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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-91524; File No. SR-Phlx-2021-07]

Self-Regulatory Organizations; Nasdaq PHLX LLC; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, to Permit the Listing and Trading of Options Based on 1/100<sup>th</sup> the Value of the Nasdaq-100 Index

April 9, 2021.

## I. Introduction

On February 10, 2021, Nasdaq PHLX LLC (“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 permit the listing and trading of index options on based on 1/100<sup>th</sup> the value of the Nasdaq-100 Index . The proposed rule change was published for comment in the Federal Register on February 26, 2021.<sup>3</sup> On March 17, 2021, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>4</sup> The Commission is approving the proposed rule change, as modified by Amendment No. 1, subject to a pilot period set to expire on November 4, 2021.

## II. Description of the Proposed Rule Change, as Modified by Amendment No. 1

The Exchange is proposing to amend its rules to permit the listing and trading of index options on the Nasdaq 100 Micro Index (“XND”) on a pilot basis. The Exchange states that the

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<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. 91178 (February 22, 2021), 86 FR 11807.

<sup>4</sup> In Amendment No. 1, the Exchange amended the proposal to: (1) extend the duration of the proposed pilot period for XND options from May 4, 2021 to November 4, 2021; and (2) specify that the Exchange intends to begin implementation of the proposed rule change prior to May 1, 2021. Because Amendment No. 1 to the proposed rule change is technical in nature and does not materially alter the substance of the proposed rule change or raise any novel regulatory issues, it is not subject to notice and comment. Amendment No. 1, which amended and replaced the original proposal in its entirety, is available on the Commission’s website at: <https://www.sec.gov/comments/sr-phlx-2021-07/srphlx202107-8513064-230103.pdf>.

XND options contract will be the same in all respects as the current Nasdaq-100 Index (“NDX”) options contract listed on the Exchange,<sup>5</sup> except that it will be based on 1/100<sup>th</sup> of the value of the Nasdaq-100 Index, and will be P.M.-settled with an exercise settlement value based on the closing index value of the Nasdaq-100 Index on the day of expiration.<sup>6</sup> In particular, XND options will be subject to the same rules that presently govern the trading of index options based on the Nasdaq-100 Index, including sales practice rules, margin requirements, trading rules, and position and exercise limits. Like NDX options, XND options will be European-style and cash-settled, and will have a contract multiplier of 100. XND options will have a minimum trading increment of \$0.01 for all series.<sup>7</sup> Strike price intervals will be set at \$2.50 or greater, subject to conditions described in Options 4A, Section 12(a)(2).<sup>8</sup> Consistent with the Exchange’s existing rules for index options, the Exchange will allow up to six expiration months at any one time that may expire at three-month intervals or in consecutive months, as well as LEAPS.<sup>9</sup> The Exchange states that, pursuant to Phlx Options 4A, Section 12(b)(5), XND options may be listed

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<sup>5</sup> See Options 4A, Section 12(e)(II).

<sup>6</sup> The Exchange notes that similar features are available with other index options contracts listed or approved for trading on the Exchange and other options exchanges, including the Exchange’s affiliate, Nasdaq ISE, LLC (“ISE”), which lists options contracts based on 1/5<sup>th</sup> the value of the Nasdaq-100 (“NQX”). See Amendment No. 1, supra note 4, at 5.

<sup>7</sup> More specifically, the Exchange proposes that as long as QQQ options participate in the Penny Interval Program, XND options shall have a minimum increment of \$.01. See proposed Supplementary Material .03 to Options 3, Section 3.

<sup>8</sup> Generally, pursuant to Options 4A, Section 12(a)(2), except as provided in Supplementary Material .04 to Options 4A, Section 12, index options listed on the Exchange are subject to strike price intervals of no less than \$5, provided that certain classes of index options (including Reduced Value NDX options) have strike price intervals of no less than \$2.50. The Exchange proposes to amend Options 4A, Section 12(a)(2) to add XND options to the list of classes where strike price intervals of no less than \$2.50 are generally permitted, if the strike price is less than \$200. The Exchange will not list long term index options series (“LEAPS”) on XND options at intervals less than \$5. If the Exchange determines to add XND options to the Short Term Option Series (“STOS”) or Quarterly Option Series programs, such options will be listed with the expirations and strike prices described in Supplementary Material .02 to Options 4A, Section 12. The Exchange notes that it expects to add XND options to the STOS program. See Amendment No. 1, supra note 4 at 11, n.18.

