

Required fields are shown with yellow backgrounds and asterisks.

Filing by NASDAQ BX, Inc.  
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial *	Amendment *	Withdrawal	Section 19(b)(2) *	Section 19(b)(3)(A) *	Section 19(b)(3)(B) *
<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
			Rule		
Pilot	Extension of Time Period for Commission Action *	Date Expires *	<input type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
<input type="checkbox"/>	<input type="checkbox"/>	<input type="text"/>	<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input checked="" type="checkbox"/> 19b-4(f)(6)	

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010	Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934
Section 806(e)(1) *	Section 806(e)(2) *
<input type="checkbox"/>	<input type="checkbox"/>
	Section 3C(b)(2) *
	<input type="checkbox"/>

Exhibit 2 Sent As Paper Document	Exhibit 3 Sent As Paper Document
<input type="checkbox"/>	<input type="checkbox"/>

**Description**

Provide a brief description of the action (limit 250 characters, required when Initial is checked \*).

A proposal to make permanent certain options market rules that are linked to the equity market Plan to Address Extraordinary Market Volatility.

**Contact Information**

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name \* Sun Last Name \* Kim

Title \* Associate General Counsel

E-mail \* Sun.Kim@Nasdaq.com

Telephone \* (212) 231-5106 Fax

**Signature**

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

(Title \*)

Date 10/18/2019 EVP, Chief Legal Counsel

By John A. Zecca

(Name \*)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

**Form 19b-4 Information \***

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

(a) Nasdaq BX, Inc. (“BX” or “Exchange”), 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> is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposal to make permanent certain options market rules that are linked to the equity market Plan to Address Extraordinary Market Volatility.

A notice of the proposed rule change for publication in the Federal Register is attached as Exhibit 1. The text of the proposed rule change is attached as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by senior management of the Exchange pursuant to authority delegated by the Board of Directors of the Exchange (the “Board”) on September 25, 2019. Exchange staff will advise the Board of any action taken pursuant to delegated authority. No other action is necessary for the filing of the rule change.

Questions and comments on the proposed rule change may be directed to:

Sun Kim  
Associate General Counsel  
Nasdaq, Inc.  
212-231-5106

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

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

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

a. Purpose

The purpose of the proposed rule change is to make permanent certain options market rules in connection with the equity market Plan to Address Extraordinary Market Volatility (the "Limit Up-Limit Down Plan" or the "Plan"). This change is being proposed in connection with the recently approved amendment to the Limit Up-Limit Down Plan that allows the Plan to continue to operate on a permanent basis ("Amendment 18").<sup>3</sup> This proposed rule change is substantially similar to a recently-approved rule change by Cboe Exchange, Inc. ("Cboe").<sup>4</sup>

In an attempt to address extraordinary market volatility in NMS Stocks, and, in particular, events like the severe volatility on May 6, 2010, U.S. national securities exchanges and the Financial Industry Regulatory Authority, Inc. (collectively, "Participants") drafted the Plan pursuant to Rule 608 of Regulation NMS and under the Act.<sup>5</sup> On May 31, 2012, the Commission approved the Plan, as amended, on a one-year

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<sup>3</sup> See Securities Exchange Act Release No. 85623 (April 11, 2019), 84 FR 16086 (April 17, 2019) (Order Approving Amendment No. 18).

<sup>4</sup> See Securities Exchange Act Release Nos. 86744 (August 23, 2019), 84 FR 45565 (August 29, 2019) (SR-CBOE-2019-049) (Notice of Filing); and 87311 (October 15, 2019) (SR-CBOE-2019-049) (Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment Nos. 1 and 2). The Exchange understands that the other national securities exchanges will also file similar proposals to make permanent their respective pilot programs.

