

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-68512; File No. SR-NASDAQ-2012-142)

December 21, 2012

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing of Proposed Rule Change with Respect to the Amendment of the By-Laws of its Parent Corporation, The NASDAQ OMX Group, Inc.

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 December 19, 2012, The NASDAQ Stock Market LLC (“NASDAQ” or “Exchange”) 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 proposes a rule change with respect to the amendment of the by-laws of its parent corporation, The NASDAQ OMX Group, Inc. (“NASDAQ OMX” or the “Corporation”). 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.

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

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

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

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 OMX is proposing amendments to provisions of its By-Laws pertaining to the compositional requirements of the NASDAQ OMX Board. The changes are primarily focused on amending the definition of “Industry Director” (and “Industry committee member”)<sup>3</sup> to make the definition less restrictive, but in a manner that NASDAQ believes will continue to serve the purpose of ensuring that members and member organizations of Self-Regulatory Subsidiaries<sup>4</sup> – the self-regulatory organizations owned by NASDAQ OMX – do not have disproportionate influence on its governance. In making the change, NASDAQ OMX is adapting concepts already approved by the Commission in its review of the Independence Policy of the NYSE Euronext Board of Directors (the “Independence Policy”).<sup>5</sup> The proposed rule change also

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<sup>3</sup> The term “committee member” in the By-Laws refers to membership in the committees authorized under Section 4.13 of the By-Laws, such as the Executive Committee and the Audit Committee. Under the By-Laws and the Delaware General Corporation Law, all members of committees with the power and authority to act on behalf of the Board in the management of the business and affairs of NASDAQ OMX must themselves be Directors. Accordingly, the definitions of “Industry Director” and “Industry committee member” are coterminous as applied to any member of these committees. The By-Laws do not presently contemplate any committees with non-Director members.

<sup>4</sup> The By-Laws define each of NASDAQ, NASDAQ OMX BX, Inc. (“BX”), NASDAQ OMX PHLX LLC (“Phlx”), the Boston Stock Exchange Clearing Corporation (“BSECC”), and the Stock Clearing Corporation of Philadelphia (“SCCP”) as a “Self-Regulatory Subsidiary”.

<sup>5</sup> Securities Exchange Act Release No. 51217 (February 16, 2005), 70 FR 9688 (February 28, 2005) (SR-NYSE-2004-54); Securities Exchange Act Release No. 55293 (February 14, 2007), 72 FR 8033 (February 22, 2007) (SR-NYSE-2006-120); Securities Exchange Act Release No. 67564 (August 1, 2012), 77 FR 47161 (SR-NYSE-2012-17; SR-NYSEArca-2012-59; SR-NYSEMKT-2012-07).

makes several other changes to provisions pertaining to the Board's compositional requirements and categorization of Directors.

### **Definitions**

The By-Laws require Directors to be assigned to certain defined categories, based on their current and past affiliations.<sup>6</sup> Specifically, Directors may be categorized as "Industry Directors," "Non-Industry Directors," "Public Directors," and/or "Staff Directors." Currently, an Industry Director is defined as a Director who:

- (1) is or has served in the prior three years as an officer, director, or employee of a broker or dealer, excluding an outside director or a director not engaged in the day-to-day management of a broker or dealer;
- (2) is an officer, director (excluding an outside director), or employee of an entity that owns more than ten percent of the equity of a broker or dealer, and the broker or dealer accounts for more than five percent of the gross revenues received by the consolidated entity;
- (3) owns more than five percent of the equity securities of any broker or dealer, whose investments in brokers or dealers exceed ten percent of his or her net worth, or whose ownership interest otherwise permits him or her to be engaged in the day-to-day management of a broker or dealer;
- (4) provides professional services to brokers or dealers, and such services constitute 20 percent or more of the professional revenues received by the Director or 20 percent or more of the gross revenues received by the Director's firm or partnership;

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<sup>6</sup> As discussed above, the categories also govern the classification of members of committees of NASDAQ OMX, as provided for in the By-Laws.

