

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62724; File No. SR-NASDAQ-2010-099)

August 16, 2010

Self-Regulatory Organizations; Notice of Filing of a Proposed Rule Change by The NASDAQ Stock Market LLC to Adopt a Definition of Professional and Require that All Professional Orders be Appropriately Marked

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹, and Rule 19b-4² thereunder, notice is hereby given that on August 6, 2010, The NASDAQ Stock Market LLC (“NASDAQ”) filed with the Securities and Exchange Commission (“SEC” or “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 (“SEC” or “Commission”) a proposal for the NASDAQ Options Market (“NOM” or “Exchange”) to amend Chapter I, Section 1 (Definitions) to adopt a definition of “Professional” on the Exchange and require that all Professional orders be appropriately marked by Exchange Participants.

The text of the proposed rule change is available from NASDAQ’s website at <http://nasdaq.cchwallstreet.com/Filings/>, at NASDAQ’s principal office, and at the Commission’s Public Reference Room.

¹ 15 U.S.C. 78s(b)(1).

² 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

The purpose of this proposal is to amend Chapter I, Section 1 (Definitions) to adopt a definition of “Professional” on the Exchange and require that all Professional orders be appropriately marked.

This filing is similar to the recent filings of PHLX NASDAQ OMX, Inc. (“Phlx”), the International Securities Exchange, LLC (“ISE”), and Chicago Board Options Exchange, Incorporated, (“CBOE”), which dealt with establishing a new definition of “professional” as a person or entity that places a certain high volume of orders in listed options per day on average during a calendar month in his or her own beneficial account.³

³ See Securities Exchange Act Release Nos. 61802 (March 30, 2010), 75 FR 17193 (April 5, 2010)(SR-Phlx-2010-05)(approval order); 61198 (December 17, 2009), 74 FR 68880 (December 29, 2009)(SR-CBOE-2009-078) (approval order); and 59287 (January 23, 2009), 74 FR 5694 (January 30, 2009) (SR-ISE-2006-26) (approval order). A filing by NYSE Amex LLC (“NYSE Amex”) proposing a similar professional designation was based on the Phlx, ISE, and CBOE proposals. See Securities Exchange Act Release No. 61818 (March 31, 2010), 75 FR 17457 (April 6, 2010) (SR-NYSEAmex-2010-18) (approval order). Phlx, ISE, CBOE, and NYSE Amex are known in this filing as the “Professional Rule Exchanges.”

Background

A member of NOM is known as a Participant or Options Participant (“Participant”).⁴ This is a firm or organization that is registered with the Exchange pursuant to Chapter II for purposes of participating in options trading on NOM as a Nasdaq Options Order Entry Firm or Nasdaq Options Market Maker.⁵ Options traded by Participants (which may include trades on behalf of Public Customers)⁶ on NOM, a wholly electronic exchange, are electronically executable and routable. The NOM System⁷ and rules provide for the ranking, display, and execution of all orders in price/time priority without regard to the status of the person or entity entering an order.⁸ The Exchange notes that NOM has, in contrast to certain other options

The cited filings discuss, among other things, the need for a professional designation to be applied by members of the respective exchanges because the systems of such exchanges differentiate for execution or processing purposes based on order origin. NOM does not similarly differentiate among orders based on their origin.

⁴ See Chapter I, Section 1(a)(40). Some NOM Participants are also members of other options exchanges such as, for example, ISE, CBOE, or Phlx.

⁵ Nasdaq Options Order Entry Firm or Order Entry Firm or OEF is defined in Chapter I, Section 1(a)(25) as: those Options Participants representing as agent Customer Orders on NOM and those non-Market Maker Participants conducting proprietary trading. Nasdaq Options Market Maker or Options Market Maker is defined in Chapter I, Section 1(a)(26) as: an Options Participant registered with the Exchange for the purpose of making markets in options contracts traded on the Exchange and that is vested with the rights and responsibilities specified in Chapter VII of these Rules.

⁶ Public Customer is defined in Chapter I, Section 1(a)(48) as: a person that is not a broker or dealer in securities.

⁷ System is defined in Chapter IV, Section 1(a) as: the automated system for order execution and trade reporting owned and operated by The Nasdaq Options Market LLC.

⁸ See Securities Exchange Act Release No. 57478 (March 12, 2008), 73 FR 14521 (March 18, 2008) (SR-NASDAQ-2007-004 and SR- NASDAQ-2007-080) (approval order). See also Chapter VI, Section 10, which discusses the price/time execution algorithm for System orders and states, in relevant part, that the System will execute trading interest at the best price in the System before executing trading interest at the next best price, and that the System will execute displayed orders before non-displayed orders at the same price.

markets, a “flat” system that does not differentiate for execution or processing purposes among orders on the basis of who or what entity enters an order on the Exchange.⁹

NASDAQ Options Services LLC ("NOS"), a member of the Exchange,¹⁰ is the Exchange's exclusive order router for all orders that come through the Exchange.¹¹ NOS performs routing functions with respect to System Securities and Non-System Securities.¹² The Exchange's general routing procedures are set forth in Chapter VI, Section 11 (Order Routing), which states in subsection (c) that, among other things, once routed by the System, an order becomes subject to the rules and procedures of the destination market.¹³ NOS also performs order routing services on behalf of Phlx.¹⁴

⁹ In contrast to NOM, hybrid options exchanges such as, for example, Phlx and CBOE blend auction and electronic market structures that differentiate certain order priority and execution functions based upon, among other things, the origin of the order (e.g. whether the order was a customer, market maker, broker or dealer, firm, or other type of order); these exchanges also charge different fees based on order origin. NOM does, like other exchanges, differentiate fees based on order origin. For example, fees for removing liquidity in SPY options are different for customers than they are for market makers and firms. This filing does not propose any changes in respect of the NOM fee structure.