<sup>5</sup> See Securities Exchange Act Release No. 64547 (May 25, 2011), 76 FR 31647 (June 1, 2011) (File No. 4-631).

pilot basis.<sup>6</sup> Though the Plan was primarily designed for equity markets, the Exchange believed it would, indirectly, potentially impact the options markets as well. Thus, the Exchange has previously adopted and amended Chapter V, Section 3(d) to ensure the option markets were not harmed as a result of the Plan's implementation and has implemented such rules on a pilot basis that has coincided with the pilot period for the Plan (the "Options Pilots").<sup>7</sup> Chapter V, Section 3(d) addresses the interplay of the Exchange's rules in response to the Plan, and includes provisions on how the Exchange will treat certain options orders during a limit or straddle state as well as options market maker quoting obligations during a limit or straddle state. In addition, Section 3(d)(iv) provides that during a limit or straddle state, trades are not subject to obvious or catastrophic error review. A limit or straddle state occurs when at least one side of the National Best Bid ("NBB") or Offer ("NBO") bid/ask is priced at a non-tradable level. Specifically, a straddle state exists when the NBB is below the lower price band while the NBO is inside the prices band or when the NBO is above the upper price band and the NBB is within the band, while a limit state occurs when the NBO equals the lower price band (without crossing the NBB), or the NBB equals the upper price band (without crossing the NBO). The Exchange adopted the Options Pilots to protect investors because when an underlying security is in a limit up-limit down state, there will not be a reliable price for the security to serve as a benchmark for the

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<sup>6</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012) 77 FR 33498 (June 6, 2012).

<sup>7</sup> See Securities Exchange Act Release Nos. 69119 (March 12, 2013), 78 FR 16746 (March 18, 2013) (SR-BX-2013-021); 69334 (April 5, 2013), 78 FR 21653 (April 11, 2013) (SR-BX-2013-022); and 69343 (April 8, 2013), 78 FR 21982 (April 12, 2013) (SR-BX-2013-026).

price of the option. Specifically, the Exchange adopted Chapter V, Section 3(d)(iv) because the application of the obvious and catastrophic error rules would be impracticable given the potential for lack of a reliable NBBO in the options market during limit and straddle states. When adjusting or busting a trade pursuant to the obvious error rule, the determination of theoretical value of a trade generally references the NBB (for erroneous sell transactions) or NBO (for erroneous buy transactions) just prior to the trade in question, and is therefore not reliable when at least one side of the NBBO is priced at a non-tradeable level, as is the case in limit and straddle states. In such a situation, determining theoretical value may often times be a very subjective rather than an objective determination and could give rise to additional uncertainty and confusion for investors. As a result, application of the obvious and catastrophic error rules would be impracticable given the lack of a reliable NBBO in the options market during limit and straddle states, and may produce undesirable effects or unanticipated consequences. As noted above, the Exchange adopted additional measures via other Options Pilot rules that are designed to protect investors during limit and straddle states.<sup>8</sup> For example, the Exchange will reject Market Orders (as defined in Chapter VI, Section 1) during a Limit Up-Limit Down state to ensure that only those orders with a limit price will be executed during a limit or straddle state given the uncertainty of market prices during such a state. Furthermore, the Exchange believes that eliminating the application of obvious error rules during a limit or straddle state eliminates the re-evaluation of a transaction executed during such a state that could potentially create an unreasonable adverse selection opportunity due to the lack of a reliable reference price on one side of the

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<sup>8</sup> As set forth in Chapter V, Section 3(d), this includes rules in connection with special handling for Market Orders, and options market maker quoting obligations during a limit or straddle state.

market or another and discourage participants from providing liquidity during limit and straddle states, which is contrary to the goal in limiting participants' adverse selection with the application of the obvious error rule during normal trading states. For these reasons, the Exchange believes the Options Pilots and related rules are designed to add certainty on the options markets, which encourages more investors to participate in light of the changes associated with the Plan. The Plan was originally implemented on a pilot-basis in order to allow the public, the participating exchanges, and the Commission to assess the operation of the Plan and whether the Plan should be modified prior to approval on a permanent basis. As stated, the Exchange adopted the Option Pilots to coincide with this pilot; to continue the protections therein while the industry gains further experience operating the Plan.

