

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-87391; File No. SR-NASDAQ-2019-057)

October 23, 2019

Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Rule 4121

I. Introduction

On July 16, 2019, The Nasdaq Stock Market LLC (“Nasdaq” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend Nasdaq Rule 4121 (Trading Halts Due to Extraordinary Market Volatility) to enhance the re-opening auction process for Nasdaq-listed securities following trading halts due to extraordinary market volatility. The proposed rule change was published for comment in the Federal Register on July 25, 2019.³ On September 5, 2019, the Commission extended the time period within which to either approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change, to October 23, 2019.⁴ The Commission received no comment letters on the proposed rule change. This order institutes proceedings under Section 19(b)(2)(B) of the Act to determine whether to approve or disapprove the proposed rule change.

II. Background and Description of the Proposal

The Exchange has proposed to amend the re-opening auction process for Nasdaq-listed securities following trading halts due to extraordinary market volatility (“market-wide circuit

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 86412 (July 19, 2019), 84 FR 35900 (“Notice”).

⁴ See Securities Exchange Act Release No. 86875 (September 11, 2019), 84 FR 47998.

breakers”).⁵ Currently, after a Level 1 or Level 2 market-wide circuit breaker trading halt initiated under Nasdaq Rule 4121 (“MWCB Halt”), trading in Nasdaq-listed securities would resume on the Exchange through a Halt Cross.⁶ Additionally, the Exchange would extend the Display Only Period for an additional 1-minute period if there is volatility during the Display Only Period (i.e., an order imbalance in the security). The volatility checks are governed under Nasdaq Rule 4120(c)(7)(C)(1) and (2), and provide that the Display Only Period will be extended if: (i) the expected cross price moves the greater of 5% or 50 cents, or (ii) all market orders will not be executed in the cross.

The Exchange proposes modifications to its rules that would allow it to instead follow a process it believes is similar to that described in Nasdaq Rule 4120(c)(10) for releasing a security following a Trading Pause initiated pursuant to the Plan to Address Extraordinary Market Volatility (“LULD” or “LULD Plan”).⁷ Proposed paragraph (d) to Nasdaq Rule 4121 provides that an MWCB Halt shall be terminated when Nasdaq releases the security for trading. For any

⁵ The Exchange also proposes a number of formatting clean-ups in Nasdaq Rule 4121. See Notice, supra note 3, at 35903.

⁶ In particular, Nasdaq Rule 4121(c)(i) provides that the re-opening of trading following a Level 1 or Level 2 trading halt shall follow the procedures set forth in Nasdaq Rule 4120. The Exchange states that these procedures are set forth in Nasdaq Rule 4120(c)(7) (see Notice, supra note 3, at 35901), which provides, in relevant part, for a 5-minute Display Only Period during which market participants may enter quotes and orders in Nasdaq systems, at the conclusion of which trading will immediately resume through the Halt Cross under Nasdaq Rule 4753.

⁷ The Exchange believes that its LULD re-opening process has been effective in facilitating a fair and orderly market following Trading Pauses initiated pursuant to the LULD Plan, and believes it is implementing similar functionality for trading halts in Nasdaq-listed securities following the initiation of market-wide circuit breakers. The Exchange further believes that the proposed changes would promote price formation and provide a more consistent re-opening process for members and investors following such trading halts, similar to the current implementations for re-opening following an MWCB Halt on NYSE Arca, Inc. (“Arca”) and Cboe BZX Exchange, Inc. (“BZX”). See Notice, supra note 3, at 35900-01.

such security listed on Nasdaq, prior to terminating the MWCB Halt, there will be a 15-minute “Initial Display Only Period” during which market participants may enter quotations and orders in that security in Nasdaq systems. The Initial Display Only Period will be 15 minutes in duration to coincide with the entire duration of an MWCB Halt.

