

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-74096; File No. SR-NASDAQ-2014-116)

January 20, 2015

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving a Proposed Rule Change Relating to the NASDAQ Opening and Halt Cross

I. Introduction

On November 21, 2014, The NASDAQ Stock Market LLC (“Nasdaq” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposed rule change relating to its process for opening trading on Nasdaq Options Market, LLC (“NOM”) at the beginning of the trading day and following a trading halt. The proposed rule change was published for comment in the Federal Register on December 10, 2014.<sup>3</sup> The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

The Exchange proposes to modify its process for opening option trading on NOM at the beginning of the trading day and following a trading halt. The Exchange proposes to accomplish this by revising definitional terms set forth in Chapter VI, Sections 1 and 8(a) of its rules, and by revising the description of the processing of the Nasdaq Opening Cross<sup>4</sup> set forth in Chapter VI, Section 8(b) of its rules. The Exchange also proposes to revise the language set forth in Chapter

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

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

<sup>3</sup> See Securities Exchange Act Release No. 73739 (November 12, 2014), 79 FR 73382 (“Notice”).

<sup>4</sup> The term “Nasdaq Opening Cross” is defined in Chapter VI, Section 8(a)(3) of the Exchange’s rules. As is discussed infra, this definition is among those that the Exchange has proposed to revise.

VI, Section 8(c) describing what occurs in the absence of an opening cross.<sup>5</sup>

Definitions – Sections 1 and 8(a)

The Exchange proposes to add an “On the Open Order” or “OPG” as a new order type and time-in-force condition defined in Section 1. As proposed, any order designated as such would be executable only during the Nasdaq Opening Cross, with any portion not so executed cancelled back to the entering participant.<sup>6</sup>

In addition, the Exchange proposes to make the following definitional changes to Section 8(a):

- “Order Imbalance Indicator” is currently defined as a message disseminated by electronic means containing information about “Eligible Interest”<sup>7</sup> and the price in penny increments at which such interest would execute at the time of dissemination.<sup>8</sup> The “Current Reference Price” is one piece of information disseminated as part of the Order Imbalance Indicator and, as currently defined, is determined based on three price parameters.<sup>9</sup> The Exchange proposes to delete these price parameters and to simplify the definition of “Current Reference Price” to

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<sup>5</sup> Unless otherwise noted, all citations herein to Sections of the Exchange’s rules are citations to Sections of Chapter VI of its rules.

<sup>6</sup> See proposed Sections 1(e)(7) and 1(g)(1).

<sup>7</sup> The term “Eligible Interest” is defined in Section 8(a)(4) and, as discussed below, is a term that the Exchange proposes to modify.

<sup>8</sup> See Section 8(a)(2). The Exchange proposes to provide itself with the ability to disseminate the Order Imbalance Indicator more frequently than the five second intervals currently required. See proposed Section 8(b)(3). The Exchange also proposes to specify that the dissemination interval, in addition to the start of dissemination, would be posted on its website. Id.

<sup>9</sup> See Section 8(a)(2)(A).

be: an indication of what the opening cross would be at a particular point in time.<sup>10</sup>

Additionally, the indicative prices at which the Nasdaq Opening Cross would occur, which are also currently disseminated as part of the Order Imbalance Indicator,<sup>11</sup> would be eliminated from such dissemination as part of the proposal.<sup>12</sup>

- The Exchange proposes to revise the term “Nasdaq Opening Cross” to mean the process for opening or resuming trading pursuant to Section 8, which includes the process for determining the price at which Eligible Interest shall be executed at the opening of trading for the day or the opening of trading for a halted option, and the process for executing such Eligible Interest.<sup>13</sup>
- The Exchange would revise the term “Eligible Interest” to mean any quotation or any order that may be entered into the system and designated with a time-in-force of IOC (immediate-or-cancel), DAY (day order), GTC (good-till-cancelled), and OPG (On the Open Order).<sup>14</sup>

The Exchange would also revise the definition of this term to specify that orders received via FIX protocol prior to the Nasdaq Opening Cross designated with a time-in-force of IOC would be rejected and shall not be considered Eligible Interest, and orders received via OTTO and SQF protocols prior to the Nasdaq Opening Cross designated with a time-in-force of IOC would remain in force through the opening but be cancelled immediately after the

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<sup>10</sup> See proposed Section 8(a)(2)(A). The Exchange states that the revised definition of Current Reference Price would be substantively similar to the current definition, but with the opening cross price determined pursuant to Section 8(b). See Notice, 79 FR at 73383.

