

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-65554; File No. SR-NASDAQ-2011-142)

October 13, 2011

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Accept Inbound Orders Routed From Its Affiliates

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 6, 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 and II below, which Items have been prepared by NASDAQ. 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

NASDAQ is filing with the Securities and Exchange Commission (“Commission”) a proposed rule change to accept inbound orders routed by Nasdaq Execution Services LLC (“NES”) from both the NASDAQ OMX PSX facility (“PSX”) of NASDAQ OMX PHLX (“PHLX”) as well as from the NASDAQ OMX BX Equities Market of NASDAQ OMX BX, Inc. (“BX”), as described further below, on a one year pilot basis.

The text of the proposed rule change is available at [nasdaq.cchwallstreet.com](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, NASDAQ 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. NASDAQ 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

NES provides all routing functions for The NASDAQ Stock Market ("NASDAQ") as well as, pursuant to recent proposed rule changes, for BX and PHLX.<sup>3</sup> Accordingly, NASDAQ now proposes that NES be permitted to route orders from BX and PSX to the Exchange on a one year pilot basis.

NES is a broker-dealer and member of NASDAQ, PHLX and BX. BX, NASDAQ, PHLX and NES are affiliates. This raises the issue of an exchange's affiliation with a member of such exchange. Specifically, in connection with prior filings, the Commission has expressed concern that the affiliation of an exchange with one of its members raises the potential for unfair competitive advantage and potential conflicts of interest between an exchange's self-regulatory obligations and its commercial interests.<sup>4</sup>

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<sup>3</sup> See Securities Exchange Act Release Nos. 65470 (October 3, 2011) (SR-BX-2011-048); and 65469 (October 3, 2011) (SR-Phlx-2011-108).

<sup>4</sup> See Securities Exchange Act Release Nos. 59153 (December 23, 2008), 73 FR 80485 (SR-NASDAQ-2008-098); and 62736 (August 17, 2010), 75 FR 51861 (August 23, 2010) (SR-NASDAQ-2010-100).

Recognizing that the Commission has previously expressed concern regarding the potential for conflicts of interest in instances where a member firm is affiliated with an exchange of which it is a member, the Exchange previously proposed, and the Commission approved, limitations and conditions on NES's affiliation with the NASDAQ.<sup>5</sup> The Commission has also expressed concern regarding the potential for conflicts of interest in instances where a member firm is affiliated with an exchange to which it is routing orders.<sup>6</sup> To address the Commission's concerns, NASDAQ proposes to accept inbound orders that NES routes from PHLX and BX, respectively, in its capacity as a facility of PHLX and BX, subject to certain limitations and conditions:

- First, the Exchange and the Financial Industry Regulatory Authority (“FINRA”) will maintain a Regulatory Contract, as well as an agreement pursuant to Rule 17d–2 under the Act (“17d–2 Agreement”).<sup>7</sup> Pursuant to the Regulatory Contract and the 17d–2 Agreement, FINRA will be allocated regulatory responsibilities to review NES's compliance with certain Exchange rules.<sup>8</sup> Pursuant to the Regulatory Contract, however, NASDAQ retains ultimate responsibility for enforcing its rules with respect to NES.
- Second, FINRA will monitor NES for compliance with the Exchange's trading rules, and will collect and maintain certain related information.<sup>9</sup>

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<sup>5</sup> Id.

<sup>6</sup> See Securities Exchange Act Release No. 62877 (September 9, 2010), 75 FR 56633 (September 16, 2010) (SR-PHLX-2010-79).

<sup>7</sup> 17 CFR 240.17d-2.

<sup>8</sup> NES is also subject to independent oversight by FINRA, its designated examining authority, for compliance with financial responsibility requirements.

<sup>9</sup> Pursuant to the Regulatory Contract, both FINRA and the Exchange will collect and maintain all alerts, complaints, investigations and enforcement actions in which NES (in its capacity as a facility of PHLX or BX routing orders to the Exchange) is identified as a participant that has potentially violated applicable Commission or Exchange rules. The

- Third, FINRA will provide a report to the Exchange’s chief regulatory officer (“CRO”), on a quarterly basis, that: (i) Quantifies all alerts (of which FINRA is aware) that identify NES as a participant that has potentially violated Commission or Exchange rules, and (ii) lists all investigations that identify NES as a participant that has potentially violated Commission or Exchange rules.
- Fourth, the Exchange will adopt Rule 2160(c), which requires NASDAQ OMX, as the holding company owning both the Exchange and NES, to establish and maintain procedures and internal controls reasonably designed to ensure that NES does not develop or implement changes to its system, based on non-public information obtained regarding planned changes to the Exchange’s systems as a result of its affiliation with the Exchange, until such information is available generally to similarly situated Exchange members, in connection with the provision of inbound order routing to the Exchange.
- Fifth, the Exchange proposes that the routing of orders from NES to the Exchange, in NES’s capacity as a facility of PHLX as well as BX, be authorized for a pilot period of one year.

The Exchange believes that the above-listed conditions protect the independence of the Exchange’s regulatory responsibility with respect to NES, and that these mitigate the aforementioned concerns about potential conflicts of interest and unfair competitive advantage.

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Exchange and FINRA will retain these records in an easily accessible manner in order to facilitate any potential review conducted by the Commission’s Office of Compliance Inspections and Examinations.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,<sup>10</sup> in general, and with Sections 6(b)(5) of the Act,<sup>11</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, because the proposed rule change will allow the Exchange to receive inbound routes of orders from NES, acting in its capacity as a facility of PHLX or BX, in a manner consistent with prior approvals and established protections. The Exchange believes that the proposed conditions establish mechanisms that protect the independence of the Exchange's regulatory responsibility with respect to NES, as well as ensure that NES cannot use any information it may have because of its affiliation with the Exchange to its advantage.

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.

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<sup>10</sup> 15 U.S.C. 78f.

<sup>11</sup> 15 U.S.C. 78f(b)(5).

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

Because the foregoing proposed rule change does not significantly affect the protection of investors or the public interest, does not impose any significant burden on competition, and, by its terms, does not 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) of the Act<sup>12</sup> and Rule 19b-4(f)(6) thereunder.<sup>13</sup>

The Exchange has requested that the Commission waive the 30-day operative delay. The Exchange believes that the waiver of the 30-day operative delay is consistent with the protection of investors and the public interest because it would benefit users by offering more opportunities for their orders to be executed.<sup>14</sup> The Commission notes that the proposed rule change is consistent with rules of other national securities exchanges, and does not raise any new substantive issues.<sup>15</sup> For these reasons, the Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest, and designates the proposal to be operative upon filing with the Commission.<sup>16</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

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<sup>12</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>13</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of 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.

<sup>14</sup> See SR-NASDAQ-2011-142, Item 7.

<sup>15</sup> See, e.g., Securities Exchange Act Release Nos. 62901 (September 13, 2010), 75 FR 57097 (September 17, 2010) (SR-BATS-2010-024); and 64729 (June 23, 2011), 76 FR 38232 (June 29, 2011) (SR-NYSE-2011-24).

<sup>16</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### 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-2011-142 on the subject line.

##### 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-2011-142. 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-2011-142 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>17</sup>

Elizabeth M. Murphy  
Secretary

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