Proposed Nasdaq Rule 4121(d)(1)(A) provides that during the Initial Display Only Period, the Exchange will also establish the “Auction Reference Price,” which is the Nasdaq last sale price (either round or odd lot) after 9:15 a.m. Eastern Time but prior to the MWCB Halt and, if none, the prior trading day’s Nasdaq Official Closing Price.⁸

Proposed Nasdaq Rule 4121(d)(1)(B) describes how the Exchange would calculate the upper and lower MWCB Auction Collar prices during the Initial Display Period. The lower MWCB Auction Collar is derived by subtracting from the Auction Reference Price 10% of the Auction Reference Price, or in the case of securities with an Auction Reference Price of \$5 or less, \$0.50. The upper MWCB Auction Collar is derived by adding to the Auction Reference Price 10% of the Auction Reference Price, rounded to the nearest minimum price increment, or in the case of securities with an Auction Reference Price of \$5 or less, \$0.50.⁹

⁸ The Exchange believes its proposal is similar to the current implementations on Arca and BZX for re-openings following an MWCB Halt. See Arca Rule 7.35-E(a)(8)(A) and BZX Rule 11.23(a)(9). The Exchange states that the proposed Auction Reference Price for MWCB Halts is substantially similar to Arca’s and BZX’s auction reference prices, except the Exchange will use the last Nasdaq sale price prior to the MWCB Halt, as opposed to the last consolidated price. The Exchange believes that it is appropriate to use the price of a trade on the primary listing market to set the reference price for auctions in Nasdaq-listed securities when such a trade has been executed recently. See Notice, supra note 3, at 35902.

⁹ The Exchange notes that both Arca and BZX employ narrower auction collar thresholds (5% of the auction reference price, or \$0.15 for securities with an auction reference price of \$3 or less). See Arca Rule 7.35-E(e)(7)(B)(ii) and BZX Rule 11.23(d)(2)(C)(i)(B). The Exchange believes that the wider parameters proposed for MWCB Auction Collars are set at appropriate levels that would allow the Exchange to re-open trading in securities more quickly while still reducing the potential to re-open at a price that is

Proposed Nasdaq Rules 4121(d)(2) and (d)(3) specify the circumstances when the Exchange would extend the Display Only Period for an MWCB Halt re-opening process, and how the Exchange would adjust the MWCB Auction Collars for each extension. In particular, at the conclusion of the Initial Display Only Period, the security will be released for trading unless, at the end of the Initial Display Only Period, Nasdaq detects an order imbalance in the security. In that case, Nasdaq will extend the Display Only Period for an additional 5-minute period (“Extended Display Only Period”), and the MWCB Auction Collar prices will be adjusted as follows:

- If the Display Only Period is extended because the calculated price at which the security would be released for trading is below the lower MWCB Auction Collar price or all sell market orders would not be executed in the cross, then the new lower MWCB Auction Collar price is derived by subtracting 10% of the Auction Reference Price, which was rounded to the nearest minimum price increment, or in the case of securities with an Auction Reference Price of \$5 or less, \$0.50, from the previous lower MWCB Auction Collar price, and the upper MWCB Auction Collar price will not be changed.
- If the Display Only Period is extended because the calculated price at which the security would be released for trading is above the upper MWCB Auction Collar

significantly away from the last traded price of the security. The Exchange also notes that it has traditionally been a listing venue for equity stocks, while Arca and BZX have traditionally listed more ETFs, which track entire sectors, indices or other groups of assets and can mute the effect of price volatility of the ETF. The Exchange believes that the proposed wider price bands strikes an appropriate balance between allowing the Exchange to return to normal continuous trading in a measured, timely manner while accommodating the potential higher volatility of individual stocks. See Notice, supra note 3, at 35902.

price or all buy market orders would not be executed in the cross, then the new upper MWCB Auction Collar price is derived by adding 10% of the Auction Reference Price, which was rounded to the nearest minimum price increment, or in the case of securities with an Auction Reference Price of \$5 or less, \$0.50, to the previous upper MWCB Auction Collar price, and the lower MWCB Auction Collar price will not be changed.

At the conclusion of the Extended Display Only Period, the security will be released for trading unless, at the end of the Extended Display Only Period, Nasdaq detects an order imbalance in the security. In that case, Nasdaq will further extend the Display Only Period, continuing to adjust the MWCB Auction Collar prices every five minutes in the manner described in proposed Nasdaq Rule 4121(d)(2) until the security is released for trading; provided, however, that Nasdaq will not adjust the MWCB Auction Collar prices past 50% of the Auction Reference Price for any security during any Extended Display Only Period.¹⁰ During any additional Extended Display Only Period after the first Extended Display Only Period, Nasdaq shall release the security for trading at the first point there is no order imbalance.

