

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-73540; File No. SR-NASDAQ-2014-099)

November 6, 2014

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Cancel-Replacement and Route Timer

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 October 28, 2014, The NASDAQ Stock Market LLC (“NASDAQ” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASDAQ. 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

NASDAQ proposes to add specificity to the Exchange’s options trading rules. The NASDAQ Options Market (“NOM”) is Nasdaq’s facility for executing and routing standardized equity and index options. The Exchange proposes to define cancel-replacement orders and also describe a route timer in Chapter VI, entitled “Trading Systems.”

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

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

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

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, Proposed Rule Change

1. Purpose

The Exchange is proposing to amend Chapter VI to add additional specificity to its rules. The Exchange proposes to amend Section 1, Definitions, to define a cancel- replacement order. The Exchange proposes to amend Section 11, Order Routing, to add greater specificity to the Rulebook concerning a route timer.

Cancel-Replacement Orders

A market participant today has the option of either sending in a cancel order and then separately sending in a new order which serves as a replacement of the original order (two separate messages) or sending a single cancel-replacement order in one message.

If an order is submitted to the System and then subsequently a cancel order is sent to the System cancelling the original order, the original order will be cancelled by the System provided the original order was not already filled partially or in its entirety. A subsequent replacement order would be treated as a new order by the System and will not retain the priority of the cancelled order.

An order that is entered as one single message (“cancel-replacement order”) containing

two orders (versus two messages as described above) will also result in the original order being cancelled, provided the original order was not already filled partially or in its entirety.<sup>3</sup> The replacement order will be considered a new order by the System and will have time priority as of the time that order is entered into the System, except in the case that the replacement order only serves to reduce the size of the order. A cancel-replacement order which only reduces the size of the order will continue to retain the priority of the original order.<sup>4</sup> The replacement order will not retain the priority of the cancelled order except when the replacement reduces the size of the order and all other terms and conditions are retained. This is similar to the manner in which partially executed orders are prioritized in the System.

By way of example, if the original order is for 600 contracts and a market participant submits a cancel-replacement order for 600 contracts and in doing so, amends a term or condition such as the order type, presuming the original order was not filled in its entirety or partially, the entire original order would be cancelled. If the original order is for 600 contracts and a market participant submits a cancel-replacement order for 600 contracts and in doing so, amends a term or condition such as the order type, and 600 contracts were already filled, the cancel-replacement order would be returned to the market participant. If the original order is for 600 contracts and a market participant submits a cancel-replacement order for 600 contracts and in doing so, amends a term or condition such as the order type, and 300 contracts were already filled, the order would be modified to 300 contracts. Finally, if the original order is for 600

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<sup>3</sup> With cancel-replacement orders, the original order is automatically canceled or reduced by the number of contracts that were executed depending on the volume of the original order that was filled. The market participant is required to enter the original order reference number when a cancel-replacement order is sent to the System as one message.

<sup>4</sup> When a cancel-replacement order is sent to the System as one message the original order number reference is maintained by the System.

contracts and a market participant submits a cancel-replacement order solely reducing the size of the order by 300 contracts, the order would be modified to 300 contracts and the original order would retain its priority. In the previous examples provided, the orders would not retain the priority of the original orders.

The Exchange proposes to add the following definition in Chapter VI, Section 1, “Cancel-replacement order shall mean a single message for the immediate cancellation of a previously received order and the replacement of that order with a new order with new terms and conditions. If the previously placed order is already filled partially or in its entirety, the replacement order is automatically canceled or reduced by the number of contracts that were executed. The replacement order will not retain the priority of the cancelled order except when the replacement order reduces the size of the order and all other terms and conditions are retained.” This language is being added to Section 1(e)(1) to reflect the manner in which cancel-replacement orders function today. This filing does not reflect a change to the System; rather, the Exchange is memorializing in its rules the manner in which cancel-replacement orders are treated today.

