

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-75536; File No. SR-BX-2015-042)

July 28, 2015

Self-Regulatory Organizations; NASDAQ OMX BX, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Rule 4702 to Introduce a Market Maker Peg Order for Use on BX

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 July 17, 2015, NASDAQ OMX BX, Inc. (“BX” 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 the Exchange. 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

The Exchange proposes to amend Rule 4702 to introduce a Market Maker Peg Order for use on BX.

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

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

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

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

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, the Proposed Rule Change

1. Purpose

The Exchange is proposing to introduce a Market Maker Peg Order (“MMPO”) for use on BX by registered BX Market Makers. The MMPO, which is currently available for use on The NASDAQ Stock Market (“NASDAQ”)<sup>3</sup> and NASDAQ OMX Phlx (“PHLX”) PSX System,<sup>4</sup> is an order type that provides a means by which a market maker may comply with its market making obligations under applicable Exchange rules.<sup>5</sup> Although the Exchange has rules allowing market making on BX, it does not currently have any market makers registered with the Exchange. In an effort to attract market makers, BX is proposing to introduce the MMPO, which will facilitate BX market maker compliance with BX quoting obligations.<sup>6</sup> The MMPO is available for use only by BX Market Makers because these obligations are not applicable to other market participants. The MMPO is available only through the Exchange’s RASH and FIX connectivity protocols, because these are the only protocols that support continuous pegging functionality.

BX Rule 4613 requires a member firm registered as a Market Maker in a particular security to be willing to buy and sell such security for its own account on a continuous basis during regular market hours and to enter and maintain a two-sided trading interest (“Two-Sided

<sup>3</sup> See NASDAQ Rule 4702(b)(7).

<sup>4</sup> See PHLX Rule 3301A(b)(5).

<sup>5</sup> See Rule 4613. The MMPO is a “one-sided” order. Therefore a member firm exclusively employing the order type to comply with its market making obligations must enter both a buy and sell MMPO.

<sup>6</sup> Id.

Obligation”) that is identified to the Exchange as the interest meeting the obligation and is displayed in BX’s quotation montage at all times. Interest eligible to be considered part of a Market Maker’s Two-Sided Obligation must have a displayed quotation size of at least one normal unit of trading.<sup>7</sup> After an execution against its Two-Sided Obligation, a Market Maker must ensure that it has additional trading interest to satisfy its Two-Sided Obligation either by immediately entering new interest to comply with this obligation to maintain continuous two-sided quotations or by identifying existing interest on the BX book that will satisfy this obligation.

BX Market Makers must also adhere to certain pricing obligations established by Rule 4613, which are premised on entering quotation prices that are not more than a “Designated Percentage”<sup>8</sup> away from the National Best Bid or National Best Offer<sup>9</sup> (as applicable), and that must be refreshed if a change in the National Best Bid or National Best Offer causes the quotation price to be more than a “Defined Limit”<sup>10</sup> away from the National Best Bid or National

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<sup>7</sup> Unless otherwise designated, 100 shares.

<sup>8</sup> The “Designated Percentage” is: (i) 8% for securities subject to Rule 4120(a)(11) and are securities included in the S&P 500<sup>®</sup> Index, Russell 1000<sup>®</sup> Index, and a pilot list of Exchange Traded Products (“Tier 1 Securities”); 28% for securities subject to Rule 4120(a)(11) and that are all NMS stocks not Tier 1 Securities with a price equal to or greater than \$1 (“Tier 2 Securities”); and 30% for securities subject to Rule 4120(a)(11) and that are all NMS stocks not Tier 1 Securities with a price less than \$1 (“Tier 3 Securities”), except that between 9:30 a.m. and 9:45 a.m. and between 3:35 p.m. and the close of trading, when Rule 4120(a)(11) is not in effect, the Designated Percentage shall be 20% for Tier 1 Securities, 28% for all Tier 2 Securities, and 30% for Tier 3 Securities. See Rule 4613(a)(2)(D).

<sup>9</sup> As determined by the Exchange in accordance with its procedures for determining Protected Quotations under SEC Rule 600 under Regulation NMS.

<sup>10</sup> The “Defined Limit” is 9.5% for Tier 1 Securities, 29.5% for Tier 2 Securities, and 31.5% for Tier 3 Securities, except that between 9:30 a.m. and 9:45 a.m. and between 3:35 p.m. and the close of trading, when Rule 4120(a)(11) is not in effect, the Defined Limit shall be 21.5% Tier 1 Securities, 29.5% for Tier 2 Securities, and 31.5% for Tier 3 Securities. See Rule 4613(a)(2)(E).

