

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-84012; File No. SR-BX-2018-040)

August 31, 2018

Self-Regulatory Organizations; Nasdaq BX, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Provide New Optional Functionality to Minimum Quantity Orders

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on August 20, 2018, Nasdaq BX, Inc. (“BX” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I and II 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 provide new optional functionality to Minimum Quantity Orders.

The text of the proposed rule change is available on the Exchange’s Website at <http://nasdaqbx.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

¹ 15 U.S.C. 78s(b)(1).

² 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 provide a new optional functionality to the Minimum Quantity Order Attribute,³ which is identical to the optional functionality provided by The Nasdaq Stock Market LLC (“Nasdaq”).⁴

Current Functionality

An Order designated with the Minimum Quantity Order Attribute (“MQ”) allows a market participant to specify a minimum share amount at which it will execute. For example, a market participant seeking to buy or sell a large position may desire to execute only if a large quantity of shares can be traded to reduce the price impact of the security being bought or sold. An Order with MQ will not execute unless the volume of contra-side liquidity available to execute against the order meets or exceeds the designated minimum. When an Order with MQ is received by the Exchange, it will execute immediately⁵ if there is sufficient liquidity available on the Exchange within the limit price of the Order with MQ. Specifically, the Order with MQ will execute if the sum of the shares of one or more resting Orders is equal to or greater than its minimum quantity. In the case of multiple resting Orders being aggregated to meet the minimum quantity, each contra-side order creates a separate execution and thus there can be multiple

³ Rule 4703(e).

⁴ See Nasdaq Rule 4703(e); see also Securities Exchange Act Release No. 73959 (Dec. 30, 2014), 80 FR 582 (Jan. 6, 2015) (SR-NASDAQ-2014-95).

⁵ An Order with MQ would satisfy the requirements of Regulation NMS Rule 611 and not trade through a protected quotation. See 17 CFR 242.611.

executions that, in aggregate, equal or exceed the minimum quantity. If an Order with MQ does not execute immediately due to lack of contra-side liquidity that is equal to or greater than the designated minimum, the Order will post⁶ to the Exchange book as a Non-Displayed Order with the characteristics of its underlying Order Type.⁷ Once posted, an Order with MQ will execute only if an incoming Order is marketable against the resting Order with MQ and is equal to or greater than the minimum quantity set on the resting Order with MQ. Multiple potential executions cannot be aggregated to meet the minimum quantity requirement of the posted Order with MQ. If an Order with MQ executes partially and the number of shares remaining is less than the minimum quantity of the Order, the minimum quantity of the Order is reduced to the remaining share size. If an Order with MQ is received that is marketable against a resting contra-side Order with size that does not meet the minimum quantity requirement, the Order with MQ will be posted on the Exchange book as a Non-Displayed Order with the characteristics of its underlying Order Type.⁸ For example, if an Order with MQ is received to buy 1,000 shares at \$10 with a minimum quantity restriction of 500 shares and there is a resting sell order for 300 shares at \$10, the Order with MQ will be posted as a Non-Displayed Order at \$10. Furthermore, the Exchange notes that a subsequent Order without a minimum quantity restriction that is marketable against the resting contra-side interest will result in an execution because the market participant entering the Order with MQ has expressed its intention not to execute against

⁶ Orders post to the Exchange book only if they are designated with a time in force that allows for posting. For example, an IOC order never posts to the book.

⁷ A Non-Displayed Order is an Order Type that is not displayed to other Participants, but nevertheless remains available for potential execution against incoming Orders until executed in full or cancelled. See Rule 4702(b)(3). Orders with MQ are always Non-Displayed when posted on the Exchange book.

⁸ SEC Rule 610(d) under Regulation NMS restricts displayed quotations that lock or cross protected quotations in NMS stock, but does not apply to non-displayed trading interest, like a resting Order with MQ. See 17 CFR 242.610(d).

liquidity below a certain minimum size, and therefore cedes execution priority to any new Orders that would otherwise have a lower priority.

