in error.

A. MOC/LOC and Closing IO Orders - Order Entry and Cancellation

Members and member organizations are reminded that the provisions of NYSE Rule 7.35B (DMM-Facilitated Closing Auctions) apply to the Close on all days, including on all expiration days. While the Exchange expects systems to operate normally, in the unlikely event the Exchange is unable to conduct a Closing Auction in one or more securities due to a systems or technical issue leading into or at the Close, the Official Closing Prices for Auction-Eligible Securities (as defined in NYSE Rule 7.35(a)(1)) will be determined in accordance with NYSE Rule 1.1(s) (Official Closing Price).

In the event the Exchange invokes its exemptive powers under NYSE Rule 7.35B(j)(2) (Extreme Order Imbalances at or Near the Close), the terms of that rule would govern the handling of orders at the Close. See Section III.D.

In connection with the entry of MOC/LOC and Closing IO Orders, members should pay particular attention to the following:

- A published Regulatory Closing Imbalance[2] is an imbalance that has been disseminated to the Tape. An imbalance announced orally or physically posted at the panel is not considered to be a published imbalance. See Section III.B. The Exchange's Auction Imbalance Information (i.e., imbalance information provided to Floor brokers for any security in which a Floor broker has entered an order or as specifically requested by a Floor broker) also does not constitute a Regulatory Closing Imbalance.

- Members and member organizations are reminded that, while they should enter orders as early in the day as possible, all MOC/LOC Orders (unless entered to offset a published Regulatory Closing Imbalance) must be entered electronically by the Closing Auction Imbalance Freeze Time (typically, 3:50 p.m.).[3] Entering MOC/LOC Orders early provides DMMs with the opportunity to more quickly identify and disseminate potential order imbalances that might exist at the Close. This, in turn, enables brokers and traders to more effectively identify potential offsetting customer interest that could mitigate any imbalance. MOC/LOC and Closing IO Order entered prior to 3:50 p.m. may be cancelled or reduced prior to that time for any reason.

- After 3:50 p.m., Exchange systems will accept only MOC and LOC Orders opposite to the side of the Regulatory Closing Imbalance. If a Regulatory Closing Imbalance has not been published, the Exchange will reject all MOC and LOC Orders after that time. Closing IO Orders may be entered on both sides of the market up to 4:00 p.m.

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[2] Per NYSE Rule 7.35B(d)(1), "[a]t the Closing Auction Imbalance Freeze Time, if the Closing Imbalance is 500 round lots or more, the Exchange will disseminate a Regulatory Closing Imbalance."

[3] "Closing Auction Imbalance Freeze Time" means 10 minutes before the scheduled end of Core Trading Hours. See NYSE Rule 7.35(a)(7). Specific time deadlines noted in this memorandum (e.g., the 3:50 p.m. deadline for entry of MOC/LOC Orders) refer to Eastern Time and are applicable to days for which the scheduled end of Core Trading Hours is 4 p.m. On days when the NYSE is scheduled to close at a time other than 4 p.m., such deadlines - tied to the scheduled end of Core Trading Hours - move accordingly.

- Between 3:50 p.m. and 3:58 p.m., MOC/LOC and Closing IO Orders may be cancelled or reduced in size only to correct a legitimate error.[4] This restriction also applies to orders that are cancelled or reduced in size by means of cancel/replace functionality.
- NYSE Regulation will monitor the cancellation of MOC/LOC and Closing IO Orders.
- After 3:58 p.m., MOC/LOC Orders may not be cancelled, adjusted or reduced in size for any reason except in accordance with NYSE Rule 7.35B(j)(2)(B), which allows for the suspension of the prohibition on canceling MOC/LOC Orders in certain limited circumstances. See Section III.D, below.
- A Regulatory Closing Imbalance will be disseminated at the Closing Auction Imbalance Freeze Time (i.e., 3:50 p.m.) regardless of whether the security has not opened or is halted or paused at that time. See NYSE Rule 7.35B(d)(1)(C). Accordingly, in the event of a trading halt effective at 3:50 p.m. or later, MOC/LOC orders may be entered, however, only to offset a published imbalance while Closing IO Orders may be entered in any amount on either side of the market.