Best Offer.<sup>11</sup> The pricing obligations established by the Rule apply during regular trading hours (i.e., 9:30 a.m. to 4:00 p.m.), but do not commence during any trading day until after the first regular way transaction on the primary listing market in the security. Moreover, the obligations are suspended during a trading halt, suspension, or pause, and do not re-commence until after the first regular way transaction on the primary listing market in the security following such halt, suspension, or pause, as reported by the responsible single plan processor. When the halt is lifted, the order will remain on the book unless cancelled by the market maker or if the displayed price is outside the permitted pricing range the order will be cancelled.

For bid quotations, at the time of entry of bid interest satisfying the Two-Sided Obligation, the displayed price of the bid interest may not be more than the applicable Designated Percentage away from the then current National Best Bid, or if no National Best Bid, not more than the Designated Percentage away from the last reported sale from the responsible single plan securities information processor. In the event that the National Best Bid (or if no National Best Bid, the last reported sale) increases to a level that would cause the bid interest of the Two-Sided Obligation to be more than the Defined Limit away from the National Best Bid (or if no National Best Bid, the last reported sale), or if the bid is executed or cancelled, the Market Maker must enter new bid interest at a displayed price not more than the Designated Percentage away from the then current National Best Bid (or if no National Best Bid, the last reported sale), or identify to the Exchange current resting interest that satisfies the Two-Sided Obligation. Similarly, for offer quotations, at the time of entry of offer interest satisfying the Two-Sided Obligation, the displayed price of the offer interest may not be more than the Designated Percentage away from the then current National Best Offer, or if no National Best

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<sup>11</sup> Nothing in Rule 4613 precludes a BX Market Maker from quoting at price levels that are closer to the National Best Bid and Offer than the levels required by the rule.

Offer, not more than the Designated Percentage away from the last reported sale received from the responsible single plan securities information processor. In the event that the National Best Offer (or if no National Best Offer, the last reported sale) decreases to a level that would cause the offer interest of the Two-Sided Obligation to be more than the Defined Limit away from the National Best Offer (or if no National Best Offer, the last reported sale), or if the offer is executed or cancelled, the Market Maker must enter new offer interest at a displayed price not more than the Designated Percentage away from the then current National Best Offer (or if no National Best Offer, the last reported sale), or identify to the Exchange current resting interest that satisfies the Two-Sided Obligation.

The MMPO is designed to assist Market Makers in complying with these requirements by being repriced in accordance with the parameters required by Rule 4613. Thus, use of the order will allow market makers to make liquidity available at prices reasonably related to the National Best Bid and National Best Offer, even in circumstances where they are not themselves quoting at the best price or have more limited liquidity available at the best price. Specifically, the MMPO is a limit order that, upon entry, is automatically priced by the BX System at the Designated Percentage away from the Reference Price to keep the displayed price of the order bounded within a price range, thereby allowing the market maker to comply with the quotation requirements under Rule 4613(a)(2). The Reference Price is the then current National Best Bid (National Best Offer), or if no National Best Bid (National Best Offer), the most recent reported last-sale eligible trade from the responsible single plan processor for that day, or if none, the previous closing price of the security as adjusted to reflect any corporate actions (e.g., dividends or stock splits) in the security. For example, if the National Best Bid was \$10 in a Tier 1 Security, the Designated Percentage would be 8%, an MMPO to buy entered between 9:45 a.m.

and 3:45 p.m. would be priced at \$9.20.<sup>12</sup> Because the order is designed to post to the book at the Designated Percentage, it would not be marketable upon entry and therefore may not be entered with a time-in-force of Immediate-or-Cancel. As a result, an MMPO would provide, rather than access, liquidity. The order may not be assigned any special conditions governing its terms of execution, other than time-in-force, limit price, and the pegging functionality described herein.

Upon reaching the Defined Limit, the displayed price of an MMPO will be repriced by the System to the Designated Percentage away from the then current Reference Price. Thus, if the National Best Bid in the above example increased to \$10.17, the MMPO priced at \$9.20 would now be more than 9.5%, the Defined Limit, away from the National Best Bid, and would be repriced to \$9.35, the Designated Percentage away from \$10.17.