¹⁰ NOS is also a member of other options exchanges such as, for example, ISE and Phlx.

¹¹ See Securities Exchange Act Release No. 57478 (March 12, 2008), 73 FR 14521 (March 18, 2008)(SR-NASDAQ-2007-004 and SR-NASDAQ-2007-080) (approval order). See also Chapter VI, Section 11(e), which states, in relevant part: NOM shall route orders in options via Nasdaq Options Services LLC, a broker-dealer that is a member of an unaffiliated SRO which is the designated examining authority for the broker-dealer. Nasdaq Options Services LLC serves as the Routing Facility of NOM. The sole function of the Routing Facility will be to route orders in options listed and open for trading on NOM to away markets pursuant to NOM rules solely on behalf of NOM. The Routing Facility is subject to regulation as a facility of Nasdaq, including the requirement to file proposed rule changes under Section 19 of the Act.

¹² Chapter VI, Section 1(b) states: "System Securities" shall mean all options that are currently trading on NOM pursuant to Chapter IV (Securities Traded on NOM) above. All other options shall be "Non System Securities."

¹³ Chapter VI, Section 11(c) states: Priority of Routed Orders. Orders sent by the System to other markets do not retain time priority with respect to other orders in the System and

The exchanges that do the great majority of all U.S. options trading, namely the Professional Rule Exchanges CBOE, ISE, NYSE AMEX, and Phlx, already have rules that are similar to the Professional designation rule proposed by the Exchange (a professional is a person or entity that places 390 or more orders in listed options per day on average during a calendar month in his or her own beneficial account). These Professional Rule Exchanges make differentiations based on whether an order is marked professional or otherwise. Some Exchange Participants are, as noted, also members of Professional Rule Exchanges such as CBOE, ISE, or Phlx. As members of these exchanges, such Exchange Participants are subject to the professional designation rules of the Professional Rule Exchanges. Similarly, NOS is a member of several Professional Rule Exchanges. Exchange rules indicate that orders routed by NOS become subject to the rules and procedures of the destination markets (away exchanges).¹⁵

The Exchange believes that disparate rules in respect of Professional order designation, and lack of uniform application of such rules, do not promote the best regulation and may, in fact, encourage regulatory arbitrage.¹⁶ The Exchange believes that it is therefore prudent and

the System shall continue to execute other orders while routed orders are away at another market center. Once routed by the System, an order becomes subject to the rules and procedures of the destination market including, but not limited to, order cancellation. If a routed order is subsequently returned, in whole or in part, that order, or its remainder, shall receive a new time stamp reflecting the time of its return to the System.

¹⁴ NOS routes certain orders in options listed and open for trading on the Phlx electronic order, trading and execution system (known as XL II) to away market centers. See Phlx Rule 1080(m)(iii)(A) and Securities Exchange Act Release No. 59995 (May 28, 2009), 74 FR 26750 (June 3, 2009) (SR-Phlx-2009-32) (approval order).

¹⁵ Once routed by the System, an order becomes subject to the rules and procedures of the destination market including, but not limited to, order cancellation. See Chapter VI, Section 11(c).

¹⁶ The Exchange believes that the risk of regulatory arbitrage is heightened where not all exchanges have Professional designation rules; and there is a lack of uniformity regarding

necessary to have a Professional designation rule as is commonplace in the industry, particularly where NOS (like Exchange Participants) is a member of several exchanges that have rules requiring professional order designations.

The Proposal

The Exchange proposes new Chapter I, Section 1(a)(48) to state that the term “Professional” means any person or entity that (i) is not a broker or dealer in securities, and (ii) places more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s). A Participant or a Public Customer may, without limitation, be a Professional. Moreover, in order to properly represent orders entered on the Exchange according to the new definition, a Participant will be required to appropriately mark all Professional orders.¹⁷ To comply with this requirement, Participants will be required to review their Public Customers’ activity on at least a quarterly basis to determine whether orders that are not for the account of a broker-dealer should be represented as Professional orders.¹⁸ The Exchange will

Professional Rule Exchanges marking orders as Professional when routing such orders away.

¹⁷ The Exchange intends to require Participants to indentify Professional orders submitted electronically by identifying them in the customer type field, and will notify Participants via an Options Trader Alert (“OTA”) or Options Regulatory Alert (“ORA”) regarding this requirement.

