

December 18, 2017  
MR-17- 09

**CHICAGO STOCK EXCHANGE, INC.  
MARKET REGULATION DEPARTMENT  
INFORMATION MEMORANDUM**

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**RE: Amendments to CHX Rules Addressing Qualified Contingent Trades, Cross Orders and CHX Recordkeeping Requirements**

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On September 22, 2017, the Securities and Exchange Commission (“SEC”) approved Chicago Stock Exchange, Inc., (“CHX” or “the Exchange”) Rule Filing SR-CHX-2017-12 regarding Qualified Contingent Trades (“QCTs”) and related information recording obligations by certain Participants which will become operative on January 9, 2018. The purpose of this Information Memorandum is to discuss the noteworthy changes set forth in the approved rule filing.

**I. QCT Crosses May Only Be Submitted by Institutional Brokers (“IBs”)**

The Exchange amended Article 1, Rule 2(b)(2)(E) to provide that QCT crosses may be submitted to the Exchange only by registered IBs. Article 1, Rule 2(b)(2) sets forth the order execution modifiers that may be attributed to cross orders, and Article 1, Rule 2(b)(2)(E) defines the QCT cross order modifier. In this rule filing, this definition has been amended to state that only IBs may utilize the QCT cross order modifier. Prior to this change, CHX rules permitted any Participant to submit QCT crosses, but in practice non-IB Participants did not submit them. Currently, CHX’s rules require only IBs to input all orders and related information into BrokerPlex – an automated Exchange order and trade management system – and that this requirement facilitates the Exchange’s ability to gather information it considers to be crucial to its review of QCT crosses executed on the Exchange. The approved rule filing creates additional IB data capture requirements as detailed below in section II. *Given that non-IB Participants do not currently submit QCTs and the Exchange’s Surveillance and Examination program is optimized to review QCT crosses submitted by IBs, upon the operative date communicated above, QCT crosses may only be submitted to the CHX Matching System by IBs.*

**II. Recordkeeping Requirements for Away Component Trades of QCT Crosses**

The CHX Broker Back Office System (“BBOS”) is an Exchange-maintained trade management system that, among other things, enables the Exchange to review information to identify the specific component transactions on away exchanges that are being used to hedge QCT crosses executed on the Exchange. Currently, the Exchange encourages, but does not require, IBs to input into BBOS certain information for away QCT component orders and trades related to QCT crosses executed on the Exchange. Moreover, Article 11, Rule 3(a)(1)-(3), which sets forth recordkeeping obligations for certain Participants, including IBs, does not currently impose recordkeeping obligations on Participants regarding such away component orders and trades of QCT crosses.

## A. Article 11, Rule 3 Amendments

With the approval of this rule filing, the Exchange has made several interrelated amendments to Article 11, Rule 3 to require IBs to maintain their own records of, and record with the Exchange, certain information regarding away QCT component orders and trades. Specifically, the Exchange adopted new Rule 3(a)(4), which would make subject to the Rule 3(a) recordkeeping requirements every component order and trade, whether handled by the Participant or not, related to a cross order marked QCT that is submitted by the Participant and executed within the Exchange matching system.

The Exchange also modified Rule 3(b) to include a cross reference to Rule 3(a)(4), requiring that, subject to exceptions set out in interpretations to Rule 3, IBs accurately record in an electronic system designated by the Exchange certain details regarding the away component orders and executions identified in proposed Rule 3(a)(4). The Exchange has set forth these details in new Rule 3(b)(27), which provides that, with respect to any cross order marked QCT that is submitted by a Participant and executed within the Exchange matching system, each Participant must accurately record the date and time of receipt by the Participant of the corresponding order from its customer and all information specified by the Exchange regarding any related component orders and trades executed within the matching system or away which shall be entered into BBOS (as applicable), in a manner prescribed by the Exchange.<sup>1</sup>

## B. Article 17 Amendments

In addition, the Exchange amended Article 17, Rule 3(a) to state that an IB must enter all orders it receives for execution and any other information required under Article 11 into an automated system approved by the Exchange. The Exchange amended this rule to broaden the scope of Article 17, Rule 3(a) beyond just orders received by the IB for execution to reflect that the requirements of new Article 11, Rule 3(b)(27) may require the recording of information related to orders that the IB did not actually receive or otherwise handle.

The Exchange also adopted new Article 17, Rule 7, which would codify the BBOS into the Exchange's rules. Specifically, new Rule 7(a) states that the BBOS is a trade management system developed and maintained by the Exchange that permits IBs to input certain information and to generate reports therefrom, and that it also is an automated system approved by the Exchange for the purposes of amended Article 17, Rule 3(a). New Rule 7(b) states that users of the BBOS are responsible for entering all transactional, order and other information into the system as required by CHX Rules, in an accurate, timely and complete manner; the Exchange, as the operator of BBOS, retains information entered into BBOS on behalf of the user in conformity with applicable rules and regulations; and the Exchange will provide such information to IBs in a format designated by the Exchange to assist IBs in conducting research regarding their own trading activities, responding to requests for information from customers, regulatory authorities or by

