SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-79290; File Nos. SR-BX-2016-046; SR-NASDAQ-2016-111)

November 10, 2016

Self-Regulatory Organizations; NASDAQ BX, Inc.; The Nasdaq Stock Market LLC; Order
Approving Proposed Rule Changes, as Modified by Amendments No. 1, Relating to Post-Only
Orders and Orders with Midpoint Pegging

I.   Introduction

On September 13, 2016, NASDAQ BX, Inc. ("BX") and The Nasdaq Stock Market LLC

("Nasdaq") (individually, an "Exchange," and together, the "Exchanges") 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] proposed rule changes

relating to Post-Only Orders and Orders with Midpoint Pegging. The proposed rule changes

were published for comment in the Federal Register on September 28, 2016.[3] On October 5,

2016, Nasdaq filed Amendment No. 1 to its proposed rule change ("Nasdaq Amendment No. 1")

and on November 3, 2016, BX filed Amendment No. 1 to its proposed rule change ("BX

Amendment No. 1").[4] The Commission received one comment letter on Nasdaq's proposed rule

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[1]   15 U.S.C. 78s(b)(1).

[2]   17 CFR 240.19b-4.

[3]   See Securities Exchange Act Release Nos. 78909 (September 22, 2016), 81 FR 66708
        ("BX Notice") and 78908 (September 22, 2016), 81 FR 66702 ("Nasdaq Notice").

[4]   In their respective Amendment No. 1, BX and Nasdaq modified the discussion of their
        respective proposal to reflect that, pursuant to proposed BX and Nasdaq Rules
        4702(b)(4)(A), if the adjusted price of a Post-Only Order would lock or cross a non-
        displayed price on the respective Exchange's Book, the Post-Only Order would be posted
        in the same manner as a Price to Comply Order. BX Amendment No. 1 is available at:
        https://www.sec.gov/comments/sr-bx-2016-046/bx2016046-1.pdf and Nasdaq
        Amendment No. 1 is available at: https://www.sec.gov/comments/sr-nasdaq-2016-
        111/nasdaq2016111-1.pdf. Because these amendments are technical in nature and do not
        materially alter the substance of the proposed rule changes, they are not subject to notice
        and comment.

change[5] and a response letter from Nasdaq.[6] The Commission is approving the Exchanges' proposals, as modified by their corresponding Amendment No. 1.

II.   Description of the Proposed Rule Changes

The Exchanges are proposing to amend the behavior of Post-Only Orders when they interact with resting Non-Displayed Orders, and the behavior of Orders with Midpoint Pegging in a crossed market. The Exchanges' proposals are substantively identical in many respects. Therefore, the description below describes the proposals jointly but notes material differences where applicable.[7]

Currently, BX and Nasdaq Rules 4702(b)(4)(A) provide that, if the adjusted price[8] of a Post-Only Order would lock or cross an Order on the respective Exchange's Book, the Post-Only Order would be repriced, ranked, and displayed at one minimum price increment below the current best-priced Order to sell on the respective Exchange's Book (for bids) or above the current best-priced Order to buy on the respective Exchange's Book (for offers). Under the

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[5]   See Letter from Joseph Saluzzi and Sal Arnuk, Partners, Themis Trading LLC, to Brent J. Fields, Secretary, Commission, dated October 10, 2016 ("Themis Letter").

[6]   See Letter from Jeffrey S. Davis, Vice President and Deputy General Counsel, The NASDAQ Stock Market LLC, to Brent J. Fields, Secretary, Commission, dated November 8, 2016 ("Response Letter").

[7]   For more details regarding the Exchanges' proposals, see Nasdaq Notice and BX Notice, supra note 3.