¹⁰ The Exchange notes that the proposal to limit the MWCB Auction Collars to 50% of the Auction Reference Price deviates from the implementations of MWCB auction collars on Arca and BZX, neither of which limit the auction collars. The Exchange states that it balanced the potential for the proposed 50% limit to prevent the transition to continuous trading, particularly in instances of extreme price volatility that could result in increased Extended Display Only Periods against the potential for extreme volatility resulting in trades at prices far away from a security's fundamental value, which could ultimately harm parties to the trade. The Exchange believes that an MWCB Halt will be triggered during a period of significant volatility across markets that may not correlate to the fundamental value of a single security and that limiting the MWCB Auction Collars to 50% of the Auction Reference Price achieves an appropriate balance in favor of preventing extraordinary volatility that could result in significant price disparity in post-auction trading. See Notice, supra note 3, at 35903.

Proposed Nasdaq Rule 4121(d)(4) specifies that an order imbalance would be established for purposes of the process under Nasdaq Rule 4121 as follows:

- the calculated price at which the security would be released for trading is above (below) the upper (lower) MWCB Auction Collar price calculated under paragraphs (1), (2), or (3) of Nasdaq Rule 4121(d); or
- all market orders would not be executed in the cross.

Proposed Nasdaq Rule 4121(d)(5) describes how the MWCB Auction Collars will function in the event of more than one trading halt initiated under Nasdaq Rule 4121 in the same day. In the event of a Level 2 Market Decline while a security is in a Level 1 MWCB Halt and has not been released for trading, Nasdaq will recalculate the lower and upper MWCB Auction Collar prices in the particular security in accordance with paragraph (B)(1) of proposed Nasdaq Rule 4121.¹¹ In this instance, the Exchange will start the calculation of the new upper and lower MWCB Auction Collar prices using 10% of the Auction Reference Price, rounded to the nearest minimum price increment, or \$0.50 for securities with an Auction Reference Price of \$5 or less. The Exchange believes that the proposed language would bring greater transparency to market participants in how the Exchange would handle the calculation of MWCB Auction Collars.

The Exchange also proposes to add new paragraph (e) to Nasdaq Rule 4121 to describe how the Exchange will handle the publication of MWCB Halt Information. Specifically, at the beginning of the Initial Display Only Period and continuing through the resumption of trading, Nasdaq will disseminate by electronic means an Order Imbalance Indicator¹² every second. The

¹¹ As currently provided in Nasdaq Rule 4121(b)(i), the Exchange would halt trading based on a Level 1 or Level 2 Market Decline only once per day.

¹² As described in Nasdaq Rule 4753(a)(3), an “Order Imbalance Indicator” is a message disseminated by electronic means containing information about Eligible Interest and the price at which such interest would execute at the time of dissemination. “Eligible

Exchange also proposes to make a related change by adding new Nasdaq Rule 4753(a)(3)(G), which will provide that for purposes of an MWCB Halt initiated pursuant to Nasdaq Rule 4121, the Order Imbalance Indicator will include Auction Reference Prices and MWCB Auction Collars, as defined in Nasdaq Rule 4121(d).

III. Proceedings to Determine Whether to Disapprove SR-NASDAQ-2019-057 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act to determine whether the proposal should be approved or disapproved.¹³ Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change, as discussed below. Institution of disapproval proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved.

Pursuant to Section 19(b)(2)(B) of the Act, the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis and input concerning the proposed rule change's consistency with the Act¹⁴ and, in particular, with Section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove

Interest" is defined as any quotation or any order that has been entered into the system and designated with a time-in-force that would allow the order to be in force at the time of the Halt Cross. See Nasdaq Rule 4753(a)(5).

¹³ 15 U.S.C. 78s(b)(2)(B).

¹⁴ 15 U.S.C. 78f(b)(5).

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.¹⁵

For the reasons discussed above, the Commission believes it is appropriate to institute proceedings pursuant to Section 19(b)(2)(B) of the Act to determine whether the proposal should be approved or disapproved.

