

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-82573; File No. SR-NASDAQ-2018-005)

January 23, 2018

Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to the Criteria for Listing Underlying Securities

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 January 16, 2018, 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 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 Chapter IV, Section 3 (Criteria for Underlying Securities) of the rules governing the Nasdaq Options Market (“NOM”) to modify the criteria for listing an option on an underlying covered security.

The text of the proposed rule change is available on the Exchange’s Website at <http://nasdaq.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 the Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of the proposed rule change is to amend NOM Chapter IV, Section 3 to modify the criteria for listing options on an underlying security as defined in Section 18(b)(1)(A) of the Securities Act of 1933 (hereinafter “covered security” or “covered securities”). In particular, the Exchange proposes to modify Section 3(b)v.1) to permit the listing of an option on an underlying covered security that has a market price of at least \$3.00 per share for the previous three consecutive business days preceding the date on which the Exchange submits a certificate to the Options Clearing Corporation (“OCC”) for listing and trading. The Exchange does not intend to amend any other criteria for listing options on an underlying security in Chapter IV, Section 3.

This proposed rule change is identical to a recently-approved rule change by the Exchange’s affiliate, Nasdaq PHLX LLC (“Phlx”), to its initial listing standards,<sup>3</sup> and serves to align the rules of Phlx and the Exchange.

Currently the underlying covered security must have a closing market price of \$3.00 per share for the previous five consecutive business days preceding the date on which the Exchange submits a listing certificate to OCC. In the proposed amendment, the market price will still be measured by the closing price reported in the primary market in which the underlying covered

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<sup>3</sup> See Securities Exchange Act Release No. 82474 (January 9, 2018) (SR-Phlx-2017-75) (Order Granting Approval of a Proposed Rule Change) (“Phlx Filing”). The Exchange, together with its affiliates, Nasdaq BX, Inc. (“BX”) and Nasdaq ISE, LLC (“ISE”), all of which are wholly owned subsidiaries of Nasdaq, Inc. (“Nasdaq HoldCo”), have filed identical rule change proposals based on the Phlx Filing.

security is traded, but the measurement will be the price over the prior three consecutive business day period preceding the submission of the listing certificate to OCC, instead of the prior five business day period.

The Exchange acknowledges that the Options Listing Procedures Plan<sup>4</sup> requires that the listing certificate be provided to OCC no earlier than 12:01 a.m. and no later than 11:00 a.m. (Chicago time) on the trading day prior to the day on which trading is to begin.<sup>5</sup> The proposed amendment will still comport with that requirement. For example, if an initial public offering (“IPO”) occurs at 11 a.m. on Monday, the earliest date the Exchange could submit its listing certificate to OCC would be on Thursday by 12:01 a.m. (Chicago time), with the market price determined by the closing price over the three-day period from Monday through Wednesday. The option on the IPO would then be eligible for trading on the Exchange on Friday. The proposed amendment would essentially enable options trading within four business days of an IPO becoming available instead of six business days (five consecutive days plus the day the listing certificate is submitted to OCC).

The Exchange’s initial listing standards for equity options in Chapter IV, Section 3 (including the current price/time standard of \$3.00 per share for five consecutive business days)

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<sup>4</sup> The Plan for the Purpose of Developing and Implementing Procedures Designed to Facilitate the Listing and Trading of Standardized Options Submitted Pursuant to Section 11a(2)(3)(B) of the Securities Exchange Act of 1934 (a/k/a the Options Listing Procedures Plan (“OLPP”)) is a national market system plan that, among other things, sets forth procedures governing the listing of new options series. See Securities Exchange Act Release No. 44521 (July 6, 2001), 66 FR 36809 (July 13, 2001) (Order approving OLPP). The sponsors of OLPP include Nasdaq; OCC; BATS Exchange, Inc.; BOX Options Exchange LLC; C2 Options Exchange, Incorporated; Chicago Board Options Exchange, Incorporated; EDGX Exchange, Inc.; Miami International Securities Exchange, LLC; MIAX PEARL, LLC; Nasdaq PHLX LLC; Nasdaq BX, Inc.; Nasdaq GEMX, LLC; Nasdaq ISE, LLC; Nasdaq MRX, LLC; NYSE American, LLC; and NYSE Arca, Inc.