<sup>11</sup> See Section 8(a)(2)(E).

<sup>12</sup> See proposed Section 8(a)(2), from which current Section 8(a)(2)(E) would be deleted.

<sup>13</sup> See proposed Section 8(a)(3).

<sup>14</sup> See proposed Section 8(a)(4).

opening.<sup>15</sup> The Exchange notes that FIX protocol users generally prefer a cancellation if an order is not executed immediately so that they can have an opportunity to access other markets, while OTTO and SQF protocol users are liquidity providers who prefer that their orders live throughout the entire opening process until it is clear that their liquidity was not utilized in the opening.<sup>16</sup>

- The Exchange also proposes to add new terms “Valid Width National Best Bid or Offer” (or “Valid Width NBBO”) and “Away Best Bid or Offer” (or “ABBO”) to Section 8(a).

Specifically, in new Section 8(a)(6), the Exchange proposes to define “Valid Width NBBO” as the combination of all away market quotes and any combination of NOM-registered Market Maker (“Market Maker”) orders and quotes received over the OTTO or SQF protocols within a specified bid/ask differential as established and published by the Exchange. The Valid Width NBBO would be configurable by underlying, and a table with valid width differentials would be posted by Nasdaq on its website.<sup>17</sup> Away markets that are crossed (i.e., an away market is internally crossed or crosses another away market) would void all Valid Width NBBO calculations.<sup>18</sup> If any Market Maker orders or quotes on NOM are crossed internally, then all such orders and quotes would be excluded from the Valid Width NBBO calculation.<sup>19</sup> In addition, in new Section 8(a)(7), the Exchange proposes to define “ABBO” as the displayed National Best Bid or Offer not including the Exchange’s Best Bid or Offer. The Exchange states that it is proposing to add these new terms in order to

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<sup>15</sup> Id.

<sup>16</sup> See Notice, 79 FR at 73383.

<sup>17</sup> See proposed Section 8(a)(6).

<sup>18</sup> Id.; see also Notice, 79 FR at 73384.

<sup>19</sup> See proposed Section 8(a)(6).

ensure that all away market quotes and any combination of Market Maker orders and quotes, whether they include the Exchange's Best Bid or Offer or not, are represented in the opening cross.<sup>20</sup>

#### Processing of Nasdaq Opening Cross – Section 8(b)

The Exchange proposes various revisions to the Nasdaq Opening Cross process set forth in Section 8(b). As an initial matter, the Exchange proposes to edit the introductory paragraph of Section 8(b) by: deleting the phrase “there is no Imbalance” so that the rule applies more generally; deleting the phrase “on a class-by-class basis” in order to clarify that the Exchange will use a regular market hours quote or trade (as determined by the Exchange) for all classes on the Exchange for the Opening Cross without distinguishing among different classes; and adding the phrase “the Opening Process shall occur” in order to clarify that an Opening Cross shall occur after a trading halt when trading resumes pursuant to Chapter V, Section 4.<sup>21</sup>

Following the introductory paragraph, the Exchange proposes to set forth the criteria that must be present for NOM to open trading at the beginning of the day or after a halt, provided the ABBO is not crossed.<sup>22</sup> Specifically, the rule would state that, if a trade is possible on NOM, there must be a Valid Width NBBO before trading will open;<sup>23</sup> and if no trade is possible on NOM, then trading would open upon the occurrence of any one of the following three criteria:

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<sup>20</sup> See Notice, 79 FR at 73384. The Exchange also notes that, with respect to the Valid Width NBBO, the orders and quotes on the Exchange would be received over the OTTO or SQF protocols. Id.

<sup>21</sup> See proposed Section 8(b); see also Notice, 79 FR at 73384. Chapter V, Section 4 states that trading in an option that has been the subject of a halt under Section 3 of Chapter V shall be resumed upon the determination by Nasdaq Regulation that the conditions which led to the halt are no longer present or that the interests of a fair and orderly market are best served by a resumption of trading. According to the Exchange, trading shall resume according to the process set forth in proposed Section 8(b). See Notice, 79 FR at 73383.

<sup>22</sup> See proposed Section 8(b).

<sup>23</sup> See proposed Section 8(b)(1).