#### Route Timer

Today, the System provides a number of routing options pursuant to which orders are sent to other available market centers for potential execution, per the entering market participant's instructions.<sup>5</sup> The System routing options are SEEK or SRCH. With SEEK and SRCH, an order will first check the System for available contracts for execution. After checking the System for available contracts, orders are sent to other available market centers for potential execution, per the entering firm's instructions.

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<sup>5</sup> Participants can designate orders as either available for routing or not available for routing. See Chapter VI, Sec. 11(a).

The Exchange proposes to add language in a new Section 11(a)(1)(C) to specify that after an order is initially routed,<sup>6</sup> pursuant to either the SEEK or SRCH routing option, the order will post to the book and will be routed after a time period (“Route Timer”) not to exceed one second as specified by the Exchange on its website provided that the order’s limit price would lock or cross other market center(s).<sup>7</sup> If, during the Route Timer, any new interest arrives opposite the order that is equal to or better than the away best bid or offer (“ABBO”) price, the order will trade against such new interest at the ABBO price. Eligible unexecuted orders will be routed at the end of the Route Timer provided the order was not filled and the order’s limit price would continue to lock or cross the ABBO. If an order was routed with either the SEEK or SRCH routing option, and has size after such routing, it will execute against contra side interest in the book, post in the book, and route again pursuant to the process described above, if applicable, if the order’s limit price would lock or cross another market center(s).

This language is being added to Section 11 to reflect the manner in which the Exchange imposes a Route Timer on routed orders today to permit quote updates to occur prior to subsequent routing. This filing does not reflect a change to the System, rather the Exchange is memorializing in its rules the manner in which orders are routed today.

The Exchange also proposes to amend rule text in Section 11(a)(1)(A) of Chapter VI concerning the SEEK routing option. The Exchange proposes to add language which clarifies the differences between SEEK and SRCH routing options with respect to contracts that remain

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<sup>6</sup> If an order is only partially routed the portion that was not routed will be posted to the book.

<sup>7</sup> Pursuant to Section 11(c) of Chapter VI, orders sent by the System pursuant to the SEEK and SRCH routing options to other markets would not retain time priority with respect to other orders in the System. If an order routed pursuant to SEEK or SRCH is subsequently returned, in whole or in part, that order, or its remainder, will receive a new time stamp reflecting the time of its return to the System.

un-executed after routing and are posted on the book. The Exchange proposes to state, “Once on the book at the limit price, should the order subsequently be locked or crossed by another market center, the System will not route the order to the locking or crossing market center.” The Exchange believes this language more clearly differentiates an order routed pursuant to SEEK as compared to the SRCH routing option. An order routed pursuant to the SEEK routing option is routable until it is posted at its limit price. Once posted at its limit price, an order routed pursuant to the SEEK routing option would not continue to route, as compared to an order routed pursuant to the SRCH routing option. An order routed pursuant to the SRCH routing option is routable for the life of the order. The routing functionality is similar to functionality currently on Phlx.<sup>8</sup>

The Exchange also proposes to correct a typographical error in Chapter VI, Section 11(a)(1).

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act<sup>9</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act<sup>10</sup> in particular, in that it is 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 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.

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<sup>8</sup> See Phlx Rule 1080(m).

<sup>9</sup> 15 U.S.C. 78f(b).

<sup>10</sup> 15 U.S.C. 78f(b)(5).

The Exchange believes that its proposal to define cancel-replacement orders will add transparency to the rules. The Exchange is not amending the manner in which the System handles these orders. The Exchange is memorializing, in its rules, the method by which orders are handled by the System. The Exchange is defining cancel-replacement orders within Chapter VI, Section 1.

Specifically, with respect to cancel-replacement orders that reduce size, the Exchange believes that allowing cancel-replacement orders where only size is reduced to retain the priority of the original order is consistent with the manner in which the Exchange treats partially executed orders, which similarly apply the priority of the executed portion of the order to the remaining portion of the order. In addition, by permitting market participants' orders to remain on the book with the original priority and reduced size, the Exchange is providing market participants an ability to reduce exposure. The Exchange believes that adding transparency and specificity to the Rules protects investors and the public interest by reducing the potential for investor confusion.

