

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-71555; File No. SR-NASDAQ-2014-017)

February 18, 2014

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Add a Risk Management Tool Commonly Known as a “Kill Switch”

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 February 4, 2014, The NASDAQ Stock Market LLC (“NASDAQ” or “Exchange”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I 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 is filing a proposed rule change to add a risk management tool commonly known as a “Kill Switch” as set forth in proposed NASDAQ Rule 6130. The new Kill Switch feature will be optional and will be offered at no charge effective March 1, 2014. The text of the proposed rule change is below. Proposed new language is italicized; proposed deletions are in brackets.

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**6130. NASDAQ Kill Switch**

(a) **Definition.** The NASDAQ Kill Switch is an optional tool offered at no charge that enables participants to establish a pre-determined level of Net Notional Risk Exposure (“NNRE”), to receive notifications as the value of executed orders approaches the NNRE level, and to have order entry ports disabled and open orders administratively cancelled when the value of executed orders exceeds the NNRE level.

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

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

(b) *Net Notional Risk Exposure.* Participants may set a NNRE for each MPID individually. Each participant is responsible for establishing and maintaining its NNRE. Participants may adjust NNRE values intra-day.

(c) *Notification.* Participants will receive notifications when the total value of executed orders associated with an MPID exceeds 50, 75, 85, 90, and 95 percent of the NNRE value. When the NNRE is exceeded, the notification will include the total number of orders cancelled and remaining open in the System.

(d) *Operation.* Unless cancellation is prohibited by Rule 4752, 4753, or 4754, a Kill Switch when triggered shall result in the immediate cancellation of all open orders of any type or duration entered by the participant via the affected MPID, and in the immediate prevention of order entry of any type via the affected MPID. The participant must request reactivation of the MPID before trading will be reauthorized.

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II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

**Background.** NASDAQ has offered a Pre-Trade Risk Management (“PRM”) toolset since 2002, before NASDAQ began operating as a national securities exchange and before the Commission adopted the Market Access Rule.<sup>3</sup> PRM provides participant firms with the ability to set a wide range of parameters for orders to facilitate pre-trade protection by creating a PRM module defined to represent checks desired. Using PRM, firms can increase controls on their

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<sup>3</sup> SEC Rule 15c3-5.

trading activity and the trading activity of their clients and customers at the order level, including the opportunity to prevent potentially erroneous transactions. PRM validates orders entered on PRM-enabled ports prior to allowing those orders into its matching engine and, using parameters set by the subscriber, determines if the order should be sent for fulfillment. PRM users may choose to set PRM Order Checks, Aggregate Total Checks within a PRM Module, and subscribe to PRM Workstation Add-ons to an existing NASDAQ Workstation or WeblinkACT 2.0. PRM manages risk by checking each order, before it is accepted into the System, against certain parameters pre-specified by the user within a module, such as maximum order size or value, order type restrictions, market session restrictions (pre/post market), security restrictions, including per-security limits, restricted stock lists, and certain other criteria.

In order for a participant firm to subscribe, at least one PRM Module per market participant ID (“MPID”) is required, but a user may have multiple PRM Module subscriptions per MPID, depending on the type and number of ports designated as PRM ports. A PRM Module is created to validate individual orders against pre-specified parameters. Aggregate Total Checks allow users to limit overall daily trading activity based on Buy, Sell, and/or Net trading limits. These daily trading activity limits may be established at an aggregate limit and/or security specific limit per PRM Module. Participant firms may subscribe to the PRM Workstation Add-on to an existing NASDAQ Workstation or WeblinkACT 2.0 for a fee.

**Current Proposal.** NASDAQ will provide a tool to allow market participants to control, for each Market Participant Identifier (“MPID”), the total Net Notional Risk Exposure (“NNRE”) they are prepared to accept per trading session, from 04:00 to 20:00 EST. If a market participant exceeds their pre-established NNRE the access ports associated with that MPID will

be disabled and open exposure on the NASDAQ Market under that MPID will be administratively cancelled.