In connection with the order approving the establishment of the obvious error pilot, as well as the extensions of the obvious error pilot, the Exchange committed to submit monthly data regarding the program and to submit an overall analysis of the obvious error pilot in conjunction with the data submitted under the Plan and any other data as requested by the Commission. Pursuant to a rule filing, approved on April 8, 2014, each month, the Exchange committed to provide the Commission, and the public, a dataset containing the data for each straddle and limit state in optionable stocks that had at least one trade on the Exchange.<sup>9</sup> The Exchange has continued to provide the Commission with this data on a monthly basis. For each trade on the Exchange, the Exchange provides (a) the stock symbol, option symbol, time at the start of the straddle or limit state, an indicator for whether it is a straddle or limit state, and (b) for the trades

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<sup>9</sup> See Securities Exchange Act Release No. 71900 (April 8, 2014), 79 FR 20951 (April 14, 2014) (SR-BX-2014-017); see also BX LULD Reports, available at: <https://www.nasdaq.com/solutions/options/LULD>.

on the Exchange, the executed volume, time-weighted quoted bid-ask spread, time-weighted average quoted depth at the bid, time-weighted average quoted depth at the offer, high execution price, low execution price, number of trades for which a request for review for error was received during straddle and limit states, an indicator variable for whether those options outlined above have a price change exceeding 30% during the underlying stock's limit or straddle state compared to the last available option price as reported by OPRA before the start of the limit or straddle state. In addition, to help evaluate the impact of the pilot program, the Exchange has provided to the Commission, and the public, assessments relating to the impact of the operation of the obvious error rules during limit and straddle states including: (1) an evaluation of the statistical and economic impact of limit and straddle states on liquidity and market quality in the options markets, and (2) an assessment of whether the lack of obvious error rules in effect during the straddle and limit states are problematic. The Exchange has concluded that the Options Pilots do not negatively impact market quality during normal market conditions,<sup>10</sup> and that there has been insufficient data to assess whether a lack of obvious error rules is problematic, however, the Exchange believes the continuation of the Options Pilots function to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets.

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<sup>10</sup> See also BX LULD Reports, available at: <https://www.nasdaq.com/solutions/options/LULD>. During the most recent Review Period the Exchange did not receive any obvious error review requests for Limit-Up-Limit Down trades, and Limit Up-Limit Down trade volume accounted for nominal overall trade volume.



The Commission recently approved the Plan on a permanent basis (Amendment 18).<sup>11</sup> In connection with this approval, the Exchange now proposes to amend Chapter V, Section 3(d) that currently implement provisions of the Plan on a pilot basis to eliminate the pilot basis, which effectiveness expires on October 18, 2019, and to make such rules permanent. In its approval order to make the Plan permanent, the Commission recognized that, as a result of the Participants' and industry analysis of the Plan's operation, the Limit Up-Limit Down mechanism effectively addresses extraordinary market volatility. Indeed, the Plan benefits markets and market participants by helping to ensure orderly markets, but also, the Exchange believes, based on the data made available to the public and the Commission during the pilot period, that the obvious error pilot does not negatively impact market quality during normal market conditions.<sup>12</sup> Rather, the Exchange believes the obvious error pilot functions to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets. The Exchange also believes the other Options Pilots rules provide additional measures designed to protect investors during limit and straddle states. For example, the Exchange will reject Market Orders during a Limit Up-Limit Down state to ensure that only those orders with a limit price will be executed during a limit or straddle state given the uncertainty of market prices during such a state.<sup>13</sup> This removes impediments to and perfects the mechanism of a free and open market and national market system by encouraging more investors to participate in light of the changes

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<sup>11</sup> See supra note 3.

<sup>12</sup> See supra note 10.

<sup>13</sup> See supra note 8.

associated with the Plan. The Exchange believes that if approved on a permanent basis, the Options Pilots would permanently provide investors with the above-described additional certainty of market prices and mitigation of unanticipated consequences and unreasonable adverse selection risk during limit and straddle states.