The Exchange is also memorializing the manner in which the Exchange routes unexecuted portions of an order that will be subsequently routed to other markets when it comes back and subsequently locks and/or crosses the market. The Exchange will continue to re-route eligible unexecuted orders pursuant to a Route Timer. Contracts which remain unexecuted will be posted to the book provided the order's limit price would not lock or cross the ABBO. Specifically, the Exchange is describing the Route Timer that applies to eligible unexecuted portions of an order which will be subsequently routed. The timer protects investors and the public interest by providing a brief time period to allow the opportunity for markets to update quotes prior to subsequent routes.

The Exchange seeks to add language concerning the specific manner in which the Exchange will handle the routed order by specifying the routing methods in which SEEK or SRCH orders will route to the away market(s). The Exchange is adding clarifying language to make clear that after an order is initially routed, pursuant to either the SEEK or SRCH routing option, the order will post to the book and will be routed after a time period (“Route Timer”) not to exceed one second as specified by the Exchange on its website provided that the order would lock or cross other market center(s). If, during the Route Timer, any new interest arrives opposite the order that is equal to or better than the ABBO price, the order will trade against such new interest at the ABBO price. Eligible unexecuted orders will be routed at the end of the Route Timer provided the order was not filled and it would continue to lock or cross the ABBO. If an order was routed with either the SEEK or SRCH routing option, and has size after such routing, it will execute against contra side interest in the book, post in the book, and route again pursuant to the process described above, if applicable, if the order would lock or cross another market center(s).

Further, the proposal to amend rule text in Section 11(a)(1)(A) of Chapter VI concerning SEEK orders clarifies the differences between SEEK and SRCH routing options with respect to contracts that remain un-executed after routing and are posted on the book. The Exchange seeks to clearly note that once an order routed pursuant to the SEEK routing option is on the order book at the limit price, it will not route, despite the order locking or crossing another market center. The Exchange believes this language more clearly differentiates an order routed pursuant to the SEEK routing option as compared to SRCH routing option.

The Exchange believes this language adds specificity and detail to the rule text so that market participants may anticipate the manner in which orders are handled by the Exchange



when routing. The Exchange believes that adding transparency and specificity to the Rules protects investors and the public interest by reducing the potential for investor confusion.

The Exchange's proposal is intended to provide additional specificity to the rules in the manner in which the System treats cancel-replacement orders and handles routing of eligible unexecuted portions of previously routed orders, which is designed to promote just and equitable principles of trade.

The Exchange is not proposing to amend the manner in which the System operates. Cancel-replacement orders have been treated in this fashion since NOM was first launched. Further, the Routing Timer for subsequent routes has also been in place on NOM since its launch. The Exchange is proposing these additions to the rules in order to provide greater specificity to the Exchange's rules.

B. Self-Regulatory Organization's Statement on Burden on Competition

Nasdaq does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The Exchange is seeking to provide greater transparency in its rules. The amendments are non-substantive and would apply to all market participants in the same manner. Permitting cancel-replacement orders to retain their original priority does not impose a burden on competition because the priority is retained only in the instance that size alone is changed and only if it is reduced. Permitting all market participants to reduce their exposure without penalty does not burden competition, rather it promotes competition by allowing participants the ability to change their orders in a changing market, provided the order was not already partially filled or filled in its entirety.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

No Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act<sup>11</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>12</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved. The Exchange has provided the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change.

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<sup>11</sup> 15 U.S.C. 78s(b)(3)(a)(ii).

<sup>12</sup> 17 CFR 240.19b-4(f)(6).

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASDAQ-2014-099 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

All submissions should refer to File Number SR-NASDAQ-2014-099. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of NASDAQ. All comments received will be posted without change; the

Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASDAQ-2014-099 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>13</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>13</sup> 17 CFR 200.30-3(a)(12).