¹⁸ Participants will be required to conduct a quarterly review and make any appropriate changes to the way in which they are representing orders within five business days after the end of each calendar quarter. While Participants will only be required to review their accounts on a quarterly basis, if during a quarter the Exchange identifies a customer for which orders are being represented as other than Professional orders but that has averaged more than 390 orders per day during a month, the Exchange will notify the Participant and the Participant will be required to change the manner in which it is representing the customer’s orders within five business days. This is similar to the process of other options exchanges that have adopted a professional designation. See, e.g., Securities Exchange Act Release No. 61802 (March 30, 2010), 75 FR 17193 (April 5, 2010) (SR-Phlx-2010-05) (approval order).

issue a notice to Participants via OTA or ORA outlining the procedures for the implementation of the proposal.

The Professional definition proposed by NOM is similar to the Professional designation that has been adopted by Phlx, ISE, CBOE, and NYSE Amex.¹⁹ As noted, the Professional definition will not impact the Exchange's price/time order entry (priority) system.²⁰ Instead, the Exchange's proposal will ensure that Exchange Participants mark their Professional orders properly, that is, similarly in terms of professional order identification regardless of whether the order is placed on NOM or some other Professional Order Exchange. Moreover, with the proposed Professional designation in place, the Exchange will be able to accept orders that are marked professional.²¹

The designation of Professional or Professional order would not result in any different treatment of such orders for purposes of NOM rules concerning away market protection. That is, all non broker or dealer orders, including those that meet the definition of Professional orders, would continue to be treated equally for purposes of Exchange away market protection rules.²²

¹⁹ See supra note 3.

²⁰ For example, unlike the Phlx proposal (which, among other things, discusses that Professional orders on Phlx will be treated in the same manner as off-floor brokers in terms of certain priority rules), the Exchange's proposal does not address or impact any priority relationship for Professional as opposed to other NOM orders.

²¹ Currently, NOM only accepts orders that are marked as customer, firm, market maker, or away market maker orders. Professional orders that may not now be accepted by NOM must be sent to other Exchanges. While the Exchange does not intend to differentiate among Professional and other orders for priority purposes, it may, in the future, feel that it is appropriate to differentiate its routing or other fees in respect of Professional as opposed to other orders; and if so, the Exchange intends to file an appropriate fee-related rule filing(s). The Exchange does not address its fee structure in the present filing.

²² See, e.g., Chapter VI, Section 11 and Chapter XII.

The Exchange believes that identifying Professional accounts based upon the average number of orders entered in qualified accounts is an appropriately objective approach that will reasonably distinguish such persons and entities from retail investors or market participants. The Exchange proposes the threshold of 390 orders per day on average over a calendar month, because it believes that this number far exceeds the number of orders that are entered by retail investors in a single day.²³ Moreover, the 390 orders per day threshold proposed by NOM directly corresponds to the daily order volume recognized by Phlx and other options exchanges that have, as previously discussed, established professional order designations.²⁴ In addition, basing the standard on the number of orders that are entered in listed options for a qualified account(s) assures that professional account holders cannot inappropriately avoid the purpose of

²³ 390 orders is equal to the total number of orders that a person would place in a day if that person entered one order every minute from market open to market close. Many of the largest retail-oriented electronic brokers offer lower commission rates to customers they define as “active traders.” Publicly available information from the websites of Charles Schwab, Fidelity, TD Ameritrade and OptionsXpress all define “active trader” as someone who executes only a few options trades per month. The highest required trading activity to qualify as an active trader among these four firms was 35 trades per quarter. See Securities Exchange Act Release No. 57254 at note 11 (which also notes that a study of one of the largest retail-oriented options brokerage firms indicated that on a typical trading day, options orders were entered with respect to 5,922 different customer accounts. There was only one order entered with respect to 3,765 of the 5,922 different customer accounts on this day, and there were only 17 customer accounts with respect to which more than ten orders were entered. The highest number of orders entered with respect to any one account over the course of an entire week was 27).

²⁴ The similarity of the Exchange’s proposed Professional order definition to that of other options exchanges is important from the regulatory perspective, that is from a desire to promote a national market system that minimizes regulatory arbitrage.

the rule by spreading their trading activity over multiple exchanges, and using an average number over a calendar month will prevent gaming of the 390 order threshold.²⁵

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act²⁶ in general, and furthers the objectives of Section 6(b)(5) of the Act²⁷ in particular, in that it 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 facilitating transactions in securities, and to remove impediments to and perfect the mechanisms of a free and open market and a national market system, by defining Professional and indicating that all Professional orders shall be appropriately marked by Participants.

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.

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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer

²⁵ The Exchange intends to notify Participants via OTA or ORA that this proposal will be implemented on the first trading day of the month after the approval or effectiveness of this proposal.

²⁶ 15 U.S.C. 78f(b).

²⁷ 15 U.S.C. 78f(b)(5).

period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve or disapprove the proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be 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 Exchange 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. Please include File Number SR-NASDAQ-2010-099 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-2010-099. 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 Web site 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-NASDAQ-2010-099 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.²⁸

Florence E. Harmon
Deputy Secretary

²⁸ 17 CFR 200.30-3(a)(12).