Since the Commission's approval of Amendment 18 allowing the Plan to operate on a permanent basis, the Exchange and other national securities exchanges have determined that no further amendments should be made to the Options Pilots;<sup>14</sup> the current Options Pilots effectively address extraordinary market volatility, are reasonably designed to comply with the requirements of the Plan, facilitate compliance with the Plan and should now operate on a permanent basis, consistent with the Plan. The Exchange does not propose any substantive or additional changes to Chapter V, Section 3(d).

b. Statutory Basis

The Exchange believes the proposed rule change is consistent with the requirements of Section 6(b) of the Act,<sup>15</sup> in general, and Section 6(b)(5) of the Act,<sup>16</sup> in particular, in that it is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest and not to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes that the proposed rule supports the objectives

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<sup>14</sup> See Securities Exchange Act Release No. 85622 (April 11, 2019), 84 FR 16116 (April 17, 2019) (SR-BX-2019-007).

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

<sup>16</sup> 15 U.S.C. 78f(b)(5).

of perfecting the mechanism of a free and open market and the national market system because it promotes transparency and uniformity across markets concerning rules for options markets adopted to coincide with the Plan. The Exchange believes that eliminating the pilot basis for the Options Pilots and making such rules permanent facilitates compliance with the Plan by adding certainty to the markets during periods of market volatility, which has been approved and found by the Commission to be reasonably designed to prevent potentially harmful price volatility in NMS Stocks. It has been determined by the Commission that the Plan benefits markets and market participants by helping to ensure orderly markets, and, based on the data made available to the public and the Commission during the pilot period for Chapter V, Section 3(d)(iv), the Plan does not negatively impact options market quality during normal market conditions. Rather, the Plan, as it is implemented under the obvious error pilot, functions to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets. During a limit or straddle state, determining theoretical value of an option may be a subjective rather than an objective determination given the lack of a reliable NBBO, which may create an unreasonable adverse selection opportunity and discourage participants from providing liquidity during limit and straddle states. Therefore, the Exchange believes eliminating obvious error review in such states would, in turn, eliminate uncertainty and confusion for investors and benefit investors by encouraging more participation in light of the changes associated with the Plan. As stated, the Exchange believes the other Options Pilots rules provide additional measures designed to protect investors during limit and straddle states. For example, the Exchange will reject Market Orders during a Limit Up-Limit Down state to ensure that only those

orders with a limit price will be executed during a limit or straddle state given the uncertainty of market prices during such a state.<sup>17</sup> Accordingly, the Exchange believes that making the Options Pilots permanent will further the goals of investor protection and fair and orderly markets as the rules effectively address extraordinary market volatility pursuant to the Plan.

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

The Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is necessary to reflect that the Plan no longer operates as a pilot and has been approved to operate on a permanent basis by the Commission. As such, Chapter V, Section 3(d), which implement protections in connection with the Plan, should be amended to operate on a permanent basis. The Exchange understands that the other national securities exchanges will also file similar proposals to make permanent their respective pilot programs.<sup>18</sup> Thus, the proposed rule change will help to ensure consistency across market centers without implicating any competitive issues.

5. 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.

6. Extension of Time Period for Commission Action

Not applicable.

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<sup>17</sup> See supra note 8.

<sup>18</sup> In addition, the Exchange's proposal is substantially similar to Cboe's recently approved rule change. See supra note 4.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(iii)<sup>19</sup> of the Act and Rule 19b-4(f)(6) thereunder<sup>20</sup> in that it effects a change that: (i) does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) by its terms, does not become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest.

The proposed rule change would not significantly affect the protection of investors or the public interest because it seeks to adopt the protections provided by the Options Pilots, without any changes, on a permanent basis. This proposed rule change would also not impose any significant burden on competition because the Exchange understands that the other national securities exchanges will also file similar proposals with the Commission to make permanent their respective pilot programs.<sup>21</sup> Accordingly, the Exchange has designated this rule filing as non-controversial under Section 19(b)(3)(A) of the Act<sup>22</sup> and paragraph (f)(6) of Rule 19b-4 thereunder.<sup>23</sup>

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<sup>19</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>20</sup> 17 CFR 240.19b-4(f)(6).

<sup>21</sup> In addition, the Exchange's proposal is substantially similar to Cboe's recently approved rule change. See supra note 4.