<sup>5</sup> See OLPP at page 3.

are substantially similar to the initial listing standards adopted by other options exchanges.<sup>6</sup> At the time the options industry adopted the “look back” period of five consecutive business days, it was determined that the five-day period was sufficient to protect against attempts to manipulate the market price of the underlying security and would provide a reliable test for stability.<sup>7</sup>

Surveillance technologies and procedures concerning manipulation have evolved since then to provide adequate prevention or detection of rule or securities law violations within the proposed time frame, and the Exchange represents that its existing trading surveillances are adequate to monitor the trading in the underlying security and subsequent trading of options on the Exchange.<sup>8</sup>

Furthermore, the Exchange notes that the scope of its surveillance program also includes cross market surveillance for trading that is not just limited to the Exchange. In particular, the Financial Industry Regulatory Authority (“FINRA”), pursuant to a regulatory services agreement, operates a range of cross-market equity surveillance patterns on behalf of the Exchange to look for potential manipulative behavior, including spoofing, algorithm gaming,

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<sup>6</sup> See, e.g., Phlx Rule 1009, Commentary .01.

<sup>7</sup> See Securities Exchange Act Release Nos. 47190 (January 15, 2003), 68 FR 3072 (January 22, 2003) (SR-CBOE-2002-62); 47352 (February 11, 2003), 68 FR 8319 (February 20, 2003) (SR-PCX-2003-06); 47483 (March 11, 2003), 68 FR 13352 (March 19, 2003) (SR-ISE-2003-04); 47613 (April 1, 2003), 68 FR 17120 (April 8, 2003) (SR-Amex-2003-19); and 47794 (May 5, 2003), 68 FR 25076 (May 9, 2003) (SR-Phlx-2003-27).

<sup>8</sup> Such surveillance procedures generally focus on detecting securities trading subject to opening price manipulation, closing price manipulation, layering, spoofing or other unlawful activity impacting an underlying security, the option, or both. As it relates to IPOs, the Exchange has price movement alerts, unusual market activity and order book alerts active for all trading symbols. These real-time patterns are active for the new security as soon as the IPO begins trading. The Nasdaq MarketWatch group, which provides such real-time surveillance on the Exchange and its affiliated markets, monitors trading activity in IPOs to see whether the new issue moves substantially above or below the public offering price in the first day or several days of trading.

marking the close and open, and momentum ignition strategies, as well as more general, abusive behavior related to front running, wash sales, quoting/routing, and Reg SHO violations. These cross-market patterns incorporate relevant data from various markets beyond the Exchange and its affiliates, including data from the New York Stock Exchange (“NYSE”).

Additionally for options, the Nasdaq Options Surveillance team utilizes an array of patterns that monitor manipulation of options, or manipulation of equity securities (regardless of venue) for the purpose of impacting options prices on any of the six Nasdaq HoldCo-operated options markets (i.e., mini-manipulation strategies). Surveillance coverage is initiated once options begin trading on any of Nasdaq HoldCo’s six options markets, including the Exchange. Accordingly, the Exchange believes that the cross market surveillance performed by FINRA on behalf of the Exchange, coupled with Exchange staff’s real-time monitoring of similarly violative activity on Nasdaq and its affiliated markets as described herein, reflects a comprehensive surveillance program that is adequate to monitor for manipulation of the underlying security and overlying option within the proposed three-day look back period.

Furthermore, the Exchange notes that the proposed listing criteria would still require that the underlying security be listed on NYSE, the American Stock Exchange (now known as NYSE American), or the National Market System of the Exchange (now known as the Nasdaq Global Market) (collectively, the “Named Markets”), as provided for in the definition of “covered security” from Section 18(b)(1)(A) of the 1933 Act.<sup>9</sup> Accordingly, the Exchange believes that the proposed rule change would still ensure that the underlying security meets the high listing standards of a Named Market, and would also ensure that the underlying is covered by the

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<sup>9</sup> See 15 U.S.C. 77r(b)(1)(A).

regulatory protections (including market surveillance, investigation and enforcement) offered by these exchanges for trading in covered securities conducted on their facilities.

In addition, the Exchange had no cases within the past five years where an IPO-related issue for which it had pricing information qualified for the \$3.00 price requirement during the first three days of trading and did not qualify for the \$3.00 price requirement during the first five days.<sup>10</sup> In other words, none of these qualifying issues fell below the \$3.00 threshold within the first three or five days of trading. As such, the Exchange believes that its existing surveillance program, coupled with its findings related to the IPO-related issues as described herein, adequately address potential concerns regarding possible manipulation or price stability within the proposed timeframe.

