

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-64696; File No. SR-NASDAQ-2011-083)

June 17, 2011

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Adopt Anti-Internalization Functionality For Registered Market Makers On The NASDAQ Options Market

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 June 14, 2011, The NASDAQ Stock Market LLC (the “Exchange” or “NASDAQ”) filed with the Securities and Exchange Commission (“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 is filing this proposed rule change to adopt anti-internalization functionality for registered market makers on the NASDAQ Options Market. NASDAQ proposes to implement the rule change thirty days after the date of filing or as soon thereafter as practicable. The text of the proposed rule change is available at <http://nasdaq.cchwallstreet.com/>, at NASDAQ’s principal office, and at the Commission’s Public Reference Room.

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

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

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

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

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

1. Purpose

NASDAQ is proposing to provide anti-internalization ("AIQ") functionality to registered market makers on the NASDAQ Options Market. Under the proposal, quotes and orders entered by market makers using the same market participant identifier ("MPID") will automatically be prevented from interacting with each other in the System. Rather than executing quotes or orders from the same MPID, the System will instead cancel the oldest of the quotes and orders back to the entering party.

Anti-internalization functionality was requested by market makers or those considering making markets on NOM. Anti-internalization processing is available only to market makers and only on an individual MPID basis. Registered market makers that conduct order entry business via alternative MPIDs will not be afforded the protection of AIQ functionality with respect to such alternative MPIDs. NASDAQ considered making AIQ functionality available to

other participants, but rejected that approach due to lack of interest and to maintain simplicity of system processing.<sup>3</sup>

Anti-internalization functionality is widely available and has been for many years.<sup>4</sup> It is designed to assist market participants in complying with certain rules and regulations of the Employee Retirement Income Security Act (“ERISA”) that preclude and/or limit managing broker-dealers of such accounts from trading as principal with orders generated for those accounts. It can also assist market makers in reducing trading costs from unwanted executions potentially resulting from the interaction of executable buy and sell trading interest from the same firm when performing the same market making function.

NASDAQ notes that use of the functionality does not relieve or otherwise modify the duty of best execution owed to orders received from public customers. Options market makers generally do not display customer orders in market making quotations, opting instead to enter customer orders using separate identifiers. In the event that an options market maker opts to include a customer order within a market making quotation, the market maker must take appropriate steps to ensure that public customer orders that do not execute due to anti-internalization functionality ultimately receive the same execution price (or better) they would have originally obtained if execution of the order was not inhibited by the functionality.

## 2. Statutory Basis

NASDAQ believes that the proposed rule change is consistent with the provisions of

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<sup>3</sup> If demand should arise from other participants, NASDAQ will reconsider providing this functionality to all participants at that time.

<sup>4</sup> See, e.g., NASDAQ Rule 4757(a)(4), NYSE Arca Equities Rule 7.31(qq)(2), and BATS Rule 11.9(f)(2).

Section 6 of the Act,<sup>5</sup> in general, and with Sections 6(b)(5) of the Act,<sup>6</sup> in particular, in that the proposal is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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 proposed rule change is consistent with this provision in that it assists market makers in performing their quotation obligations, and prevents market makers from violating applicable provisions of ERISA. Market makers remain able to utilize alternative MPIDs without the use of AIQ functionality.

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

NASDAQ does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days after the date of the filing, or such shorter time as the

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<sup>5</sup> 15 U.S.C. 78f.

<sup>6</sup> 15 U.S.C. 78f(b)(5).

Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>7</sup> and Rule 19b-4(f)(6) thereunder.<sup>8</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-NASDAQ-2011-083 on the subject line.

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<sup>7</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>8</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 Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASDAQ-2011-083. 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 website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the

Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASDAQ-2011-083 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>9</sup>

Cathy H. Ahn  
Deputy Secretary

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<sup>9</sup> 17 CFR 200.30-3(a)(12).