<sup>22</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>23</sup> 17 CFR 240.19b-4.

The Exchange respectfully requests that the Commission waive the 30-day operative delay so that the proposed rule change may become effective and operative upon filing with the Commission pursuant to Section 19(b)(3)(A) of the Act<sup>24</sup> and paragraph (f)(6) of Rule 19b-4 thereunder.<sup>25</sup> Waiver of the 30-day operative delay would allow the Exchange to immediately adopt the Options Pilots on a permanent basis before the pilot expires on October 18, 2019. Waiver of the operative delay is consistent with the protection of investors and the public interest because it seeks to make permanent the protections provided by the Options Pilot, without any changes.

At any time within sixty (60) days of the filing of such proposed rule change, the Commission may summarily temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

The proposed rule change is based on SR-CBOE-2019-049.<sup>26</sup>

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

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<sup>24</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>25</sup> 17 CFR 240.19b-4(f)(6).

<sup>26</sup> See supra note 4.

11. Exhibits

1. Notice of Proposed Rule Change for publication in the Federal Register.
5. Text of the proposed rule change.

**EXHIBIT 1**

SECURITIES AND EXCHANGE COMMISSION  
(Release No. \_\_\_\_\_ ; File No. SR-BX-2019-038)

October \_\_, 2019

Self-Regulatory Organizations; Nasdaq BX, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to make certain options market rules permanent

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 October 18, 2019, 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, II, and III, 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 make permanent certain options market rules that are linked to the equity market Plan to Address Extraordinary Market Volatility.

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

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

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



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

The purpose of the proposed rule change is to make permanent certain options market rules in connection with the equity market Plan to Address Extraordinary Market Volatility (the "Limit Up-Limit Down Plan" or the "Plan"). This change is being proposed in connection with the recently approved amendment to the Limit Up-Limit Down Plan that allows the Plan to continue to operate on a permanent basis ("Amendment 18").<sup>3</sup> This proposed rule change is substantially similar to a recently-approved rule change by Cboe Exchange, Inc. ("Cboe").<sup>4</sup>

In an attempt to address extraordinary market volatility in NMS Stocks, and, in particular, events like the severe volatility on May 6, 2010, U.S. national securities exchanges and the Financial Industry Regulatory Authority, Inc. (collectively, "Participants") drafted the Plan pursuant to Rule 608 of Regulation NMS and under the

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<sup>3</sup> See Securities Exchange Act Release No. 85623 (April 11, 2019), 84 FR 16086 (April 17, 2019) (Order Approving Amendment No. 18).

<sup>4</sup> See Securities Exchange Act Release Nos. 86744 (August 23, 2019), 84 FR 45565 (August 29, 2019) (SR-CBOE-2019-049) (Notice of Filing); and 87311 (October 15, 2019) (SR-CBOE-2019-049) (Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment Nos. 1 and 2). The Exchange understands that the other national securities exchanges will also file similar proposals to make permanent their respective pilot programs.

Act.<sup>5</sup> On May 31, 2012, the Commission approved the Plan, as amended, on a one-year pilot basis.<sup>6</sup> Though the Plan was primarily designed for equity markets, the Exchange believed it would, indirectly, potentially impact the options markets as well. Thus, the Exchange has previously adopted and amended Chapter V, Section 3(d) to ensure the option markets were not harmed as a result of the Plan's implementation and has implemented such rules on a pilot basis that has coincided with the pilot period for the Plan (the "Options Pilots").<sup>7</sup> Chapter V, Section 3(d) addresses the interplay of the Exchange's rules in response to the Plan, and includes provisions on how the Exchange will treat certain options orders during a limit or straddle state as well as options market maker quoting obligations during a limit or straddle state. In addition, Section 3(d)(iv) provides that during a limit or straddle state, trades are not subject to obvious or catastrophic error review. A limit or straddle state occurs when at least one side of the National Best Bid ("NBB") or Offer ("NBO") bid/ask is priced at a non-tradable level. Specifically, a straddle state exists when the NBB is below the lower price band while the NBO is inside the prices band or when the NBO is above the upper price band and the NBB is within the band, while a limit state occurs when the NBO equals the lower price band (without crossing the NBB), or the NBB equals the upper price band (without crossing the NBO). The Exchange adopted the

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<sup>5</sup> See Securities Exchange Act Release No. 64547 (May 25, 2011), 76 FR 31647 (June 1, 2011) (File No. 4-631).