(A) a Valid Width NBBO is present, (B) a certain number of other options exchanges (as determined by the Exchange) have disseminated a firm quote on OPRA, or (C) a certain period of time (as determined by the Exchange) has elapsed.<sup>24</sup>

In addition, the Exchange proposes to add language in proposed Section 8(b)(4)(A)-(C) to specify how the Opening Cross price would be determined when a trade is possible on NOM and a Valid Width NBBO is present. Proposed Section 8(b)(4)(A) would state that the Nasdaq Opening Cross shall occur at the price that maximizes the number of contracts of Eligible Interest in NOM to be executed at or within the ABBO and within a defined range, as established and published by the Exchange, of the Valid Width NBBO.<sup>25</sup> Proposed Section 8(b)(4)(B) would state that if more than one price exists under subparagraph (A) and there are no contracts that would remain unexecuted in the cross, the Nasdaq Opening Cross shall occur at the midpoint price, rounded to the penny closest to the price of the last execution in that series (and in the absence of a previous execution price, the price will round up, if necessary),<sup>26</sup> of (1) the National Best Bid or the last offer on NOM against which contracts would be traded, whichever is higher; and (2) the National Best Offer or the last bid on NOM against which contracts would

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<sup>24</sup> See proposed Section 8(b)(2). In the case of a crossed ABBO, the Exchange notes that the conditions set forth in proposed Sections 8(b)(1) and (b)(2) would become operative when the ABBO becomes uncrossed. See Notice, 79 FR at 73384 n.18. Additionally, the Exchange notes that, due to its proposed addition of new Sections 8(b)(1) and (b)(2), it has proposed to renumber current Sections 8(b)(1) through 8(b)(5) to 8(b)(3) through 8(b)(7), respectively. See Notice, 79 FR at 73386.

<sup>25</sup> See proposed Section 8(b)(4)(A).

<sup>26</sup> The Exchange notes that rounding would be applied, if needed, in the following manner: if the previous closing price is less than the midpoint, then the opening price rounds down; and if the previous closing price is greater than the midpoint, or if there is no closing price, then the opening price rounds up. For example, if there is a midpoint of 1.045, the opening price would be rounded to 1.04 if the previous closing price was 1.00, and would be rounded to 1.05 if the previous closing price was 1.10. See Notice, 79 FR at 73385 n.22.

be traded, whichever is lower.<sup>27</sup> Proposed Section 8(b)(4)(C) would state if more than one price exists under subparagraph (A) and contracts would remain unexecuted in the cross, then the opening price would be the highest (lowest) price in the case of a buy (sell) imbalance at which the maximum number of contracts can trade which is equal to or within a defined range, as established and published by the Exchange,<sup>28</sup> of the Valid Width NBBO on the contra side of the imbalance that would not trade through the ABBO.<sup>29</sup>

Further, the Exchange proposes to add subsections to proposed Section 8(b)(4)(C) in order to specify the price at which unexecuted contracts would be posted on the book following the Opening Cross and the subsequent handling of the residual unexecuted contracts.<sup>30</sup> These subsections would provide as follows: (i) if unexecuted contracts remain with a limit price that is equal to the opening price, then the remaining unexecuted contracts would be posted at the opening price, displayed one minimum price variation (MPV) away if displaying at the opening price would lock or cross the ABBO, with the contra-side NOM BBO reflected as firm; (ii) if unexecuted contracts remain with a limit price that is through the opening price, and there is a contra side ABBO at the opening price, then the remaining unexecuted contracts would be posted at the opening price, displayed one minimum price variation (MPV) away from the ABBO, with the contra side NOM BBO reflected as firm, and order handling of any remaining interest would be done in accordance with the routing and time-in-force instructions of such interest and would follow the Acceptable Trade Range mechanism set forth in Section 10; (iii) if

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<sup>27</sup> See proposed Section 8(b)(4)(B).

<sup>28</sup> The Exchange notes that, pursuant to Section 10(7), the system will also calculate a defined range to limit the range of prices at which an order would be allowed to execute. See Notice, 79 FR at 73385 n.23.

<sup>29</sup> See proposed Section 8(b)(4)(C).