Proposed Functionality

The Exchange is proposing to add a new optional functionality to further enhance the utility of the Minimum Quantity Order Attribute to market participants.⁹ As was noted by Nasdaq in proposing the optional functionality proposed herein,¹⁰ some market participants have noted that they avoid sending large Orders with MQ to the Exchange out of concern that such Orders may interact against small Orders entered by professional traders. These market participants are concerned that such interaction may negatively impact the execution of their larger Orders. Often institutional Orders are much larger in size than the average Order in the marketplace. Furthermore, in order to facilitate the liquidation or acquisition of a large position, multiple Orders are submitted into the market, which although larger than the average Order in the market, only represent a small proportion of the overall institutional position to be executed. The various strategies used to execute large size are based on a desire to limit price movement of the stock the institution is pursuing. Executing in small sizes, even if in aggregate it meets a minimum quantity designation, may impact the market such that the additional Orders that the institution has yet to submit to the market may be more costly to execute. If an institution is able to execute in larger sizes, the contra-party to the execution is less likely to be a participant that reacts to short term changes in the stock price and as such the price impact to the stock could be

⁹ The option is available at the port level. Accordingly, all Orders entered through a particular port will receive the selected functionality. All trading ports default to the current functionality.

¹⁰ See note 4, supra.

less acute when larger individual executions are obtained by the institution.¹¹ As a consequence of this concern, these Orders are often executed away from the Exchange in dark pools, at least some of which have the functionality proposed herein,¹² or via broker-dealer internalization.

Accordingly, to attract larger Orders with MQ to the Exchange, it is proposing new optional functionality that will allow a market participant to designate a minimum individual execution size, and thus allow users to avoid interaction with such smaller Orders resting on the book. As discussed above, under the current rule, an incoming Order with MQ will execute against any number of smaller contra-side Orders that, in aggregate, meet the minimum quantity set by the market participant. For example, if a market participant entered an Order with MQ to buy with a price of \$10, a size of 1,000 and a minimum quantity of 500, and the order was marketable against two resting sell orders for 300 and 400 shares, the System would aggregate both orders for purposes of meeting the minimum quantity, thus resulting in executions of 300 shares and 400 shares respectively with the remaining 300 shares of the Order with MQ posting to the Exchange book with a minimum quantity restriction of 300 shares. The proposed new optional functionality will not allow aggregation of smaller executions to satisfy the minimum quantity of an incoming Order with MQ. Using the same scenario as above, but with the proposed new functionality and a minimum execution size requirement of 400 shares selected by

¹¹ The Commission has long recognized this concern: “Another type of implicit transaction cost reflected in the price of a security is short-term price volatility caused by temporary imbalances in trading interest. For example, a significant implicit cost for large investors (*who often represent the consolidated investments of many individuals*) is the price impact that their large trades can have on the market. Indeed, disclosure of these large orders can reduce the likelihood of their being filled.” See Securities Exchange Act Release No. 42450 (Feb. 23, 2000), 65 FR 10577, 10581 (Feb. 28, 2000) (SR-NYSE-99-48) (emphasis added) (internal citation omitted).

¹² For example, the BIDS Alternative Trading System also has functionality that allows its subscribers to select a minimum size requirement, which prevents a subscriber’s interest from interacting with contra-side interest if its size is less than the specified minimum. See <http://www.bidstrading.com/solutions/faqs/>.

the market participant, the Order with MQ would not execute against the two sell orders because the order at the top of the Exchange book is less than 400 shares. The new functionality will reprice the Order with MQ to one minimum price increment lower than (higher than) the lowest price (highest price) of the resting contra-side Order, and post the Order to the Exchange book as a Non-Displayed Order when the top of the Exchange book is of insufficient size to satisfy the minimum execution size requirement. Applied to the example above, the Order would post to the Exchange book as a Non-Displayed Order to buy 1,000 shares at \$9.99. The Exchange notes that the market participant entering the Order with MQ has expressed its intention not to execute against liquidity below a certain minimum size, and therefore cedes execution priority when it would lock or cross resting Orders against which it would otherwise execute if it were not for the minimum execution size restriction.