<sup>6</sup> See Securities and Exchange Act Release No. 67091 (May 31, 2012) 77 FR 33498 (June 6, 2012).

<sup>7</sup> See Securities Exchange Act Release Nos. 69119 (March 12, 2013), 78 FR 16746 (March 18, 2013) (SR-BX-2013-021); 69334 (April 5, 2013), 78 FR 21653 (April 11, 2013) (SR-BX-2013-022); and 69343 (April 8, 2013), [78](#) FR 21982 (April 12, 2013) (SR-BX-2013-026).

Options Pilots to protect investors because when an underlying security is in a limit up-limit down state, there will not be a reliable price for the security to serve as a benchmark for the price of the option. Specifically, the Exchange adopted Chapter V, Section 3(d)(iv) because the application of the obvious and catastrophic error rules would be impracticable given the potential for lack of a reliable NBBO in the options market during limit and straddle states. When adjusting or busting a trade pursuant to the obvious error rule, the determination of theoretical value of a trade generally references the NBB (for erroneous sell transactions) or NBO (for erroneous buy transactions) just prior to the trade in question, and is therefore not reliable when at least one side of the NBBO is priced at a non-tradeable level, as is the case in limit and straddle states. In such a situation, determining theoretical value may often times be a very subjective rather than an objective determination and could give rise to additional uncertainty and confusion for investors. As a result, application of the obvious and catastrophic error rules would be impracticable given the lack of a reliable NBBO in the options market during limit and straddle states, and may produce undesirable effects or unanticipated consequences. As noted above, the Exchange adopted additional measures via other Options Pilot rules that are designed to protect investors during limit and straddle states.<sup>8</sup> For example, the Exchange will reject Market Orders (as defined in Chapter VI, Section 1) during a Limit Up-Limit Down state to ensure that only those orders with a limit price will be executed during a limit or straddle state given the uncertainty of market prices during such a state. Furthermore, the Exchange believes that eliminating the application of obvious error rules during a limit or straddle state eliminates the re-evaluation of a

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<sup>8</sup> As set forth in Chapter V, Section 3(d), this includes rules in connection with special handling for Market Orders, and options market maker quoting obligations during a limit or straddle state.

transaction executed during such a state that could potentially create an unreasonable adverse selection opportunity due to the lack of a reliable reference price on one side of the market or another and discourage participants from providing liquidity during limit and straddle states, which is contrary to the goal in limiting participants' adverse selection with the application of the obvious error rule during normal trading states. For these reasons, the Exchange believes the Options Pilots and related rules are designed to add certainty on the options markets, which encourages more investors to participate in light of the changes associated with the Plan. The Plan was originally implemented on a pilot-basis in order to allow the public, the participating exchanges, and the Commission to assess the operation of the Plan and whether the Plan should be modified prior to approval on a permanent basis. As stated, the Exchange adopted the Option Pilots to coincide with this pilot; to continue the protections therein while the industry gains further experience operating the Plan.

In connection with the order approving the establishment of the obvious error pilot, as well as the extensions of the obvious error pilot, the Exchange committed to submit monthly data regarding the program and to submit an overall analysis of the obvious error pilot in conjunction with the data submitted under the Plan and any other data as requested by the Commission. Pursuant to a rule filing, approved on April 8, 2014, each month, the Exchange committed to provide the Commission, and the public, a dataset containing the data for each straddle and limit state in optionable stocks that had at least one trade on the Exchange.<sup>9</sup> The Exchange has continued to provide the Commission with this data on a monthly basis. For each trade on the Exchange, the

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<sup>9</sup> See Securities Exchange Act Release No. 71900 (April 8, 2014), 79 FR 20951 (April 14, 2014) (SR-BX-2014-017); see also BX LULD Reports, available at: <https://www.nasdaq.com/solutions/options/LULD>.