IV. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the concerns identified above, as well as any other concerns they may have with the proposal. In particular, the Commission invites the written views of interested persons concerning whether the proposed rule change is inconsistent with Section 6(b)(5) or any other provision of the Act, or the rules and regulation thereunder.

Although there do not appear to be any issues relevant to approval or disapproval which would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.¹⁶

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register]. The Commission asks that commenters address the sufficiency of the Exchange's

¹⁵ Id.

¹⁶ Section 19(b) (2) of the Act, as amended by the Securities Act Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

statements in support of the proposal which are set forth in the Notice,¹⁷ in addition to any other comments they may wish to submit about the proposed rule change. In particular, the Commission seeks comment, including where relevant, any specific data, statistics, or studies, on the following:

1. The Nasdaq proposal appears to differ from other primary listing market MWCB re-opening processes in three ways. First, the Nasdaq proposal would establish a security's auction reference price after a MWCB Halt by referring to the Nasdaq last sale price (as opposed to the consolidated last sale price). Second, the Nasdaq proposal would establish wider price bands of 10% of the Auction Reference Price, or in the case of securities with an Auction Reference Price of \$5 or less, \$0.50 (as opposed to 5% of the auction reference price, or \$0.15 for securities with an auction reference price of \$3), and would widen the price bands in those larger increments (as opposed to widening in the smaller increments). Third, the Nasdaq proposal would not widen the price bands for an individual security beyond 50% (as opposed to gradually widening price bands without limit until a security is reopened). Should the primary listing exchanges harmonize their respective processes for reopening trading after a halt pursuant to the market-wide circuit breaker mechanism following a Level 1 or Level 2 Market Decline, and if so, why? If so which aspects of the re-opening processes should be harmonized (e.g. period of auction order entry, type of auction information disseminated, length of dissemination period, frequency of dissemination, auction reference price, determination of auction match price, width of auction collars, reasons for

¹⁷ See Notice, supra note 3.

extending auction, length of auction extension period, thresholds for expanding auction collars, or limits on expansion of auction collars) and what are the appropriate parameters? Should Nasdaq further harmonize its proposed MWCB reopening process to align with Arca and BZX on establishment of auction reference prices, auction collars levels, and/or the limit (or lack thereof) on auction collar adjustments?

2. Is it appropriate for the Exchange to derive and expand the lower/upper MWCB Auction Collar by subtracting from/adding to the Auction Reference Price 10% of the Auction Reference Price (or \$0.50 for securities priced \$5 or less), which are currently wider than the parameters that Arca and BZX use to derive and expand their respective MWCB auction collars? Are there any specific data, statistics, or studies to support the Exchange's belief that (1) the wider parameters proposed for MWCB Auction Collars are set at appropriate levels that would allow the Exchange to re-open trading in securities more quickly while still reducing the potential to re-open at a price that is significantly away from the last traded price of the security and (2) the wider parameters are appropriate because the Exchange has traditionally been a listing venue for equity stocks as contrasted with Arca and BZX which have traditionally listed more ETFs, which can mute the effect of price volatility?¹⁸
3. Is it appropriate for the Exchange to not adjust the MWCB Auction Collar prices past 50% of the Auction Reference Price for any security during any Extended Display Only Period? Are there any specific data, statistics, or studies to support

¹⁸ See Notice, supra note 3, at 35902.

the Exchange's belief that (1) without this limitation, there is potential for extreme volatility resulting in trades at prices far away from a security's fundamental value, ultimately harming investors that are party to the trade and (2) it may be more appropriate to continue adjusting price collars in the context of LULD where trading is halted due to a period of extraordinary volatility in a single security because there may be instances of a discrete event that ultimately impacts the value of the individual security and that an MWCB Halt will be triggered during a period of significant volatility across markets that may not correlate to the fundamental value of a single security?¹⁹

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. Please include File Number SR-NASDAQ-2019-057 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-2019-057. 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 Web site (<http://www.sec.gov/rules/sro.shtml>).

¹⁹ See id. at 35903.

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-2019-057 and should be submitted on or before [insert date 21 days from publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁰

Jill M. Peterson
Assistant Secretary

²⁰ 17 CFR 200.30-3(a)(57).