The Exchange believes that it is appropriate to adjust the price one minimum price increment lower than (higher than) the lowest price (highest price) of the resting contra-side Order prior to posting on the Exchange book because, by using the minimum execution size option, the submitter of the Order is choosing to reduce the number of situations in which the Order could potentially execute. Thus, an Order without this further restriction provides greater contribution to the price discovery process of the market. All bona fide market participation that results in an execution on a data feed contributes to the price discovery process that is essential to a proper functioning market. However, there are different degrees to which activity within the market contributes to price discovery. A displayed Order at the NBBO of an Exchange, and the subsequent execution thereof, contributes significantly to price discovery because both the Displayed Order prior to execution, and the execution itself, provide a reference price to the market. Further, a non-displayed order on an exchange contributes to price discovery as it is part

of the continuous auction on a market with publicly displayed orders and quotes - albeit the contribution of a non-displayed order on an exchange is less than the contribution of a displayed order on an exchange. Furthermore, a non-displayed order on a dark pool contributes less to price discovery because it is resting in a less transparent trading venue that is not part of the continuous auction of a lit exchange. If one were to rank the contribution to price discovery that different market activity provides, it would include the following (listed from least price discovery contribution to most):

- Order resting in dark pool (no contribution)
- Non-displayed order on exchange (no or very little contribution)
- Order execution in dark pool (some contribution, execution reported publicly via TRF)
- Non-displayed order execution on exchange (contribution as part of continuous auction, execution reported publicly, and priority is behind displayed – i.e., priority is ceded to orders that contribute more to price discovery)
- Displayed order on exchange (significant contribution)
- Displayed order execution on exchange (significant contribution, publicly displayed order + execution reported publicly)

In this sense, the proposed change continues to contribute more meaningfully to price discovery than an order in a dark pool because it is part of the continuous auction market on the exchange but, similar to a regular Non-Displayed Order ceding priority to Displayed Orders on the Exchange, the Order with MQ that uses the proposed functionality will cede price priority to Orders that do not contain the minimum execution size restriction. Also unlike the current process, the proposed new functionality will cancel the remainder of a marketable Order with

MQ that is partially filled upon entry if the partially-executed Order with MQ would lock or cross resting contra-side liquidity that does not meet the minimum execution size requirement. Under the current process, an Order with MQ that receives a partial execution has the remainder of the Order posted to the Exchange book as a Non-Displayed Order. The proposed new functionality will, instead, cancel any shares not executed after a partial execution of an Order with MQ if there are more shares that remain resting on the Exchange book at a price that would satisfy the limit price of the Order with MQ but that are not executable against the incoming Order with MQ due to the minimum execution size set on the Order. For example, an Order with MQ to buy priced at \$10 with a size of 1,000 and a minimum quantity of 500, that is marketable against two sell orders on the Exchange book, one for 500 shares and one for 400 shares, would result in the execution of 500 shares and the cancellation of the remaining 500 shares. Under the current process, the Order would receive two partial executions of 500 and 400 shares, and the remaining 100 shares would be posted to the Exchange book as a Non-Displayed Order to buy priced at \$10.

The Exchange notes that when a non-IOC Order with MQ is partially executed and cancelled in this situation, the contra-side liquidity that is not executed may be Non-Displayed. If an Order with MQ is cancelled due to Non-Displayed contra-side liquidity, the submitter of the Order will know that there may be a resting Order or Orders at the price of the Order with MQ and also that the resting Order or Orders are for fewer shares than the minimum execution size required by the Order. The Exchange believes this is acceptable because the Order with MQ has already partially executed for a size of at least one round lot and thus the Order submitter has taken on risk due to the execution and therefore contributed to price discovery in the market place.

Under the proposed change, a resting Order with MQ will operate the same way as it does currently. When an Order with MQ is posted on the book, it will only execute against incoming Orders if the individual incoming Order is equal to or greater than the minimum designated on the Order. The primary difference between the current functionality and the proposed new functionality is that upon receipt, an incoming Order with MQ will only execute against individual resting Orders if the order at the top of the Exchange book meets or exceeds the minimum on the Order. The Exchange notes that this is no different than Nasdaq's Minimum Quantity Order Attribute, on which the proposed change is based, and is also similar to Cboe BZX Exchange, Inc.'s ("BZX") Minimum Quantity Order,¹³ which allows BZX Users to specify that such an order will not execute against multiple aggregated orders simultaneously and that the minimum quantity condition be satisfied by each individual order resting on the BZX book.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,¹⁴ in general, and furthers the objectives of Section 6(b)(5) of the Act,¹⁵ 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 proposal will provide market participants, including institutional firms that *ultimately represent individual retail investors in many cases*, with better control over their Orders, thereby providing them with greater potential to improve the quality of their Order executions. Currently, the rule allows the market participant to designate a minimum

¹³ See BZX Rule 11.9(c)(5).