The Kill Switch tool will operate on an MPID level, meaning that participants will need to set a unique NNRE for each MPID used for order entry. Participants can set limits for none, one, some, or all MPIDs registered to their firm. The tool will operate on all orders attributable to each MPID. Therefore, participants that utilize a single MPID for multiple trading desks will be unable to establish a different NNRE for each trading desk. Participants may adjust their NNRE values intraday. The NNRE will be calculated daily, meaning that it will reset at the start of each trading day.

With the limited exceptions noted below, the Kill Switch will operate at all times and on all orders when the NASDAQ System is open (*i.e.*, 4:00 a.m. to 8:00 p.m.) and it will cancel all open interest of all order types and all time-in-force durations. The Kill Switch function will not cancel orders directed to a NASDAQ Cross during the period leading up to a NASDAQ Cross when order cancellation is prohibited. Specifically, the Kill Switch will not cancel Cross orders just prior to an Opening Cross (9:28:00-09:30:00),<sup>4</sup> a Halt or Initial Public Opening Cross,<sup>5</sup> or a Closing Cross (15:50:00-16:00:00).<sup>6</sup> With these exceptions, the Kill Switch will operate universally whenever the NASDAQ System is open.

The tool will generate and send an email to a market participant as it approaches and then exceeds the pre-determined NNRE for an MPID. As a Participant executes trades during the trading session, an email will be sent to associated Infocenter accounts containing their current

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<sup>4</sup> See NASDAQ Rule 4752(a).

<sup>5</sup> See NASDAQ Rule 4753(a).

<sup>6</sup> See NASDAQ Rule 4754(a).

proximity to the NNRE limit they had previously established. Such notification will occur when the executed value reaches 50, 75, 85, 90, and 95 percent of the pre-determined NNRE limit.

In the event the NNRE limit is exceeded, the order entry port associated with the affected MPID will be disabled and open orders in the System will be administratively cancelled. A notification will be sent that indicates that the breach has occurred and that order flow from that port has been stopped. It will also include a count of the total number of orders cancelled and the total number of auction-specific orders still exposed.<sup>7</sup> The notification will also be delivered to NASDAQ's trading operations team so that NASDAQ personnel are aware and can assist participants in managing their risk exposure.

After a Kill Switch has been triggered, the participant will be required to contact NASDAQ operations staff in order to re-authorize trading under the affected MPID. Participants will be required to explain why a Kill Switch was triggered and why it is safe for the Exchange to re-authorize the MPID for order entry. Upon such request, NASDAQ operations staff will be reactivate the order entry port associated with the affected MPID.

NASDAQ plans to offer the Kill Switch functionality by March 1, 2014.

## 2. Statutory Basis

The rule change proposed in this submission is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.<sup>8</sup> Specifically, the proposed change is consistent with Section 6(b)(5) of the Act,<sup>9</sup> because it would promote just and

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<sup>7</sup> Auction orders will continue to be available to execute in the cross. Auction orders that do not execute in the intended cross will be cancelled administratively when the cross is complete.

<sup>8</sup> 15 U.S.C. 78f(b).

<sup>9</sup> 15 U.S.C. 78f(b)(5).

equitable principles of trade, remove impediments to, and perfect the mechanism of, a free and open market and a national market system, and, in general, protect investors and the public interest. The Kill Switch is designed to protect firms and investors alike by limiting the risk and damage of potential technological or other erroneous trading activity. As such, the Kill Switch is an important compliance tool that participants may use to help maintain the regulatory integrity of the markets.

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

NASDAQ 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. To the contrary, the Exchange does not believe that the provision of Kill Switch functionality should be the subject of competitive analysis. In that regard, the Exchange notes that it has coordinated with other national securities exchanges and the Financial Industry Regulatory Authority to deliver a standard level of risk management functionality commonly known as the Kill Switch.

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)(ii) of

the Act<sup>10</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>11</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 No. SR-NASDAQ-2014-017 on the subject line.

##### Paper comments:

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

All submissions should refer to File Number SR-NASDAQ-2014-017. 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

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<sup>10</sup> 15 U.S.C. 78s(b)(3)(a)(ii).

<sup>11</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) 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

all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>).

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of 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-NASDAQ-2014-017 and should be submitted by [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>12</sup>

Kevin M. O'Neill  
Deputy Secretary

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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.

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