<sup>9</sup> See id. at 11 & n.16.

and traded in accordance with the Nonstandard Expirations Pilot Program, which permits the Exchange to list Weekly Expirations<sup>10</sup> and End of Month (“EOM”) Expirations<sup>11</sup> on any broad-based index<sup>12</sup> eligible for standard options trading. XND options will have European-style exercise and will not be subject to position limits, although the Exchange proposes to amend Options 4A, Section 6 to describe how positions in micro index value options would be aggregated with full value and reduced value options.<sup>13</sup>

As proposed, XND options would be subject to a pilot for a period that would end on November 4, 2021 (“Pilot Program”). If the Exchange were to propose an extension of the Pilot Program or should the Exchange propose to make the Pilot Program permanent, then the Exchange would submit a filing proposing such amendments to the Pilot Program. The Exchange notes that any positions established under the pilot would not be impacted by the expiration of the pilot. For example, a position in an XND options series that expires beyond the conclusion of the pilot period could be established during the pilot. If the Pilot Program were not extended, then the position could continue to exist. However, the Exchange notes that any further trading in the series would be restricted to transactions where at least one side of the trade is a closing transaction.

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<sup>10</sup> Weekly Expirations may expire on any Monday, Wednesday, or Friday (other than the third Friday-of-the-month or days that coincide with an EOM expiration). See Options 4A, Section 12(b)(5).

<sup>11</sup> EOMs expire on last trading day of the month. See Options 4A, Section 12(b)(5).

<sup>12</sup> The Exchange states XND is a broad-based index. See Amendment No. 1, supra note 4, at 4, n. 6. To the extent the Exchange lists XND options pursuant to the Nonstandard Expirations Pilot Program, the Exchange would be required to provide the same information with respect to XND that it does for others options listed pursuant to the Nonstandard Expirations Pilot Program in the reports and data it provides to the Commission.

<sup>13</sup> For a more detailed description of the proposed XND contract, see Amendment No. 1, supra note 4. The Exchange also proposes to add new Options 4A, Section 12(a)(5) titled “European-Style Exercise” to clarify in the Exchange’s rules which Exchange-listed index options will trade European-Style Exercise, and to add rule text within Options 4A, Section 12(b)(2), which describes LEAPS, to specifically allow for the listing of long term options series on XND.

The Exchange proposes to submit a Pilot Program report to Commission at least two months prior to the expiration date of the Pilot Program (the “annual report”). The annual report would contain an analysis of volume, open interest, and trading patterns. The analysis would examine trading in the proposed option product as well as trading in the securities that comprise the Nasdaq-100 Index. In addition, for series that exceed certain minimum open interest parameters, the annual report would provide analysis of index price volatility and share trading activity. In addition to the annual report, the Exchange would provide the Commission with periodic interim reports while the Pilot Program is in effect that would contain some, but not all, of the information contained in the annual report. The annual report would be provided to the Commission on a confidential basis. The annual report would contain the following volume and open interest data:

- (1) monthly volume aggregated for all trades;
- (2) monthly volume aggregated by expiration date;
- (3) monthly volume for each individual series;
- (4) month-end open interest aggregated for all series;
- (5) month-end open interest for all series aggregated by expiration date; and
- (6) month-end open interest for each individual series.

In addition to the annual report, the Exchange would provide the Commission with interim reports of the information listed in items (1) through (6) above periodically as required by the Commission while the Pilot Program is in effect. These interim reports would also be provided on a confidential basis.

Finally, the annual report would contain the following analysis of trading patterns in third Friday of the month (“Expiration Friday”), P.M.-settled XND option series in the Pilot Program:

- (1) a time series analysis of open interest; and (2) an analysis of the distribution of trade sizes.

Also, for series that exceed certain minimum parameters, the annual report would contain the following analysis related to index price changes and underlying share trading volume at the

close on Expiration Fridays: a comparison of index price changes at the close of trading on a given Expiration Friday with comparable price changes from a control sample. The data would include a calculation of percentage price changes for various time intervals and compare that information to the respective control sample. Raw percentage price change data as well as percentage price change data normalized for prevailing market volatility, as measured by an appropriate index as agreed by the Commission and the Exchange, would be provided. The Exchange would provide a calculation of share volume for a sample set of the component securities representing an upper limit on share trading that could be attributable to expiring in-the-money series. The data would include a comparison of the calculated share volume for securities in the sample set to the average daily trading volumes of those securities over a sample period. The minimum open interest parameters, control sample, time intervals, method for randomly selecting the component securities, and sample periods would be determined by the Exchange and the Commission.<sup>14</sup>

### III. Discussion and Commission Findings

After careful consideration of the proposal, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange,<sup>15</sup> and, in particular, the requirements of Section 6 of the Act.<sup>16</sup> Specifically, the Commission finds that the proposed rule change, as Modified by Amendment No. 1, is consistent with Section 6(b)(5) of the Act,<sup>17</sup>

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<sup>14</sup> See *id.* The proposed Pilot Program for XND options is similar to the pilot program approved for the listing and trading of P.M.-settled options on the full value of the Nasdaq-100 (“NDXPM”) on the Exchange and NQX options on ISE. See Securities Exchange Act Release Nos. 81293 (August 2, 2017), 82 FR 37138 (August 8, 2017)(“NDXPM Order”) and 82911 (March 20, 2018), 83 FR 12966 (March 26, 2018) (“NQX Order”).