[8]   According to BX and Nasdaq Rules 4702(b)(4)(A), if a Post-Only Order would lock or cross a Protected Quotation, the price of the Order would first be adjusted. If the Order is Attributable, its adjusted price would be one minimum price increment lower than the current Best Offer (for bids) or higher than the current Best Bid (for offers). If the Order is not Attributable, its adjusted price would be equal to the current Best Offer (for bids) or the current Best Bid (for offers). However, the Order would not post or execute until the Order, as adjusted, is evaluated with respect to Orders on the respective Exchange's Book.

proposals,[9] if the adjusted price of the Post-Only Order would lock or cross a non-displayed price

on the respective Exchange's Book, the Post-Only order would be posted in the same manner as

a Price to Comply Order.[10] However, the Post Only Order would execute:

- on Nasdaq if (i) it is priced below $1.00 and the value of price improvement

  associated with executing against an Order on the Nasdaq Book (as measured

  against the original limit price of the Order) equals or exceeds the sum of fees

  changed for such execution and the value of any rebate that would be provided if

  the Order posted to the Nasdaq Book and subsequently provided liquidity, or (ii)

  it is priced at $1.00 or more and the value of price improvement associated with

  executing against an Order on the Nasdaq Book (as measured against the original

  limit price of the Order) equals or exceeds $0.01 per share;[11] and

- on BX, if (i) it is priced at $1.00 or more,[12] or (ii) it is priced below $1.00 and the

  value of price improvement associated with executing against an Order on the

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[9]   The Exchanges are also proposing conforming changes throughout BX and Nasdaq Rules 4702(b)(4)(A) to reflect this change.

[10]   According to BX and Nasdaq Rules 4702(b)(1)(A), if the entered limit price of a Price to Comply Order would lock or cross a Protected Quotation and the Price to Comply Order could not execute against an Order on the respective Exchange's Book at a price equal to or better than the price of the Protected Quotation, the Price to Comply Order will be displayed on the respective Exchange's Book at a price one minimum price increment lower than the current Best Offer (for a Price to Comply Order to buy) or higher than the current Best Bid (for a Price to Comply Order to sell), but will also be ranked on the respective Exchange's Book with a non-displayed price equal to the current Best Offer (for a Price to Comply Order to buy) or the current Best Bid (for a Price to Comply Order to sell).

[11]   This behavior related to the execution of the Post-Only Order is not changed by Nasdaq's proposal.

[12]   On BX, unlike on Nasdaq, executions in securities priced at or above $1 result in rebates for the accessor of liquidity and as such it is always in the best interest of the incoming Post-Only Order to execute in securities at or above $1.

Exchange Book (as measured against the original limit price of the Order) equals or exceeds the sum of fees charged for such execution and the value of any rebate that would be provided if the Order posted to the Exchange Book and subsequently provided liquidity.[13]

Currently, BX and Nasdaq Rules 4702(b)(4)(A) also provide that, if the Post-Only Order would not lock or cross a Protected Quotation but would lock or cross an Order on the respective Exchange's Book, the Post Only Order would be repriced, ranked, and displayed at one minimum price increment below the current best-priced Order to sell on the respective Exchange's Book (for bids) or above the current best-priced Order to buy on the respective Exchange's Book (for offers). Under the proposals,[14] if the Post-Only Order would not lock or cross a Protected Quotation but would lock or cross a Non-Displayed Order on the respective Exchange's Book, the Post-Only Order would be posted, ranked, and displayed at its limit price.[15] However, the Post Only Order would execute:

- on Nasdaq if (i) it is priced below $1.00 and the value of price improvement associated with executing against an Order on the Nasdaq Book equals or exceeds the sum of fees charged for such execution and the value of any rebate that would be provided if the Order posted to the Nasdaq Book and subsequently provided liquidity, or (ii) it is priced at $1.00 or more and the value of price improvement

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[13] This behavior related to the execution of the Post-Only Order is not changed by BX's proposal.

[14] The Exchanges are also proposing conforming changes throughout BX and Nasdaq Rules 4702(b)(4)(A) to reflect this change.

