

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-69758; File No. SR-NASDAQ-2013-081)

June 13, 2013

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Make Changes to NASDAQ's Pricing Incentive Programs and Schedule of Fees and Credits

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup>, and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on June 3, 2013, The NASDAQ Stock Market LLC ("NASDAQ" 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 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 the Substance of the Proposed Rule Change

NASDAQ is proposing to make minor modifications to pricing incentive programs under Rule 7014 and NASDAQ's schedule of fees and credits applicable to execution and routing of orders in securities priced at \$1 or more per share under Rule 7018, and to make a conforming change to the fee schedule under Rule 7015. The changes pursuant to this proposal are effective upon filing, and the Exchange will implement the proposed rule changes on June 3, 2013.

The text of the proposed rule change is available on the Exchange's Website at <http://nasdaq.cchwallstreet.com>, at the principal office of the Exchange, 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. 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 Rule 7014 contains a number of pricing incentive programs that are designed to encourage participation in NASDAQ by members representing retail investors and to increase the extent to which members offer to provide liquidity at the national best bid and/or national best offer ("NBBO"). NASDAQ is proposing to make a minor modification to reduce the costs of the programs in a period of persistent low trading volumes without materially diminishing the incentives offered by these programs.

Under the NBBO Setter Incentive program, NASDAQ provides an enhanced liquidity provider rebate with respect to displayed liquidity-providing orders that set the NBBO or cause NASDAQ to join another trading center with a protected quotation at the NBBO. Under the Qualified Market Maker ("QMM") Program, a member may be designated as a QMM with respect to one or more of its market participant identifiers ("MPIDs") if (i) the member is not assessed any "Excess Order Fee" under Rule 7018 during the month;<sup>3</sup> and (ii) through such

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<sup>3</sup> Rule 7018(m). Last year, NASDAQ introduced an Excess Order Fee, aimed at reducing inefficient order entry practices of certain market participants that place excessive burdens on the systems of NASDAQ and its members and that may negatively impact the usefulness and life cycle cost of market data. In general, the determination of whether to impose the fee on a particular MPID is made by calculating the ratio between (i) entered

MPID the member quotes at the NBBO at least 25% of the time during regular market hours<sup>4</sup> in an average of at least 1,000 securities per day during the month.<sup>5</sup> The financial incentives received by a QMM include an NBBO Setter Incentive credit that may be higher than the NBBO Setter Incentive paid to members that do not qualify for the QMM program. Finally, under the Investor Support Program (the “ISP”), NASDAQ pays an enhanced liquidity provider credit to members for providing additional liquidity to NASDAQ and increasing the NASDAQ-traded volume of what are generally considered to be retail and institutional investor orders in exchange-traded securities. Participants in the ISP are required to designate specific NASDAQ order entry ports for use under the ISP and to meet specified criteria focused on market participation, liquidity provision, and high rates of order execution.

At present, if a member is a participant in both the QMM program and the ISP, it may receive a supplemental credit of \$0.00005, \$0.0001, or \$0.0002 per share executed for displayed liquidity-providing orders that qualify for the ISP, and an NBBO Setter Incentive credit or \$0.0002 or \$0.0005 per share executed for displayed liquidity-providing orders that set the

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orders, weighted by the distance of the order from the NBBO, and (ii) orders that execute in whole or in part. The fee is imposed on MPIDs that have an “Order Entry Ratio” of more than 100.

<sup>4</sup> Defined as 9:30 a.m. through 4:00 p.m., or such shorter period as may be designated by NASDAQ on a day when the securities markets close early (such as the day after Thanksgiving).

<sup>5</sup> A member MPID is considered to be quoting at the NBBO if it has a displayed order at either the national best bid or the national best offer or both the national best bid and offer. On a daily basis, NASDAQ will determine the number of securities in which the member satisfied the 25% NBBO requirement. To qualify for QMM designation, the MPID must meet the requirement for an average of 1,000 securities per day over the course of the month. Thus, if a member MPID satisfied the 25% NBBO requirement in 900 securities for half the days in the month, and satisfied the requirement for 1,100 securities for the other days in the month, it would meet the requirement for an average of 1,000 securities.