The Exchange also believes that the proposed look back period can be implemented in connection with the other initial listing criteria for underlying covered securities. In particular, the Exchange recognizes that it may be difficult to verify the number of shareholders in the days immediately following an IPO due to the fact that stock trades generally clear within two business days (T+2) of their trade date and therefore the shareholder count will generally not be known until T+2.<sup>11</sup> The Exchange notes that the current T+2 settlement cycle was recently reduced from T+3 on September 5, 2017 in connection with the Commission's amendments to

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<sup>10</sup> There were over 750 IPO-related issues on the Exchange within the past five years. Out of all of the issues with pricing information, there was only one issue that had a price below \$3 during the first five consecutive business days. The Exchange notes, however, that it allows for companies to list on the Nasdaq Capital Market at \$2.00 or \$3.00 per share in some instances, which was the case for this particular issue. See Rule 5500 Series for initial listing standards on the Nasdaq Capital Market.

<sup>11</sup> The number of shareholders of record can be verified from large clearing agencies such as The Depository Trust and Clearing Corporation ("DTCC") upon the settlement date (i.e., T+2).

Exchange Rule 15c6-1(a) to adopt the shortened settlement cycle,<sup>12</sup> and the look back period of three consecutive business days proposed herein reflects this shortened T+2 settlement period. As proposed, stock trades would clear within T+2 of their trade date (i.e., within three business days) and therefore the number of shareholders could be verified within three business days, thereby enabling options trading within four business days of an IPO (three consecutive business days plus the day the listing certificate is submitted to OCC).

Furthermore, the Exchange notes that it can verify the shareholder count with various brokerage firms that have a large retail customer clientele. Such firms can confirm the number of individual customers who have a position in the new issue. The earliest that these firms can provide confirmation is usually the day after the first day of trading (T+1) on an unsettled basis, while others can confirm on the third day of trading (T+2). The Exchange has confirmed with some of these brokerage firms who provide shareholder numbers to the Exchange that they are able to provide these numbers within T+2 after an IPO. For the foregoing reasons, the Exchange believes that basing the proposed three business day look back period on the T+2 settlement cycle would allow for sufficient verification of the number of shareholders.

The proposed rule change will apply to all covered securities that meet the relevant criteria in Chapter IV, Section 3. Pursuant to Section 3(b), Nasdaq Regulation establishes guidelines to be considered in evaluating potential underlying securities for NOM options transactions. However, the fact that a particular security may meet the standards established by Nasdaq Regulation does not necessarily mean that it will be selected as an underlying security.<sup>13</sup>

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<sup>12</sup> See Securities Exchange Act Release No. 78962 (September 28, 2016), 81 FR 69240 (October 5, 2016) (Amendment to Securities Transaction Settlement Cycle) (File No. S7-22-16).

<sup>13</sup> See Chapter IV, Section 3(b).

As part of the established criteria, the issuer must be in compliance with any applicable requirements of the Act and the rules thereunder.<sup>14</sup> Additionally, in considering the underlying security, Nasdaq Regulation relies on information made publicly available by the issuer and/or the markets in which the security is traded.<sup>15</sup> The Exchange believes that these measures, together with its existing surveillance procedures, provide adequate safeguards in the review of any covered security that may meet the proposed criteria for consideration of the option within the timeframe contained in this proposal.

## 2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,<sup>16</sup> in general, and furthers the objectives of Section 6(b)(5) of the Act,<sup>17</sup> in particular, in that it is designed to promote just and equitable principles of trade, 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.

The Exchange believes that the proposed changes to its listing standards for covered securities would allow the Exchange to more quickly list options on a qualifying covered security that has met the \$3.00 eligibility price without sacrificing investor protection. As discussed above, the Exchange believes that its existing trading surveillances provide a sufficient measure of protection against potential price manipulation within the proposed three consecutive business day timeframe. The Exchange also believes that the proposed three consecutive business day timeframe would continue to be a reliable test for price stability in light of its

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<sup>14</sup> See Chapter IV, Section 3(b)iii.

<sup>15</sup> See Chapter IV, Section 3(d).

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

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

findings that none of the IPO-related issues on Nasdaq within the past five years that qualified for the \$3.00 per share price standard during the first three trading days fell below the \$3.00 threshold during the fourth or fifth trading day. Furthermore, the established guidelines to be considered by the Exchange in evaluating the potential underlying securities for Exchange option transactions,<sup>18</sup> together with existing trading surveillances, provide adequate safeguards in the review of any covered security that may meet the proposed criteria for consideration of the option within the proposed timeframe.