[15] One effect of this proposal is that, when a Post-Only Order encounters a Non-Displayed Order that is a Midpoint Peg Order and posts at its limit price, the Post-Only Order would establish a new NBBO and the Midpoint Peg Order would either be cancelled or re-adjusted based on the change to the NBBO.

associated with executing against an Order on the Nasdaq Book equals or exceeds $0.01 per share; [16] and

- on BX, if (i) it is priced at $1.00 or more,[17] or (ii) it is priced below $1.00 and the value of price improvement associated with executing against an Order on the Exchange Book equals or exceeds the sum of fees charged for such execution and the value of any rebate that would be provided if the Order posted to the Exchange Book and subsequently provided liquidity.[18]

Currently, Nasdaq Rule 4702(b)(5)(A) provides that, if the NBBO is crossed, a Midpoint Peg Post-Only Order[19] would nevertheless be priced at the midpoint between the NBBO. Currently, BX and Nasdaq Rules 4703(d) provide that, in the case of an Order with Midpoint Pegging,[20] if the Inside Bid and Inside Offer are crossed, the Order would nevertheless be priced at the midpoint between the Inside Bid and the Inside Offer. Moreover, even if the Inside Bid and Inside Offer are crossed, an Order with Midpoint Pegging that crossed an Order on the respective Exchange's Book would execute. Under the proposed amendments to Nasdaq Rule

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[16] This behavior related to the execution of the Post-Only Order is not changed by Nasdaq's proposal.

[17] On BX, unlike on Nasdaq, executions in securities priced at or above $1 result in rebates for the accessor of liquidity and as such it is always in the best interest of the incoming Post-Only Order to execute in securities at or above $1.

[18] This behavior related to the execution of the Post-Only Order is not changed by BX's proposal.

[19] According to Nasdaq Rule 4702(b)(5)(A), a Midpoint Peg Post-Only Order is an Order Type with a Non-Display Order Attribute that is priced at the midpoint between the NBBO and that would execute upon entry only in circumstances where economically beneficial to the party entering the Order.

[20] According to BX and Nasdaq Rules 4703(d), Midpoint Pegging means Pegging with reference to the midpoint between the Inside Bid and the Inside Offer. The price to which an Order is pegged is referred to as the Inside Quotation, Inside Bid, or Inside Offer, as appropriate.

4702(b)(5)(A), if the NBBO is crossed, any existing Midpoint Peg Post-Only Order would be cancelled and any new Midpoint Peg Post-Only Order would be rejected. Similarly, under the proposed amendments to BX and Nasdaq Rules 4703(d), if the Inside Bid and Inside Offer are crossed, any existing Order with Midpoint Pegging would be rejected and any new Order with Midpoint Pegging would be cancelled.

III.   Summary of Comments and Response to Comments

The Commission received a comment letter opposing Nasdaq's proposal and a response letter from Nasdaq.[21]

Regarding Nasdaq's proposal, the commenter specifically questions whether allowing Post-Only Orders to lock Non-Displayed Orders would help or enhance price discovery.[22] The commenter also questions whether allowing this locking behavior would undermine investors' reliance on the public market of bids, offers, and trades to reflect the true price of an asset.[23] Moreover, the commenter questions the impact of this proposal on the ban against locked and crossed markets.[24] Finally, the commenter questions whether allowing a non-displayed locked market would maintain fair and orderly efficient markets, facilitate capital formation, and protect and serve the interests of investors.[25]

In response to these comments, Nasdaq states that its proposal to modify the processing of Post-Only Orders under a narrow set of conditions would ensure that the market operates as

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[21]   See supra notes 5 and 6.

[22]   See Themis Letter at 3.

[23]   See id.

[24]   See id. at 4.