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

<sup>16</sup> 15 U.S.C. 78f.

<sup>17</sup> 15 U.S.C. 78f(b)(5).

which requires that an exchange have rules designed to remove impediments to and perfect the mechanism of a free and open market and to protect investors and the public interest, to allow the Exchange to conduct a limited, and carefully monitored, pilot as proposed.

The Commission has previously approved the listing and trading of options based on a reduced value of the Nasdaq-100 Index,<sup>18</sup> including P.M.-settled reduced value options,<sup>19</sup> and, as stated in the Commission's order approving the listing and trading of NDXPM on the Exchange on a pilot program basis, the Commission has had concerns about the potential adverse effects and impact of P.M. settlement upon market volatility and the operation of fair and orderly markets on the underlying cash market at or near the close of trading, including for cash-settled derivatives contracts based on a broad-based index.<sup>20</sup> The potential impact today remains unclear, given the significant changes in the closing procedures of the primary markets in recent decades. The Commission is mindful of the historical experience with the impact of P.M. settlement of cash-settled index derivatives on the underlying cash markets, but recognizes that these risks may be mitigated today by the enhanced closing procedures that are now in use at the primary equity markets.

For the reasons described below, the Commission believes that the Exchange's proposed XND Pilot Program is designed to mitigate concerns regarding P.M. settlement and will provide additional trading opportunities for investors while providing the Commission with data to monitor the effects of XND options and the impact of P.M. settlement on the markets. To assist

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<sup>18</sup> See, e.g., Securities Exchange Act Release Nos. 57654 (April 11, 2008), 73 FR 21003 (April 17, 2008) and 51121 (February 1, 2005), 70 FR 6476 (February 7, 2005).

<sup>19</sup> See NQX Order, *supra* note 14.

<sup>20</sup> See NDXPM Order, *supra* note 14, at 37140. See also Securities Exchange Act Release Nos. 64599 (June 3, 2011), 76 FR 33798, 33801-02 (June 9, 2011) (order instituting proceedings to determine whether to approve or disapprove a proposed rule change to allow the listing and trading of SPXPM options); 65256 (September 2, 2011), 76 FR 55969, 55970-76 (September 9, 2011) (order approving proposed rule change to establish a pilot program to list and trade SPXPM options); and 68888 (February 8, 2013), 78 FR 10668, 10669 (February 14, 2013) (order approving the listing and trading of SPXPM on CBOE).

the Commission in assessing any potential impact of a P.M.-settled XND option on the options markets as well as the underlying cash equities markets, the Exchange will be required to submit data to the Commission in connection with the Pilot Program. The Commission believes that the Exchange's proposed Pilot Program, together with the data and analysis that the Exchange will provide to the Commission, will allow the Exchange and the Commission to monitor for and assess any potential for adverse market effects of allowing P.M. settlement for XND options, including on the underlying component stocks. In particular, the data collected from the Exchange's XND Pilot Program will help inform the Commission's consideration of whether the Pilot Program should be modified, discontinued, extended, or permanently approved. Furthermore, the Exchange's ongoing analysis of the Pilot Program should help it monitor any potential risks from large P.M.-settled positions and take appropriate action on a timely basis if warranted.

The Exchange represents that it has adequate surveillance procedures to monitor trading in these options thereby helping to ensure the maintenance of a fair and orderly market, and has represented that it has sufficient capacity to handle additional traffic associated with this new listing.<sup>21</sup>

For the reasons discussed above, the Commission finds that the Exchange's proposal is consistent with the Act, including Section 6(b)(5) thereof, in that it is designed to remove impediments to and perfect the mechanism of a free and open market, and, in general, to protect investors and the public interest. In light of the enhanced closing procedures at the underlying markets and the potential benefits to investors discussed by the Exchange in its filing,<sup>22</sup> the Commission finds that it is appropriate and consistent with the Act to approve the Exchange's

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<sup>21</sup> See Amendment No. 1, *supra* note 4, at 17. In addition, the Commission notes that the Exchange would have access to information through its membership in the Intermarket Surveillance Group with respect to the trading of the securities underlying the XND, as well as tools such as large options positions reports to assist its surveillance of XND options.

<sup>22</sup> See Amendment No. 1, *supra* note 4.

proposal on a pilot basis. The collection of data during the Pilot Program and the Exchange's active monitoring of any effects of XND options on the markets will help the Exchange and the Commission assess any impact of P.M. settlement in today's market.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>23</sup> that the proposed rule change (SR-Phlx-2021-07), as modified by Amendment No. 1, be, and hereby is, approved, subject to a pilot period set to expire on November 4, 2021.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>24</sup>

J. Matthew DeLesDernier,  
Assistant Secretary.

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<sup>23</sup> 15 U.S.C. 78s(b)(2).

<sup>24</sup> 17 CFR 200.30-3(a)(12).