NBBO or allow NASDAQ to join another market at the NBBO.<sup>6</sup> Under the proposed change, NASDAQ will pay the greater of the applicable credit under the ISP or the NBBO Setter Incentive Program, but not a credit under both programs. At present, this means that the applicable credit would be paid under the NBBO Setter Incentive program, since the credits under that program equal or exceed ISP credits, but NASDAQ is adopting language to provide for the greater credit under either program, to cover the possibility that ISP credits may be increased at some point in the future. Orders receiving the NBBO Setter Incentive credit would continue to be included in calculations to determine a member's eligibility for the ISP. Thus, under the change, the ISP would continue to incentivize members representing retail and institutional investors to bring orders to NASDAQ. Moreover, to the extent that such orders enhance NASDAQ's market quality by allowing it to set or join the NBBO, the NBBO Setter Incentive credit would be paid. However, NASDAQ believes that paying both rebates would be unwarranted under these circumstances, since members representing retail or institutional orders are not in a position to influence the pricing of such orders.

In addition to the NBBO Setter Incentive credit described above, QMMs are also eligible to receive a discount on fees for ports used by the QMM for entering orders under the program. Effective April 1, 2013, NASDAQ reduced the applicable discount from (i) 25%, up to a total discount of \$10,000 per MPID per month, to (ii) the lesser of the QMM's total fees for such ports or \$5,000.<sup>7</sup> The change is reflected in the text of Rule 7014. However, NASDAQ did not make a conforming change to the text of Rule 7015, and is proposing to do so now.

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<sup>6</sup> The ISP credit and the NBBO Setter Incentive credit are both in addition to the rebate otherwise applicable under NASDAQ's main schedule of fees and credits under Rule 7018.

<sup>7</sup> Securities Exchange Act Release No. 69376 (April 15, 2013), 78 FR 23611 (April 19, 2013) (SR-NASDAQ-2013-063).

Currently, NASDAQ pays a credit of \$0.0020 per share executed for midpoint pegged and midpoint post-only orders (“midpoint orders”) if a member provides an average daily volume of more than 5 million shares through midpoint orders during the month and the member’s average daily volume of liquidity provided through midpoint orders during the month is at least 2 million shares more than in April 2013. NASDAQ pays a credit of \$0.0017 per share executed for midpoint orders if the member provides an average daily volume of 3 million or more shares through midpoint orders during the month (but does not qualify for the \$0.0020 tier), and a credit of \$0.0015 per share executed for midpoint orders if the member provides an average daily volume of less than 3 million shares through midpoint orders during the month. NASDAQ is proposing to increase the requirement for the \$0.0017 per share executed tier to an average daily volume of 5 million or more shares through midpoint orders (but without the requirement for an increase in volume over April 2013 applicable to the \$0.0020 per share rebate). In addition, NASDAQ proposes to reduce the midpoint order rebate for members not reaching these tiers (i.e., with an average daily volume of less than 5 million shares provided through midpoint orders during the month) from \$0.0015 to \$0.0014 per share executed. The changes are intended to reduce costs during a period of persistent low trading volumes. In addition, the changes maintain NASDAQ’s established policy of encouraging use of displayed orders through rebates that are higher than those paid for non-displayed orders, but paying higher rebates for midpoint orders, which offer price improvement, than for other forms of non-displayed orders.

Finally, under both Rule 7014 and Rule 7018, various pricing tiers depend upon the extent of a member’s trading activity, expressed as a percentage of, or a ratio to, Consolidated

Volume.<sup>8</sup> For example, NASDAQ pays a rebate of \$0.00295 per share executed with respect to displayed orders that provide liquidity if a member has shares of liquidity provided in all securities through one of its Nasdaq Market Center MPIDs that represent more than 0.90% of Consolidated Volume during the month. NASDAQ has determined that it would be beneficial to members to exclude the date of the annual reconstitution of the Russell Investments Indexes (the “Russell Reconstitution”) (in 2013, June 28) from calculations of Consolidated Volume. Trades occurring on that date would be excluded from the calculation of total Consolidated Volume and from the calculation of the member’s trading activity (i.e., they would be excluded from both the numerator and the denominator of the calculation of a member’s percentage or ratio).<sup>9</sup>