[25]   See id. This commenter also urges the Commission to eliminate all post-only order types. See id. at 1. The Commission notes that the comment urging the elimination of all post-only orders types is beyond the scope of the proposals.

efficiently as possible, reduce information leakage, and improve execution quality.[26] In addition, according to Nasdaq, posting Post-Only Orders at their limit price would result in tighter bid-ask spreads relative to the current re-pricing practice, and tighter spreads would reflect enhanced price discovery.[27] Moreover, according to Nasdaq, many economists believe that a locked market is "the truest reflection of the price of an asset."[28] Therefore, Nasdaq believes that allowing buyers and sellers to reflect their true demand and supply prices, rather than re-pricing to an artificial price, would enhance investors' experience on Nasdaq.[29] Nasdaq notes that the proposal does not permit a locked market as defined by Rule 610 of Regulation NMS, as Rule 610 defines a locked market as the display of bids and offers at the same price, while Nasdaq's proposal would involve only the display of a bid or an offer, but not both.[30] Finally, Nasdaq states its belief that the proposal is consistent with maintaining fair and orderly markets, efficient capital formation, and the protection of investors.[31] According to Nasdaq, the proposal would lead to tighter spreads, better execution prices, and lower information leakage for investors who currently quote and trade on Nasdaq.[32] Nasdaq states that it anticipates that, as a result of the proposal, current members would quote and trade more actively and new members would commence quoting and trading, which would further enhance the quality of the Nasdaq market.[33]

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[26]   See Response Letter at 1-2.

[27]   See id. at 2.

[28]   See id. at 3.

[29]   See id.

[30]   See id.

[31]   See id.

[32]   See id.

[33]   See id.

IV.   Commission Findings

After careful review, the Commission finds that the proposed rule changes, as modified

by Amendments No. 1, are consistent with the requirements of the Act and the rules and

regulations thereunder applicable to a national securities exchange.[34] In particular, the

Commission finds that the proposed rule changes, as modified by Amendments No. 1, are

consistent with Section 6(b)(5) of the Act,[35] 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 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 Commission notes that the Exchanges believe that the proposals related to the

interaction between Post-Only Orders and Non-Displayed Orders would help to reduce the

information leakage that can occur when a Post-Only Order re-prices to avoid locking or

crossing the price of a Non-Displayed Order resting on the respective Exchange's book.[36]

Specifically, under the proposals, if a Post-Only Order would not lock or cross a Protected

Quotation but would lock or cross a Non-Displayed Order on the respective Exchange's Book,

the Post-Only Order would be posted, ranked, and displayed at its limit price, rather than be re-

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[34]   In approving this proposed rule change, the Commission has considered the proposed
rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

[35]   15 U.S.C. 78f(b)(5).

[36]   The Commission notes that, in conjunction with these proposals, the Exchanges are
adopting the Trade Now instruction, which is an Order Attribute that would allow a
resting Order that becomes locked by an incoming Displayed Order to execute against the
available size of the contra-side locking Order as a liquidity taker. See Securities
Exchange Act Release Nos. 79281 (November 10, 2016) (SR-BX-2016-059) and 79282
(November 10, 2016) (SR-NASDAQ-2016-156).

priced. In addition, if the adjusted price of a Post-Only Order would lock or cross a non-displayed price on the respective Exchange's Book, the Post-Only Order would be posted in the same manner as a Price to Comply Order (i.e., displayed at a price one minimum price increment lower than the current Best Offer (for a buy order) or higher than the current Best Bid (for a sell order); ranked with a non-displayed price equal to the current Best Offer (for a buy order) or the current Best Bid (for a sell order)).

The Commission notes that the Exchanges' proposals to discontinue pricing and executing Midpoint Peg Post-Only Orders (Nasdaq only) and Orders with Midpoint Pegging when the NBBO is crossed would reflect that the midpoint of a crossed market is not a clear and accurate indication of a valid price and would avoid mispriced executions. The Commission also notes that this proposed behavior is similar to the rules of other exchanges.[37]

Based on the foregoing and the Exchanges' representations, the Commission believes that the proposed rule changes, as modified by Amendments No. 1, are consistent with the Act.

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[37]   See, e.g., BatsBZX Rule 11.9(c)(9).

V.   Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[38] that the

proposed rule changes (SR-BX-2016-046 and SR-NASDAQ-2016-111), as modified by their

respective Amendment No. 1, be, and they hereby are, approved.

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

authority.[39]

Brent J. Fields
Secretary

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[38]   15 U.S.C. 78s(b)(2).

[39]   17 CFR 200.30-3(a)(12).