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<sup>1</sup> The Exchange also made various clarifying amendments to Article 11, Rule 3 regarding certain recordkeeping requirements concerning orders and executions by certain types of Participants, including, but not limited to, IBs. Specifically, the Exchange amended Article 11, Rule 3(a) to state that the provisions of Rule 3 only apply to the Participants described in paragraph (e) of the rule – namely, registered IBs and registered market makers, as well as any Participant for which the Exchange is the Designated Examining Authority. The Exchange also amended paragraph (e) to state that any other Participant also is required to maintain the information specified in Rule 3 to the extent such information is required to be maintained pursuant to the Exchange Act and the rules thereunder or, as previously set forth in the pre-existing version of paragraph (e), pursuant to the rules of the other self-regulatory organizations of which they are members. In addition, the Exchange clarified that proprietary orders fall under the purview of Article 11, Rule 3. Specifically, the Exchange deleted from paragraph .01 under the Interpretations and Policies of Article 11, Rule 3 the sentence stating that a decision by a Participant to buy or sell securities for his or her own account on the Exchange shall not constitute an order for which a record must be made under the rule. Further, the Exchange amended paragraph .03 under the Interpretations and Policies of Article 11, Rule 3 to state that a Participant that sends or receives orders, cancellations and executions through the matching system or through any other electronic system that the Exchange expressly recognizes as providing the required information in a format acceptable to the Exchange is not required to maintain separate records of such orders, cancellations and executions.

process of law, and for other legitimate business purposes. Further, new Rule 7(b) states that the Exchange charges IBs the fees specified in its published Schedule of Fees and Assessments for the collection and retrieval of such information. New Rule 7(c) lists the specific information regarding component orders and trades related to QCT crosses that IBs are required to enter into the BBOS, as applicable. Specifically, new Rule 7(c) provides that, for all orders and trades described under amended Article 11, Rule 3(b)(27), IBs must record the following information into the BBOS, as applicable: (1) QCT Type; (2) Related Exchange; (3) Print Time; (4) Expiration Year; (5) Expiration Month; (6) Price; (7) Contracts; (8) Strike Price; (9) Call/Put; (10) Volume; and (11) Short Sale Indicator. *For purposes of recording such information into BBOS, the Exchange is requiring by notice that CHX IBs enter all information into BBOS as required under Article 11, Rule 7(c), no later than 4:30 p.m. on the following day in which the transaction occurred (T+1).*

#### C. Clarification Regarding IB Trading Accounts

Article 17, Rule 3(c) provides that each IB must maintain separate accounts for handling agency transactions, principal transactions, and transactions involving errors, and must enter transactions into the appropriate accounts. The Exchange amended this rule to clarify that the required accounts relate to special recordkeeping accounts that must be maintained at the Exchange, which is necessary for the Exchange to adequately surveil and examine the relevant IB trading activity, as well as to provide additional detail as to the types of transactions that must be recorded in the respective accounts. Accordingly, the Exchange amended Article 17, Rule 3(c) to state that each IB must establish and maintain separate CHX recordkeeping accounts at the Exchange for the sole purpose of recording the following activity: (1) an agency recordkeeping account for agency transactions; (2) a principal recordkeeping account for principal and riskless principal transactions; and (3) an error recordkeeping account for transactions involving only bona fide errors. The amended rule states that an IB must record each above-mentioned transaction into the appropriate CHX recordkeeping account.

#### D. Clarification Regarding Cross Orders

The Exchange also amended its rules to the operation of cross orders and Cross With Size handling and to eliminate redundant language in those rules. Specifically, the Exchange amended the definition of “cross order” to state that a cross order may only execute within the Exchange’s matching system if it is priced better than the working price, as defined under Article 1, Rule 1(pp), of all resting orders on the CHX Book. The Exchange notes that the amended definition is intended to clarify that while the pricing requirement is a prerequisite for executing a cross order within the matching system, a cross order that does not meet the pricing requirement is still, by definition, a cross order for purposes of the Exchange’s rules. The Exchange also amended Article 1, Rule 2(g)(1), which defines and sets forth special order handling requirements for Cross With Size orders, to state that a cross order that meets the Cross With Size definition will execute if there are no resting orders on the CHX Book with a working price better than the cross order. In addition, the Exchange amended Article 20, Rule 8(e)(1), which specifies how certain order types will be executed in the matching system, to remove references to Cross With Size and to state that cross orders are to be handled pursuant to Article 1, Rule 2(a)(2) and Rule 2(g)(1); because Cross With Size is a special handling for cross orders, and not itself an order type or order modifier.

IBs are reminded of their responsibility to ensure the timely, accurate and complete reporting of all transactions that they execute. IBs are also reminded that they must have appropriate systems, written supervisory procedures and internal controls to ensure compliance with general trading rules and recordkeeping requirements articulated in Article 11, Rule 3 and Article 17, Rule 3.

For operational questions concerning BBOS, please contact the CHX Trading Operations Department at (312) 663-2111.

For any regulatory questions or inquiries regarding this notice, please contact the undersigned at (312) 663-2548 or [mdonovan@chx.com](mailto:mdonovan@chx.com).

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