<sup>30</sup> See proposed Section 8(b)(4)(C)(i)-(iv).

unexecuted contracts remain with a limit price that is through the opening price, and there is no contra side ABBO at the opening price, then the remaining contracts would be posted at the opening price, with the contra-side NOM BBO reflected as non-firm; and (iv) order handling of any residual unexecuted contracts would be done in accordance with Section 10(7), with the opening price representing the reference price.<sup>31</sup>

This proposed handling of unexecuted contracts set forth in subsections (i)-(iv) of proposed Section 8(b)(4)(C) is intended to ensure that residual unexecuted contracts from the Opening Cross, regardless of their limit prices, are posted on the book at the opening price before subsequently being routed pursuant to Section 11 or walked to the next potential execution price(s) under the Acceptable Trade Range set forth in Section 10(7) (with the opening price representing the “reference price” of that rule).<sup>32</sup> Moreover, the “firm” versus “non-firm” tagging of contra-side interest when residual Opening Cross interest is posted follows the construct currently in place on the Exchange when aggressive interest is received and triggers an Acceptable Trade Range (ATR) process.<sup>33</sup> Contra-side NOM BBO interest is reflected as non-firm when the Exchange has interest with a limit price (or market order) that is more aggressive than the Opening Cross price in order to ensure that aggressively priced residual interest maintains priority should other aggressively priced interest be entered before the residual interest is permitted to access the next allowable range of prices.<sup>34</sup>

The Exchange is also proposing to add new text to proposed Section 8(b)(5) to indicate that if the Nasdaq Opening Cross price is selected and fewer than all contracts of Eligible Interest

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<sup>31</sup> Id.

<sup>32</sup> See Notice, 79 FR at 73386.

<sup>33</sup> Id.

<sup>34</sup> Id.



that are available in NOM would be executed, all Eligible Interest shall be executed at the Nasdaq Opening Cross price in accordance with the execution algorithm assigned to the associated underlying option.<sup>35</sup>

#### Absence of Opening Cross – Section 8(c)

Lastly, the Exchange proposes to add a new Section 8(c) providing for the return of orders in un-opened symbols in the absence of an Opening Cross. Proposed new Section 8(c) would be substituted for current Section 8(c) and would provide that if an Opening Cross in a symbol is not initiated before the conclusion of the Opening Order Cancel Timer, a firm may elect to have orders returned by providing written notification to the Exchange.<sup>36</sup> These orders include all non GTC orders received over the FIX protocol.<sup>37</sup> The Opening Order Cancel Timer represents a period of time since the underlying market has opened, and shall be established and disseminated by Nasdaq on its website.<sup>38</sup>

### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>39</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>40</sup> which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and

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<sup>35</sup> See proposed Section 8(b)(5).

<sup>36</sup> See proposed Section 8(c).

<sup>37</sup> Id.

<sup>38</sup> Id.

<sup>39</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>40</sup> 15 U.S.C. 78f(b)(5).

practices, 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 proposal is consistent with Section 6(b)(5) of the Act because it will enhance and clarify the opening cross process, minimize or negate unnecessary complexity, and encourage liquidity when trading opens. The Exchange notes that it proposes to set forth in Section 8(b) clear language describing under what circumstances an opening cross will occur, and how the opening cross will occur if more than one possible cross price exists. In addition, according to the Exchange, the proposed rule change will enhance the price discovery mechanism in the opening process by including not only Market Maker orders and quotes but also away market interest as represented by quotes. The Exchange believes this change will make the transition from the opening cross period to regular market trading more efficient and thus promote just and equitable principles of trade and serve to protect investors and the public interest. The Exchange also believes that the proposal will significantly improve the quality of execution of NOM's opening, which should attract new order flow. In the Exchange's view, the proposed rule changes should prove helpful to market participants, particularly those that are involved in adding liquidity during the opening cross.

The Commission believes that the proposal is reasonably 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 to protect investors and the public interest by adding clarity to the Exchange's rules governing NOM's opening cross process. This enhanced transparency should help to reduce the potential for investor confusion as to when an opening cross occurs, how the price for the opening cross is determined, and how orders involved in the

opening cross are handled. The Commission also believes that the proposed opening cross process is reasonably designed to open trading in a fair and orderly manner, which is consistent with the protection of investors and the public interest. Additionally, to extent the proposal results in additional liquidity during NOM's opening at the beginning of the trading day or following a trading halt, and a more orderly transition to regular trading, it should further promote the goals of Section 6(b)(5) of the Act.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>41</sup> that the proposed rule change (SR-NASDAQ-2014-116) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>42</sup>

Brent J. Fields  
Secretary

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<sup>41</sup> 15 U.S.C. 78s(b)(2).

<sup>42</sup> 17 CFR 200.30-3(a)(12).