Exchange provides (a) the stock symbol, option symbol, time at the start of the straddle or limit state, an indicator for whether it is a straddle or limit state, and (b) for the trades on the Exchange, the executed volume, time-weighted quoted bid-ask spread, time-weighted average quoted depth at the bid, time-weighted average quoted depth at the offer, high execution price, low execution price, number of trades for which a request for review for error was received during straddle and limit states, an indicator variable for whether those options outlined above have a price change exceeding 30% during the underlying stock's limit or straddle state compared to the last available option price as reported by OPRA before the start of the limit or straddle state. In addition, to help evaluate the impact of the pilot program, the Exchange has provided to the Commission, and the public, assessments relating to the impact of the operation of the obvious error rules during limit and straddle states including: (1) an evaluation of the statistical and economic impact of limit and straddle states on liquidity and market quality in the options markets, and (2) an assessment of whether the lack of obvious error rules in effect during the straddle and limit states are problematic. The Exchange has concluded that the Options Pilots do not negatively impact market quality during normal market conditions,<sup>10</sup> and that there has been insufficient data to assess whether a lack of obvious error rules is problematic, however, the Exchange believes the continuation of the Options Pilots function to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets.

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<sup>10</sup> See also BX LULD Reports, available at: <https://www.nasdaq.com/solutions/options/LULD>. During the most recent Review Period the Exchange did not receive any obvious error review requests for Limit-Up-Limit Down trades, and Limit Up-Limit Down trade volume accounted for nominal overall trade volume.

The Commission recently approved the Plan on a permanent basis (Amendment 18).<sup>11</sup> In connection with this approval, the Exchange now proposes to amend Chapter V, Section 3(d) that currently implement provisions of the Plan on a pilot basis to eliminate the pilot basis, which effectiveness expires on October 18, 2019, and to make such rules permanent. In its approval order to make the Plan permanent, the Commission recognized that, as a result of the Participants' and industry analysis of the Plan's operation, the Limit Up-Limit Down mechanism effectively addresses extraordinary market volatility. Indeed, the Plan benefits markets and market participants by helping to ensure orderly markets, but also, the Exchange believes, based on the data made available to the public and the Commission during the pilot period, that the obvious error pilot does not negatively impact market quality during normal market conditions.<sup>12</sup> Rather, the Exchange believes the obvious error pilot functions to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets. The Exchange also believes the other Options Pilots rules provide additional measures designed to protect investors during limit and straddle states. For example, the Exchange will reject Market Orders during a Limit Up-Limit Down state to ensure that only those orders with a limit price will be executed during a limit or straddle state given the uncertainty of market prices during such a state.<sup>13</sup> This removes impediments to and perfects the mechanism of a free and open market and national market system by encouraging more investors to participate in light of the changes

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<sup>11</sup> See supra note 3.

<sup>12</sup> See supra note 10.

<sup>13</sup> See supra note 8.

associated with the Plan. The Exchange believes that if approved on a permanent basis, the Options Pilots would permanently provide investors with the above-described additional certainty of market prices and mitigation of unanticipated consequences and unreasonable adverse selection risk during limit and straddle states.

Since the Commission's approval of Amendment 18 allowing the Plan to operate on a permanent basis, the Exchange and other national securities exchanges have determined that no further amendments should be made to the Options Pilots;<sup>14</sup> the current Options Pilots effectively address extraordinary market volatility, are reasonably designed to comply with the requirements of the Plan, facilitate compliance with the Plan and should now operate on a permanent basis, consistent with the Plan. The Exchange does not propose any substantive or additional changes to Chapter V, Section 3(d).

## 2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the requirements of Section 6(b) of the Act,<sup>15</sup> in general, and Section 6(b)(5) of the Act,<sup>16</sup> in particular, in that it is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest and not to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes that the proposed rule supports the objectives of perfecting the mechanism of a free and open market and the national market system

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<sup>14</sup> See Securities Exchange Act Release No. 85622 (April 11, 2019), 84 FR 16116 (April 17, 2019) (SR-BX-2019-007).