B. Imbalance Publications[5]

NYSE Rule 7.35B(d) provides for the publication of order imbalances as described below. DMMs are reminded that erroneous imbalance publications must be corrected as soon as practicable.

1. Publication of Manual Closing Imbalance between 3:00 p.m. and 3:50 p.m.

Between 3:00 p.m. and 3:50 p.m., DMMs are encouraged to issue Manual Closing Imbalance Publications of any size if they believe that there could be significant price dislocation at the Close. These publications are informational only and do not limit MOC/LOC or Closing IO Order entry or cancellation before 3:50 p.m. DMMs who wish to issue a Manual Closing Imbalance Publication must obtain prior approval from a Floor Official (see NYSE Rule 46.20) or qualified Exchange employee (see NYSE Rule 46.10) prior to issuance. Floor Official approvals to issue Manual Closing Imbalance Publications must be recorded in the Floor Official Request Tracking Engine ("FORTÉ"). DMMs must record the proposed imbalance information and note any other relevant information (e.g., average daily trading volume ("ADTV"), size, or degree of impact) in connection with the request.

2. Publication of Regulatory Closing Imbalance at 3:50 p.m.

If the Closing Imbalance is 500 round lots or more, at 3:50 p.m. the Exchange will disseminate a Regulatory Closing Imbalance regardless of whether the security has not opened or is halted or paused at that time. If, at 3:50 p.m., the Closing Imbalance is less than 500 round lots, but is otherwise significant in relation to the average daily trading volume in the security, a DMM may disseminate a Regulatory Closing Imbalance only with prior Floor Official approval. As with Manual Closing Imbalance Publications, a Floor Official approval to issue a Regulatory Closing Imbalance Publication must be recorded in FORTÉ and DMMs should record the proposed imbalance information and note any other relevant information (e.g., ADTV, size, or degree of impact) in connection with the request.

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4 "Legitimate Error" means an error in any term of an order, such as price, number of shares, side of the transaction (buy or sell), or identification of the security. See NYSE Rule 7.35(a)(13).

5 For more information on how imbalance publications are calculated, see NYSE Rule 7.35(a)(4).

3. Publication of Auction Imbalance Information

In addition to the Manual Closing Imbalance and Regulatory Closing Imbalance Publications described above, the Exchange also makes available Auction Imbalance Information prior to the Close in accordance with NYSE Rule 7.35B(e). From 2:00 p.m. until 3:50 p.m., the Exchange will make available Total Imbalance, Side of Total Imbalance, Paired Quantity, Unpaired Quantity, Side of Unpaired Quantity, and if published, Manual Closing Imbalance, to Floor brokers for any security (i) in which a Floor broker has entered an order or (ii) as specifically requested by a Floor broker. In addition, beginning at 3:50 p.m., all Closing Auction Imbalance Information will be made available to Floor Brokers.

C. The Closing Auction

1. Determining an Auction Price

DMMs are reminded that the DMM must select an Auction Price at which all better-priced orders on the Side of the Imbalance can be satisfied.[6] Additionally, DMMs are reminded of their obligation to maintain a fair and orderly market pursuant to NYSE Rule 104.