¹⁴ 15 U.S.C. 78f(b).

¹⁵ 15 U.S.C. 78f(b)(5).

quantity on an Order that, upon entry, may aggregate multiple executions to meet the minimum quantity requirement. Once posted to the Exchange book, however, the minimum quantity requirement is equivalent to a minimum execution size requirement. The Exchange is now proposing to provide a market participant with control over the execution of their Order with MQ by allowing them an option to designate the minimum individual execution size *upon entry*. The control offered by the proposed change is consistent with the various types of control currently provided by exchange order types. For example, the Exchange, Nasdaq and other exchanges offer limit orders, which allow a market participant control over the price it will pay or receive for a stock.¹⁶ Similarly, exchanges offer order types that allow market participants to structure their trading activity in a manner that is more likely avoid certain transaction cost related economic outcomes.¹⁷ Moreover, and as discussed above, other trading venues provide the very functionality that the Exchange is proposing, with the proposed rule text and operation of the functionality identical to that of Nasdaq.

As discussed above, some market participants have requested the functionality proposed herein so they may avoid transacting with smaller Orders that they believe ultimately increase the cost of the transaction. Market participants, such as large institutions that transact a large number of orders on behalf of retail investors, have noted that because the Exchange does not have this functionality, they avoid sending large orders to the Exchange to avoid potentially more expensive transactions.¹⁸ In this regard, the Exchange notes that proposed new optional

¹⁶ See, e.g., Rule 4703(c).

¹⁷ See, for example, the Exchange's Post-Only Order. See Rule 4702(b)(4).

¹⁸ As noted, the proposal is designed to attract liquidity to the Exchange by allowing market participants to designate a minimum size of contra-side Order with which to interact, thus providing market participants with functionality that is otherwise available to them on another exchange (*i.e.*, Nasdaq). The designation of a minimum size may reduce the interaction that such new Order flow would have with smaller contra-side Orders on the

functionality may improve the Exchange market by attracting more Order flow, which is currently trading on less transparent venues that contribute less to price discovery and price competition than executions and quotes that occur on lit exchanges. Such new Order flow will further enhance the depth and liquidity on the Exchange, which supports just and equitable principles of trade. Furthermore, the proposed modification to the Minimum Quantity Order Attribute is consistent with providing market participants with greater control over the nature of their executions so that they may achieve their trading goals and improve the quality of their executions.

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, as amended. Specifically, the proposed change allows market participants to condition the processing of their Orders based on a minimum execution size. The changes to the Minimum Quantity Order Attribute will enhance the functionality offered by the Exchange to its members, thereby promoting its competitiveness with other exchanges and non-exchange trading venues that already offer the same or similar functionality. As a consequence, the proposed change will promote competition among exchanges and their peers, which, in turn, will decrease the burden on competition rather than place an unnecessary burden thereon.

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.

Exchange, some of which may be retail Order flow. The Exchange notes that since the Order flow attracted by this functionality may also represent retail investors and is in addition to the existing Order flow currently on the Exchange, market quality for retail investors ultimately should not be negatively impacted. Accordingly, the Exchange does not believe that retail Orders will be disadvantaged by the proposed change.

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) of the Act¹⁹ and Rule 19b-4(f)(6) thereunder.²⁰

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

¹⁹ 15 U.S.C. 78s(b)(3)(A).

²⁰ 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires a self-regulatory organization to give 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, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-BX-2018-040 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-BX-2018-040. 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-BX-2018-040 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.²¹

Eduardo A. Aleman
Assistant Secretary

²¹ 17 CFR 200.30-3(a)(12).