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

<sup>16</sup> 15 U.S.C. 78f(b)(5).

because it promotes transparency and uniformity across markets concerning rules for options markets adopted to coincide with the Plan. The Exchange believes that eliminating the pilot basis for the Options Pilots and making such rules permanent facilitates compliance with the Plan by adding certainty to the markets during periods of market volatility, which has been approved and found by the Commission to be reasonably designed to prevent potentially harmful price volatility in NMS Stocks. It has been determined by the Commission that the Plan benefits markets and market participants by helping to ensure orderly markets, and, based on the data made available to the public and the Commission during the pilot period for Chapter V, Section 3(d)(iv), the Plan does not negatively impact options market quality during normal market conditions. Rather, the Plan, as it is implemented under the obvious error pilot, functions to protect against any unanticipated consequences in the options markets during a limit or straddle state and add certainty on the options markets. During a limit or straddle state, determining theoretical value of an option may be a subjective rather than an objective determination given the lack of a reliable NBBO, which may create an unreasonable adverse selection opportunity and discourage participants from providing liquidity during limit and straddle states. Therefore, the Exchange believes eliminating obvious error review in such states would, in turn, eliminate uncertainty and confusion for investors and benefit investors by encouraging more participation in light of the changes associated with the Plan. As stated, the Exchange believes the other Options Pilots rules provide additional measures designed to protect investors during limit and straddle states. For example, the Exchange will reject Market Orders during a Limit Up-Limit Down state to ensure that only those orders with a limit price will be executed during a limit or straddle state given the



uncertainty of market prices during such a state.<sup>17</sup> Accordingly, the Exchange believes that making the Options Pilots permanent will further the goals of investor protection and fair and orderly markets as the rules effectively address extraordinary market volatility pursuant to the Plan.

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

The Exchange does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is necessary to reflect that the Plan no longer operates as a pilot and has been approved to operate on a permanent basis by the Commission. As such, Chapter V, Section 3(d), which implement protections in connection with the Plan, should be amended to operate on a permanent basis. The Exchange understands that the other national securities exchanges will also file similar proposals to make permanent their respective pilot programs.<sup>18</sup> Thus, the proposed rule change will help to ensure consistency across market centers without implicating any competitive issues.

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

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<sup>17</sup> See supra note 8.

<sup>18</sup> In addition, the Exchange's proposal is substantially similar to Cboe's recently approved rule change. See supra note 4.

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)(iii) of the Act<sup>19</sup> and subparagraph (f)(6) of Rule 19b-4 thereunder.<sup>20</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 necessary or appropriate in the public interest, for the protection of investors, or 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 Number SR- BX- 2019-038 on the subject line.

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<sup>19</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>20</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file 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.

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-2019-038. 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>).

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; 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- BX-2019-038 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.<sup>21</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>21</sup> 17 CFR 200.30-3(a)(12).

**EXHIBIT 5**

Proposed new language is underlined; proposed deletions are in [brackets].

**Rules of Nasdaq BX**

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**Chapter V Regulation of Trading on BX Options**

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**Sec. 3 Trading Halts**

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(d) [This paragraph shall be in effect during a pilot period that expires at the close of business on October 18, 2019.] Capitalized terms used in this paragraph shall have the same meaning as provided for in the Plan to Address Extraordinary Market Volatility Pursuant to Rule 608 of Regulation NMS, as it may be amended from time to time (“LULD Plan”). During a Limit State and Straddle State in the Underlying NMS stock:

(i) – (iii) No change.

(iv) [For a pilot period that expires at the close of business on October 18, 2019, t]Trades are not subject to an obvious error or catastrophic error review pursuant to Chapter V, Sections 6(c) or (d). Nothing in this provision shall prevent trades from review on Exchange motion pursuant to Chapter V, Section 6(c)(3), or subject to nullification or adjustment pursuant to Chapter V, Section 6(e) - (j).

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