In addition, the Exchange believes that basing the proposed timeframe on the T+2 settlement cycle adequately addresses the potential difficulties in confirming the number of shareholders of the underlying covered security. Having some of the largest brokerage firms that provide these shareholder counts to the Exchange confirm that they are able to provide these numbers within T+2 further demonstrates that the 2,000 shareholder requirement can be sufficiently verified within the proposed timeframe. For the foregoing reasons, the Exchange believes that the proposed amendments will remove and perfect the mechanism of a free and open market and a national market system by providing an avenue for investors to swiftly hedge their investment in the stock in a shorter amount of time than what is currently in place.<sup>19</sup>

Finally, it should be noted that a price/time standard for the underlying security was first adopted when the listed options market was in its infancy, and was intended to prevent the proliferation of options being listed on low-priced securities that presented special manipulation concerns and/or lacked liquidity needed to maintain fair and orderly markets.<sup>20</sup> When options

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<sup>18</sup> See notes 13 - 15 above.

<sup>19</sup> This proposed rule change does not alter any obligations of issuers or other investors of an IPO that may be subject to a lock-up or other restrictions on trading related securities.

<sup>20</sup> See Securities Exchange Act Release No. 29628 (August 29, 1991), 56 FR 43949-01

trading commenced in 1973, the Commission determined that it was necessary for securities underlying options to meet certain minimum standards regarding both the quality of the issuer and the quality of the market for a particular security.<sup>21</sup> These standards, including a price/time standard, were imposed to ensure that those issuers upon whose securities options were to be traded were widely-held, financially sound companies whose shares had trading volume and float substantial enough so as not to be readily susceptible to manipulation.<sup>22</sup> At that time, the Commission determined that the imposition of these standards was reasonable in view of the pilot nature of options trading and the limited experience of investors with options trading.<sup>23</sup>

Now more than 40 years later, the listed options market has evolved into a mature market with sophisticated investors. In view of this evolution, the Commission has approved various exchange proposals to relax some of these initial listing standards throughout the years,<sup>24</sup> including reducing the price/time standard in 2003 from \$7.50 per share for the majority of business days over a three month period to the current \$3.00 per share/five business day standard (“2003 Proposal”).<sup>25</sup> It has been almost fifteen years since the Commission approved the 2003 Proposal, and both the listed options market and exchange technologies have continued to evolve since then. In this instance, Nasdaq is only proposing a modest reduction of the current five

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(September 5, 1991) (SR-AMEX-86-19; SR-CBOE-86-15; SR-NYSE-86-20; SR-PSE-86-15; and SR-PHLX-86-21) (“1991 Approval Order”) at 43949 (discussing the Commission’s concerns when options trading initially commenced in 1973).

<sup>21</sup> See 1991 Approval Order at 43949.

<sup>22</sup> Id.

<sup>23</sup> Id.

<sup>24</sup> See e.g., 1991 Approval Order (modifying a number of initial listing criteria, including the reduction of the price/time standard from \$10 per share each day during the preceding three calendar months to \$7.50 per share for the majority of days during the same period).

<sup>25</sup> See note 7 above.

business day standard to three business days to correspond to the securities industry's move to a T+2 standard settlement cycle.<sup>26</sup> The \$3.00 per share standard and all other initial options listing criteria in Chapter IV, Section 3 will remain unchanged by this proposal. For the reasons discussed herein, the Exchange therefore believes that the proposed three business day period will be beneficial to the marketplace without sacrificing investor protections.

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

The Exchange 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 proposed rule change reduces the number of days to list options on an underlying security, and is intended to bring new options listings to the marketplace quicker.

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 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 if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>27</sup> and Rule 19b-4(f)(6) thereunder.<sup>28</sup>

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<sup>26</sup> See note 12 above.

<sup>27</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>28</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business

A proposed rule change filed under Rule 19b-4(f)(6)<sup>29</sup> normally does not become operative for 30 days after the date of filing. However, pursuant to Rule 19b-4(f)(6)(iii),<sup>30</sup> the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the proposal may become operative upon filing. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest as it will allow the Exchange to align its initial options listing standards with that of its affiliates, and the Exchange's proposal does not raise new issues. Accordingly, the Commission hereby waives the 30-day operative delay requirement and designates the proposed rule change as operative upon filing.<sup>31</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 necessary or appropriate in the public interest, for the protection of investors, or 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.

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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.

<sup>29</sup> 17 CFR 240.19b-4(f)(6).

<sup>30</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>31</sup> For purposes only of waiving the 30-day operative delay, the Commission has also considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

#### 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-2018-005 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.

All submissions should refer to File Number SR-NASDAQ-2018-005. 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 the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change.

Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASDAQ-2018-005, 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>32</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>32</sup> 17 CFR 200.30-3(a)(12).