2. Floor Broker Verbal Interest at the Close

For a temporary period (which began on June 17, 2020 and which will end on the earlier of a full reopening of the Trading Floor facilities or after the Exchange closes on April 30, 2021), while the Trading Floor is open to only a subset of staff from DMM units that choose to return to the Trading Floor, DMMs are precluded from accepting verbal bids and offers from Floor brokers. Accordingly, Floor Broker Interest will not be eligible to participate in the Closing Auction and verbal interest will not be available on the Expiration Day.[7]

D. Extreme Order Imbalances at or Near the Close[8]

In order to avoid significant dislocation in the closing price that may result from an order entered or represented at or near the Close, NYSE Rule 7.35B(j)(2) permits the Exchange, on a security-by-security basis, to temporarily suspend the requirement that all order instructions be entered by the end of Core Trading Hours (per NYSE Rule 7.34(a)(2)(B)) and to permit the solicitation and entry of orders into Exchange systems. However, NYSE Rule 7.35B(j)(2)(A)(i) requires that such orders are solicited solely to offset any Imbalance in a security that may exist as of the scheduled end of Core Trading Hours. Offsetting interest may be solicited from both on-Floor and off-Floor participants up to a cut-off time designated by the Exchange. Offsetting interest is solicited using Exchange Trader Updates as well as messages sent directly to Floor broker hand-held devices. These Exchange-

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6 For more information on the Auction allocation following the determination of the Auction Price, see NYSE Rules 7.35B(h) and 7.37(b)(2) - (7).

7 See Commentary .03 to NYSE Rule 7.35B, which provides that "[f]or a temporary period that begins on June 17, 2020 and ends on the earlier of a full reopening of the Trading Floor facilities to DMMs or after the Exchange closes on April 30, 2021, Floor Broker Interest will not be eligible to participate in the Closing Auction."

8 For additional guidance on prohibitions on holding the close and considerations in connection with the entry of verbal interest at the Close, see Member Education Bulletin 2019-01, issued June 21, 2019, available at: https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-interpretations/2019/NYSE%20MEB%2019-01.pdf, and Member Education Bulletin 2019-03 available at: https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-interpretations/2019/NYSE%20MEB%2019-03.pdf.

issued solicitation requests include the security symbol, the Total Imbalance, the Side of the Total Imbalance and the Exchange Last Sale Price. If the side of the Total Imbalance is to buy (sell), during the Solicitation Period, the Exchange will accept only sell (buy) Limit Orders and Floor Broker Interest with a limit price equal to or higher (lower) than the Exchange Last Sale Price. The Exchange will reject all other orders and requests to cancel any orders, regardless of the time of entry of the original order. Exchange systems will accept interest entered electronically in the named security after 4:00 p.m. only if NYSE Rule 7.35B(j)(2) is invoked.

NYSE Rule 7.35B(j)(2)(B) allows for the temporary suspension of the prohibition on canceling an MOC or LOC Order after two minutes before the scheduled end of Core Trading Hours (i.e., typically 3:58 p.m.) where there is a legitimate error in such an order and the execution of the order would cause significant price dislocation at the Close.

Only the DMM assigned to a particular affected security may request relief under NYSE Rule 7.35B(j)(2). A request for relief under Rule 7.35B(j)(2) must be approved and supervised by an Executive Floor Governor or qualified Exchange employee and supervised by a qualified Exchange officer. All Rule 7.35B(j)(2)-related approvals must be recorded in FORTÉ.

E. Block-Sized Interest at the Close

Although orders entered at or near the Close are eligible to be executed either prior to the Close or as part of the Close, members and member organizations should keep in mind that such orders can result in price dislocation in the stock, particularly if the size of the order is unusual in relation to the average daily volume of the stock or otherwise cannot easily be absorbed because of prevailing market conditions. As a result, members and member organizations should not hold back large interest until at or near the Close and are advised that, if they do, they may face disciplinary action for potentially affecting the Close inappropriately. Efforts to improperly manipulate stock prices, regardless of their size, are strictly prohibited. In addition, members and member organizations should be aware that their orders may execute at multiple prices in a series of transactions that are distinct from the Close.

