NASDAQ OMX

Joan Conley
SENIOR VICE PRESIDENT & CORPORATE SECRETARY
9600 BLACKWELL ROAD
ROCKVILLE, MD 20850

P: (301) 978-8435
F: (301) 978-8472
E: joan.conley@nasdaqomx.com

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Ms. Elizabeth M. Murphy
Secretary
US Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: NYSE Amex LLC Proposal to Establish Equity Incentive Plan (Release No. 34-64144; File No. SR-NYSEAmex-2011-18)

Dear Ms. Murphy:

The NASDAQ OMX Group, Inc. ("NASDAQ") appreciates the opportunity to comment on the proposal by NYSE Amex LLC ("NYSE Amex") to form a joint venture with seven pre-selected member firms that would result in these firms collectively acquiring a majority ownership interest in NYSE Amex's options business. As proposed in this equity incentive plan ("Incentive Plan"), the economic interest of each member firm at a given time would correlate to the options order flow provided by that firm to NYSE Amex during the preceding measurement period. The proposal does not disclose the thresholds the firms must meet, the economic benefit to firms—or even why these particular firms were selected. NYSE Amex's Incentive Plan is virtually indistinguishable in purpose and effect from other fee or rebate-based incentive plans operated by national securities exchanges.[1]

NYSE Amex publicly announced the Incentive Plan with the pre-selected firms in 2009. We understand that NYSE Amex has been working with the Commission since then on this plan and therefore assume that the Incentive Plan reflects the Commission's current thinking on rebates and order flow incentive plans. If so, we applaud the Commission for recognizing that exchanges should be free to experiment with creative pricing models to attract liquidity and remain competitive. Rather than micromanaging how economic incentives are allocated among exchange members, the Commission is allowing NYSE Amex to make reasonable distinctions among market participants and to pre-select the firms that will be rewarded for order flow. However, this flexibility cannot be confined to one form of incentive plan. Fairness dictates that

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1 See, e.g., NASDAQ's Investor Support Plan that allows members to receive rebates based on the amount of targeted retail and institutional order flow sent by such members to NASDAQ. Rule 7014.

similar rules should apply to similar activities. Therefore, we believe that comparable flexibility must be extended to other fee and rebate-based plans.

<u>NYSE Amex Incentive Plan</u>

Although several material terms of the Incentive Plan have been redacted in the rule filing, we understand the plan to be as follows:

- Seven member firms were pre-selected in 2009 to participate in the plan, but no other NYSE Amex members are entitled to participate;

- The participating firms would own 52.8% of the common interests of NYSE Amex Options LLC ("LLC"), a facility of NYSE Amex, with NYSE Amex retaining the remaining common and preferred interests;

- The interests of the participating firms are reallocated periodically among themselves based on order flow (with no impact on NYSE Amex's ownership interest);

- Participating firms have received or will receive credit for order flow extending back to October 2009;

- Participating firms that do not meet volume targets will be diluted and may be forced to divest their interests;

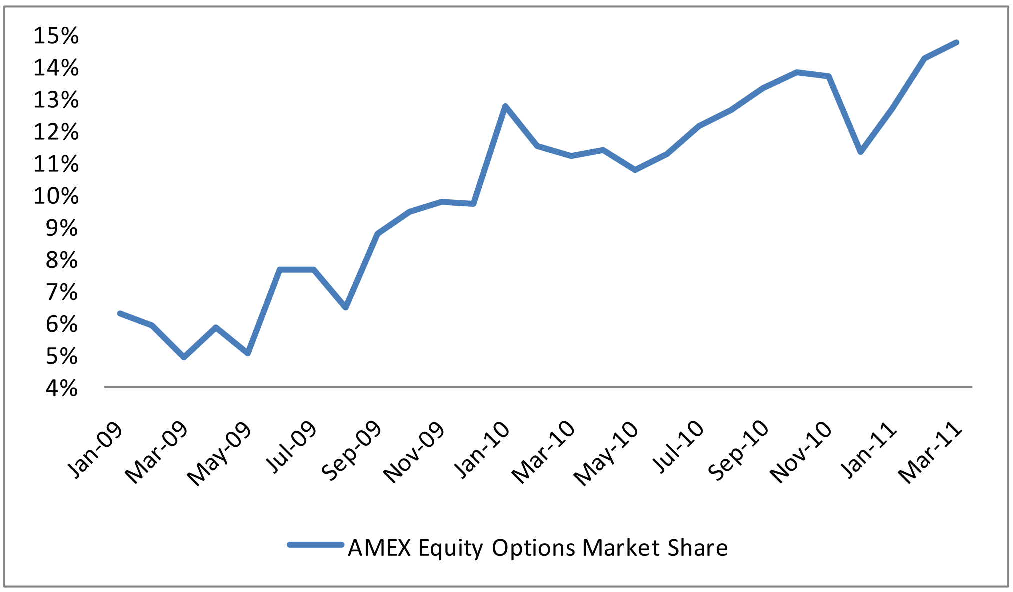
- Each year the LLC will distribute the company's "available cash" to NYSE Amex and the participating firms based on the allocation of interests among the firms at the time of distribution; and