An MMPO order could execute in the circumstances shown below. The best bid in a particular security is currently \$10.00 and all MMPO's in the security are currently priced at \$9.50 with no other bids resting between those two prices. If the \$10.00 bid were cancelled or executed, the MMPO's resting at \$9.50 would become the inside market and would then be available for execution against any order willing to sell at \$9.50 or lower. Alternatively, assume there is a bid for 100 shares at \$10.00 and the next order on the book is the MMPO resting at \$9.50 for 100 shares. If a 200 share order to sell at \$9.50 is received, it would execute 100 shares against the \$10.00 bid and 100 shares against the MMPO that is posted at \$9.50.

If as a result of a change to the Reference Price, the displayed price of a Market Maker Peg Order to buy (sell) is at least one minimum price variation more than (less than) a price that

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<sup>12</sup> As noted above, the MMPO is a limit order and therefore must be assigned a limit price beyond which it will not execute. If the repricing mechanism of the order would result in the order being priced at a level inconsistent with its limit price, the order will be rejected or cancelled.

is 4% less than (more than) the Reference Price, rounded up (down), then the price of the Market Maker Peg Order to buy (sell) will be re-priced to the Designated Percentage away from the Reference Price. Thus, if the National Best Bid was initially \$10 in a Tier 1 Security, and an MMPO to buy was initially entered at \$9.20, if the National Best Bid decreased to \$9.57 (such that the displayed price of the MMPO would be at least \$0.01 more than a price that is 4% less than the National Best Bid, rounded up (i.e.,  $\$9.57 - (\$9.57 \times 0.04) = \$9.1872$ , rounding up to \$9.19), the MMPO would be repriced to \$8.81 (8% away from the National Best Bid).<sup>13</sup>

For a given MMPO, a Market Maker may designate a more aggressive offset from the National Best Bid or National Best Offer than the given Designated Percentage, but such an offset will be expressed as a price difference from the Reference Price. Thus, for example, the Market Maker could designate an offset of \$0.25, in which case the order would be continually repriced to maintain the \$0.25 offset as the Reference Price moved. Thus, if the National Best Bid was \$10, an MMPO to buy with a \$0.25 offset would initially be priced at \$9.75, with the price rising or falling continually as the Reference Price moved.<sup>14</sup> If there is no Reference Price, an MMPO with a designated offset amount will be sent back to the Market Maker.

In the absence of a Reference Price, a Market Maker Peg Order will be cancelled (if on the BX Book) or rejected (if it is an incoming Order). If, after entry, a Market Maker Peg Order has a displayed price based on a Reference Price other than the National Best Bid or National Best Offer and such Market Maker Peg Order is established as the National Best Bid or National Best Offer, the Market Maker Peg Order will not be subsequently repriced in accordance with

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<sup>13</sup> If the resulting calculated price is \$9.185, the price would round up or down to the compliant price for the entering party, up for a buyer and down for a seller.

<sup>14</sup> An MMPO with an offset operates in a manner similar to a Primary Pegged Order with an offset amount (see Rule 4702(b(4))), but an MMPO is always displayed. Note also that if the repricing of an order with an offset amount would result in the order being priced at a level inconsistent with its limit price, the order will be rejected or cancelled.

this rule until a new Reference Price is established. Thus, if the last sale price on the consolidated tape was \$10 and an MMPO to buy is priced at \$9.20 and establishes the National Best Bid, the order will not then be repriced to maintain an offset from itself. Rather, the order will be repriced only once there is an independent basis pricing the order. In the event of an execution against an MMPO that reduces the size of the order below one round lot, the Market Maker would need to enter a new order (after performing required regulatory checks, as discussed below) to satisfy its obligations under Rule 4613.<sup>15</sup> If a Market Maker Peg Order is repriced 1,000 times, it will be cancelled.<sup>16</sup>

MMPOs are not eligible for routing pursuant to Rule 4758 and are always displayed on BX. Notwithstanding the availability of MMPO functionality, a Market Maker remains responsible for entering, monitoring, and resubmitting, as applicable, quotations that meet the requirements of Rule 4613. A new timestamp is created for an MMPO each time that its displayed price is automatically repriced. At a particular price, the order would be processed in regular price/time priority, with better priced interest being executed prior to the MMPO and with the MMPO being executed behind similarly priced orders entered before the MMPO is repriced.

Although Rule 4613 does not govern the pre-market trading session before 9:30 a.m. and the post-market trading session after 4:00 p.m., a Market Maker may enter an MMPO during such periods. In that case, the Designated Percentage and Defined Limit applicable to the

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<sup>15</sup> Rule 4613 generally sets forth BX Market Maker requirements, which include quotation and pricing obligations, and the firm quote obligation.