IV. Adequacy of Operations and Supervisory Staff

All members and member organizations, including DMMs, should ensure that both operational and supervisory staffing on and around the Expiration Day will be sufficient to monitor and process all orders, regardless of the form in which they are received, as well as to handle the anticipated increased workload associated with that event. All members and member organizations should also review their systems to ensure that they have adequate capacity to handle the expected increase in volume. For example, DMM firms should review their DMM Unit algorithm to ensure that they meet their obligations to maintain a fair and orderly market. DMMs are reminded to seek the advice of a Floor Official regarding any unusual situations as quickly as possible.

V. Supervision

A. Review of Policies and Procedures

Members and member organizations should carefully review their procedures as well as their supervisory systems for handling an increased volume of orders in connection with the Expiration Day. Specifically, members and member organizations should review their practices for handling orders at or near the Close. Their reviews should include practices applicable to manual orders and as well as those handled systemically, such as orders that are handled by a computer algorithm. In addition, members and member organizations should take all necessary steps to ensure that the relevant trading and back-office staffs are familiar with firm procedures for handling orders at or near the Close.

In addition, members and member organizations are reminded of their obligation to have adequate systems and controls relating to the use of firm systems by correspondents or others. Please consult Information Memo 11-13 (May 16, 2011), Information Memo 18-04 (August 13, 2018) and Information Memo 18-05 (August 13, 2018) for more information.

B. <u>Adequacy of Compliance Program</u>

Members and member organizations are also reminded to ensure that they have a robust compliance program that includes adequate written policies, procedures and supervisory controls to monitor for compliance with all applicable provisions of the Rule 7.35 series and the guidance contained in this memo. Policies and procedures must be adequate to ensure that all procedures related to MOC/LOC Orders and orders entered at or near the Close are appropriately followed and to detect and deter any actions that may violate Exchange or SEC rules.

C. <u>Supervision to Prevent Improperly Affecting the Close</u>

Members and member organizations must ensure that their activity does not have the effect of artificially impacting the closing price. As such, members, member organizations and compliance staff should be mindful of Information Memo 05-52 (August 1, 2005) regarding VWAP trading at or near the Close, which addresses their responsibility to ensure that trading strategies engaged in to facilitate or hedge VWAP orders have an economic basis and do not have the effect of marking the close or marking the value of a position. Member organizations should also be aware that certain orders and order entry practices may have the potential to cause price dislocation before the Close or distort the closing price due to prevailing market conditions at the time the order is entered. Similarly, trading at or near the Close is of particular concern due to the condensed timeframe for execution, and because the resultant closing prices are used to set benchmarks, such as index rebalancing. As a result, concerns regarding manipulation and disruptive trading may be heightened when trading occurs at or near the close.

Firms should review procedures utilized in connection with orders to be executed at or near the Close with their traders and other order-entry personnel. Firms should also review systemic order entry functions (e.g., algorithms or “smart servers”) for compliance with the provisions of Information Memorandum 05-52. Members and member organizations are also reminded that, when a firm has committed to purchase from or sell to a customer at a price that is derived from the closing price (e.g., VWAP and MOC orders) while also reserving a significant portion of its hedging or covering transaction to be executed at or near the Close, it must operate with substantial care. If the transaction is completed in a manner that does not effectively place the firm at market risk or if the transaction does not provide an opportunity for possible contra side interest to develop and/or react to the activity, it could raise regulatory concerns and constitute conduct inconsistent with just and equitable principles of trade.

D. <u>Compliance with Federal Securities Laws and Rules</u>

In addition to complying with Exchange rules and policies, members and member organizations should review all other applicable federal securities laws and regulations, including, among others, Sections 9(a)(2) and 10(b) of the Securities Exchange Act of 1934, Rules 10b-5 and 15c3-5 thereunder, Regulation SHO, and applicable margin and capital rules. Firms must ensure that they have written policies, procedures, and supervisory controls reasonably designed to detect and deter potentially violative conduct.

Members and member organizations are reminded that failure to comply with any of the requirements described in this memo may result in disciplinary action.

VI. Staff Contacts

Questions concerning this Information Memo should be directed to:

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