- Participating firms have a "put right" to require NYSE Amex to repurchase a percentage of their interest in the LLC each year at what appears to be a pre-negotiated price or favorable valuation.

<u>NYSE Amex's Incentive Plan is functionally equivalent to an exchange rebate or fee-based incentive plan</u>

There can be no doubt that the Incentive Plan will operate like a traditional rebate for the firms pre-selected for the program. The economic value to the firms is directly related to how much order flow they send NYSE Amex and, as far as we can tell from the redacted filing, the order volume thresholds are the sole determinant of how the interests are reallocated after each volume measurement period. Moreover, the put right reduces the economic risk to the firms of owning the interests.

Certainly the creation of the Incentive Plan has had the same effect as a rebate plan or other fee-based incentive plan on NYSE Amex's share of options trading. As shown in the chart below, NYSE Amex's market share has increased in direct relation to the milestones in the Incentive Plan. The filing indicates that NYSE Amex's board approved the plan in July 2009 and we assume that there were preliminary discussions with firms prior to board approval. The initial volume measurement period began in October 2009 and the exchange finally filed this proposal with the SEC at the end of March 2011. NYSE Amex's options volume, which had languished near 6% since early 2007, began climbing in the early summer of 2009 and is now routinely above 15%. All indications suggest that this increase is predominantly attributable to the Incentive Plan.



Source: Options Clearing Corporation

The Commission must apply the same standards to all rebate and fee-based incentive plans

NASDAQ does not object to NYSE Amex's proposal, which seems reasonably designed to incentivize order flow and enhance the competitiveness of its market. Market participants benefit in reduced costs and improved liquidity when the Commission allows genuine competition among exchanges. However, the Commission must apply the same principles to all fee and rebate plans. The Commission traditionally has been reluctant to endorse differential pricing for exchanges even though Section 6(b)(4) of the Securities Exchange Act of 1934 (the "Act") focuses on "equitable" allocation of fees—not identical fees— among members and Section 6(b)(5) of the Act prohibits "unfair discrimination"—not any differentiation—between customers. [2] As a result, the Commission has required in the past that fees and rebates be open to all members and that transparent thresholds provide equal fees and rebates to all members that

[2] See 15 U.S.C. 78f(b)(4) and 15 U.S.C. 78f(b)(5).

meet the thresholds. The NYSE Amex proposal is a departure from this interpretation of the statutory requirements.

We credit the Commission with recognizing that greater flexibility in fee incentives and rebates is needed. This flexibility should not be limited to those exchanges that use an equity or equity-like instrument as part of a rebate or incentive program. Indeed, such a limitation would create a perverse incentive for exchanges. The ownership of self regulatory organizations by their members can raise at least the appearance of a conflict of interest. [3] If the Commission's endorsement of flexibility were to be limited to equity incentive plans and exclude other economically similar approaches it would penalize exchanges that chose not to risk this appearance of conflict. Such exchanges would struggle using more rigid and less targeted rebate programs to compete with exchanges that sold off interests to member firms. [4] The steep rise in NYSE Amex's market share illustrates this outcome. The best result is not to restrain NYSE Amex, but to allow others to compete by applying the same flexibility proposed in the Incentive Plan to all fee and rebate-based plans. Investors will be the ultimate beneficiaries of the greater competition that will result.

Respectfully submitted,

Joan C. Conley

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cc: The Hon. Mary L. Schapiro, Chairman
The Hon. Kathleen L. Casey, Commissioner
The Hon. Elisse B. Walter, Commissioner
The Hon. Luis A. Aguilar, Commissioner
The Hon. Troy A. Paredes, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
James A. Brigagliano, Deputy Director, Division of Trading and Markets
David Shillman, Associate Director, Division of Trading and Markets

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3 This risk was addressed by Congress with respect to clearing agencies, execution facilities and exchanges that clear or execute security-based swaps. See Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, Section 765(a). NYSE Amex's proposal includes several provisions attempting to deal with this issue.

4 Similarly, it could be argued that member firms are more likely to share traditional cash rebates with investors than they are likely to share rebates that are labeled "return on investment."