Trading volumes on the date of the Russell Reconstitution are generally far in excess of volumes on other days during the month, and members that are not otherwise active on NASDAQ to a great extent often participate in the NASDAQ Closing Cross on that date. As a result, the trading activity of members that are regular daily participants in NASDAQ, expressed as a percentage of Consolidated Volume, is likely to be lower than their percentage of Consolidated Volume on other days during the month. Including the date of the Russell Reconstitution in calculations of Consolidated Volume is therefore likely to make it more difficult for members to achieve particular pricing tiers during the month. Accordingly, excluding the date of the Russell Reconstitution from these calculations will diminish the likelihood of a de facto price increase occurring because a member is not able to reach a volume percentage on that date that it reaches on other trading days during the month. Moreover, excluding the date is very unlikely to result in a price increase for any members, since a member

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<sup>8</sup> “Consolidated Volume” is the consolidated volume of shares reported to all consolidated transaction reporting plans by all exchanges and trade reporting facilities during a month.

<sup>9</sup> NASDAQ is also moving the location of the definition of Consolidated Volume in Rule 7018.

that was not, on other days during the month, trading in NASDAQ at volume levels that would allow it qualify for a particular pricing tier would be unlikely to achieve percentage volume levels on the date of the Russell Reconstitution that would increase its overall monthly percentage to the required levels, even if it was very active on that date.

## 2. Statutory Basis

NASDAQ 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)(4) and 6(b)(5) of the Act,<sup>11</sup> in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system which NASDAQ operates or controls, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

NASDAQ believes that the proposed change to provide that members participating in both the QMM program and the ISP may not receive both an ISP credit and an NBBO Setter Incentive credit with respect to the same order (but rather would receive the higher of the two credits), is reasonable because such members will continue to receive an enhanced rebate of \$0.0002 or \$0.0005 per share executed with respect to such orders. NASDAQ does not believe, however, that it is reasonable to pay an added credit with respect to ISP-qualified orders that set or join the NBBO, since a member entering retail or institutional orders is not in a position to influence their pricing. NASDAQ further believes that the change is consistent with an equitable allocation of fees because NASDAQ will continue to pay the higher of the two credits to reflect the fact that such orders improve NASDAQ's market quality by setting or allowing NASDAQ to join the NBBO. NASDAQ further believes that the change is not unfairly discriminatory

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

<sup>11</sup> 15 U.S.C. 78f(b)(4) and (5).

because the change will eliminate an instance in which members may receive credits that are high in relation to those paid to other members while still paying credits that reflect the value of applicable orders as both retail or institutional orders and orders that set or join the NBBO. Finally, the change does not unfairly burden competition because it does not disadvantage affected members in a manner that would impair their ability to compete, in that they will continue to receive enhanced rebates. The change with respect to the text of Rule 7015 is reasonable, consistent with an equitable allocation, not unfairly discriminatory, and does not burden competition, in that is designed merely to ensure that the fee language of Rule 7015 reflects a change that was made to Rule 7014 in April 2013. As such, it is not a substantive change.

The changes to increase the required threshold for a rebate of \$0.0017 per share executed for midpoint orders and to reduce the rebate for midpoint orders for members not reaching this tier from \$0.0015 to \$0.0014 per share executed are reasonable, consistent with an equitable allocation, not unfairly discriminatory, and do not burden competition. Specifically, the change in the threshold is reasonable because it provides an incentive for members that wish to receive a higher rebate to increase their levels of liquidity provision, while continuing to provide a rebate for midpoint orders, whether or not a member reaches the tier threshold, that is higher than the rebate for other non-displayed orders. The change to the threshold is consistent with an equitable allocation of fees and not unfairly discriminatory because although it will affect only a small number of market participants, it is designed to incentivize all market participants that use midpoint orders to increase their volumes of liquidity provision in order to achieve a higher rebate for such orders, or, in the alternative, to increase use of displayed orders to receive a still higher rebate. Thus, the change is consistent with NASDAQ's longstanding policy of



encouraging the use of displayed orders, which promote price discovery, while nevertheless favoring midpoint orders over other non-displayed orders due to the price improvement they offer. The change does not burden competition since affected members may readily adjust trading behavior to maintain or increase their rebates, and will therefore not be disadvantaged in their ability to compete.