<sup>16</sup> BX limits the total number of repricings to 1,000 to control message traffic in the System. For example, a MMPO may be affected by a flickering quotation, which is a condition whereby the displayed quotation (off of which the MMPO is pegged) can change multiple times in a single second. The Exchange determined that, if the MMPO repricing was unlimited, the flickering quotation may cause unnecessary System traffic as the MMPO continually reprices in reaction to each rapid change of the quotation.



MMPO will be the same as for the periods from 9:30 a.m. through 9:45 a.m., as described in Rule 4613.<sup>17</sup> As BX does not have a special market opening or closing process, an MMPO does not behave differently at 9:30 a.m. or 4:00 p.m. than it does immediately before or after such times.

Use of the MMPO does not frustrate compliance with any broker-dealer risk management obligations required by SEC Rule 15c3-5 (the “Market Access Rule”), or any Regulation SHO marking and locate requirement prior to order entry. As such, use of the order is not inconsistent with Market Makers fulfilling their obligations under these rules, while also meeting their Exchange market making obligations. It should be noted, however, that use of the order does not ensure that the Market Maker is in compliance with its regulatory obligations under the Market Access Rule or Regulation SHO.

## 2. Statutory Basis

BX believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,<sup>18</sup> in general, and with Section 6(b)(5) of the Act,<sup>19</sup> in particular, in that the proposal 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 regulating, clearing, settling, processing information with respect to, and 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; and also in that it is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The Exchange believes that the MMPO will aid Market Makers in complying with the

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<sup>17</sup> Supra notes 8 and 10.

<sup>18</sup> 15 U.S.C. 78f.

<sup>19</sup> 15 U.S.C. 78f(b)(5).

requirements of Rule 4613. The Exchange further believes that compliance with this rule will remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest, because it will provide a means by which Market Makers may offer liquidity at prices that are reasonably related to the National Best Bid and National Best Offer, even in circumstances where they are not willing to quote at the inside market. As a result, in circumstances where liquidity available at displayed prices closer to the inside than the price of an MMPO is exhausted, the MMPO will nevertheless be available to support executions at prices that are not widely at variance with the prior inside market. Moreover, a Market Maker may elect to set a more aggressive offset from the National Best Bid or National Best Offer than the given Designated Percentage, which would support executions at prices closer to the prior inside market. Because the MMPO is repriced to avoid triggering a limit-up, limit-down restriction or a trading pause, it will not contribute to aberrant volatility in a particular stock.

The methodology for repricing an MMPO is consistent with the requirements of the Act because it will ensure that the displayed price of the order bears a reasonable relationship to the inside market and is less likely to execute at a price that would trigger a limit-up, limit-down restriction or a trading pause. Moreover, because the repricing of an MMPO results in a new timestamp being attached to the order, the MMPO does not provide a means by which an MMPO may achieve an execution priority superior to an order entered at that price earlier in time. In addition, the use of the MMPO would not be inconsistent with Market Makers fulfilling their obligations under the Market Access Rule and Regulation SHO.

The Exchange also believes that although the order may be used only by Market Makers, this restriction is not unfairly discriminatory because only Market Makers are subject to the

requirements of Rule 4613; accordingly, the order is not needed to assist other market participants in fulfilling regulatory obligations. To the extent that a market participant wishes to maintain an order at a displayed price that deviates from the inside market by a particular amount, however, it may use the Primary Peg Order to achieve this purpose. Accordingly, an alternative to the MMPO is already available to market participants.

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

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Specifically, the Exchange believes that the proposal will enhance BX's competitiveness by providing Market Makers on BX with a means to offer liquidity at prices reasonably related to the inside market. The Exchange believes that this functionality will be appealing to potential Market Makers, and therefore will make it more likely that market participants will choose to become active on BX. This may, in turn, increase the extent of liquidity available on BX and increase its ability to compete with other execution venues to attract orders that are seeking liquidity. The Exchange further believes that the introduction of the MMPO will not impair in any manner the ability of market participants or other execution venues to compete.

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

No written comments were either solicited or 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)(iii) of the Act<sup>20</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>21</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.

#### 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-BX-2015-042 on the subject line.

##### Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

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<sup>20</sup> 15 U.S.C. 78s(b)(3)(a)(iii).

<sup>21</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

All submissions should refer to File Number SR-BX-2015-042. 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 offices of the Exchange. 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-BX-2015-042, 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>22</sup>

Robert W. Errett  
Deputy Secretary

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<sup>22</sup> 17 CFR 200.30-3(a)(12).