The change in the applicable rebate for midpoint orders to which a pricing tier does not apply is reasonable because it reflects a reduction of only \$0.0001 to the applicable rebate. The change is consistent with an equitable allocation of fees and not unfairly discriminatory because it provides further incentives for members to increase their volume of liquidity provision through midpoint orders and/or increase their use of displayed orders in order to earn a higher rebate. As such, the change is consistent with NASDAQ's policy of encouraging the use of displayed orders, while nevertheless favoring midpoint orders over other non-displayed orders. Moreover, the impact of the change will be spread across a large number of firms that use midpoint orders. Finally, the change does not burden competition since affected members may readily adjust trading behavior to increase rebates, or alternatively, will see only a small reduction in rebates with respect to continued use of the midpoint orders. Accordingly, affected members will not be disadvantaged in their ability to compete.

NASDAQ believes that the proposed change to exclude the date of the Russell Reconstitution from calculations of Consolidated Volume under Rules 7014 and 7018 is reasonable because it will diminish the likelihood of a de facto price increase occurring because a member is not able to reach a volume percentage on that date that it reaches on other trading days during the month. NASDAQ further believes that the change is consistent with an equitable allocation of fees and is not unfairly discriminatory. Specifically, because trading activity on the

date of the Russell Reconstitution will be excluded from determinations of a member's percentage of Consolidated Volume, NASDAQ believes it will be easier for members to determine the volume required to meet a certain percentage of participation than would otherwise be the case. To the extent that a member has been active in NASDAQ at a significant level throughout the month, excluding the date of the Russell Reconstitution, on which its percentage of Consolidated Volume is likely to be lower than on other days, will increase its overall percentage for the month. Conversely, even if a member was more active on the date of Russell Reconstitution than on other dates, it is unlikely that its activity on one day would be able to increase its overall monthly percentage to a meaningful extent. Thus, NASDAQ believes that the change will benefit members that are in a position to achieve volume levels required by the NASDAQ pricing schedule but without harming the ability of any members to reach such levels. Finally, NASDAQ believes that the change does not unfairly burden competition because it will help to preserve or improve the pricing status that would apply to members' trading activity in the absence of the Russell Reconstitution, and therefore will not impact the ability of such members to compete.

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. NASDAQ notes that it operates in a highly competitive market in which market participants can readily favor competing venues if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. In such an environment, NASDAQ must continually adjust its fees to remain competitive with other exchanges and with alternative trading systems that have been exempted from compliance with

the statutory standards applicable to exchanges. Because competitors are free to modify their own fees in response, and because market participants may readily adjust their order routing practices, NASDAQ believes that the degree to which fee changes in this market may impose any burden on competition is extremely limited. In this instance, although certain of the proposed changes have the effect of reducing certain rebates or limiting their availability, the rebates in question remain in place and are themselves reflective of the need for exchanges to offer significant financial incentives to attract order flow. Moreover, if the changes are unattractive to market participants, it is likely that NASDAQ will lose market share as a result. In addition, the change with respect to the Russell Reconstitution is designed to protect members from the possibility of a de facto price increase. As a result of all of these considerations, NASDAQ does not believe that the proposed changes will impair the ability of members or competing order execution venues to maintain their competitive standing in the financial markets.

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>12</sup> and paragraph (f) of Rule 19b-4 thereunder.<sup>13</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.

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

<sup>13</sup> 17 CFR 240.19b-4(f).

#### 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-2013-081 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-2013-081. 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 20549-1090, 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 offices of NASDAQ.

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-2013-081, 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>14</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>14</sup> 17 CFR 200.30-3(a)(12).