(5) provides professional services to a director, officer, or employee of a broker, dealer, or corporation that owns 50 percent or more of the voting stock of a broker or dealer, and such services relate to the director's, officer's, or employee's professional capacity and constitute 20 percent or more of the professional revenues received by the Director or 20 percent or more of the gross revenues received by the Director's firm or partnership; or

(6) has a consulting or employment relationship with or provides professional services to the Corporation or any affiliate<sup>7</sup> thereof (including any Self-Regulatory Subsidiary) or to the Financial Industry Regulatory Authority (“FINRA”) (or any predecessor) or has had any such relationship or provided any such services at any time within the prior three years.

Thus, the current definition focuses on a Director’s affiliation with any broker-dealer, regardless of whether the broker-dealer is a member or member organization of a Self-Regulatory Subsidiary. The definition also features a three-year “look-back” period during which a Director formerly associated with a broker-dealer would continue to be deemed an Industry Director.

In lieu of this definition, NASDAQ OMX is proposing to adopt a definition that focuses on whether a Director is affiliated with a member or a member organization of a Self-Regulatory Subsidiary. Under the revised definition, an Industry Director will be defined as a Director who:

(1) is, or within the last year was, or has an immediate family member<sup>8</sup> who is, or within

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<sup>7</sup> NASDAQ OMX is adding a definition of “affiliate” as follows: “An ‘affiliate’ of, or a person ‘affiliated’ with, a specified person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.” The definition is identical to the definition of the term in SEC Rule 12b-2, 17 CFR 240.12b-2.

<sup>8</sup> NASDAQ OMX is adding a definition of “immediate family member” as follows: “‘Immediate family member’ means a person’s spouse, parents, children and siblings, whether by blood, marriage or adoption, or anyone residing in such person’s home.” The

the last year was, a member of a Self-Regulatory Subsidiary;<sup>9</sup>

(2) is, or within the last year was, employed by a member or a member organization of a Self-Regulatory Subsidiary;<sup>10</sup>

(3) has an immediate family member who is, or within the last year was, an executive officer of a member or a member organization<sup>11</sup> of a Self-Regulatory Subsidiary;

(4) has within the last year received from any member or member organization of a Self-Regulatory Subsidiary more than \$100,000 per year in direct compensation, or received from such members or member organizations in the aggregate an amount of direct compensation that in any one year is more than 10 percent of the Director's annual gross compensation for such year, excluding in each case director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service); or

(5) is affiliated, directly or indirectly, with a member or member organization of a Self-Regulatory Subsidiary.

NASDAQ OMX believes that the change is warranted to ensure that the definition of Industry Director is appropriately focused on the mitigation of potential conflicts of interest associated with Directors who are currently or were very recently employed by members or

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definition is identical to the definition of "family member" contained in NASDAQ listing standards, as provided in NASDAQ Rule 5605.

<sup>9</sup> This provision would apply to an individual that was a member of Phlx, the only Self-Regulatory Subsidiary that allows natural persons to become members.

<sup>10</sup> A broker-dealer that is admitted to membership in Phlx is referred to as a "member organization;" broker-dealers admitted to membership in the other Self-Regulatory Subsidiaries are referred to as "members."

<sup>11</sup> An "Executive Officer" of a member or member organization means those officers covered in Rule 16a-1(f) under the Act, as if the member or member organization were an issuer within the meaning of such Rule. 17 CFR 240.16a-1(f).

member organizations of Self-Regulatory Subsidiaries, or that otherwise have material affiliations with such members or member organizations. The current definition covers individuals who are employed by broker-dealers that are not members of Self-Regulatory Subsidiaries, or who retired from service at a broker-dealer more than one, but less than three years in the past. NASDAQ OMX and the Exchange believe that by deeming such potential Directors to be Industry Directors, the current By-Laws unnecessarily restrict highly qualified individuals with extensive knowledge of the financial services industry from serving on the Board.

In addition to this change, NASDAQ OMX is also proposing the following additional changes to the definitions applicable to categories of Directors:

(1) NASDAQ OMX proposes a new definition of “Staff Director.” Currently, the definition of “Staff Director” is included within the definition of “Industry Director,” and is defined as “any two officers of the Corporation, selected at the sole discretion of the Board, amongst those officers who may be serving as Directors.” By virtue of being designated as Staff Directors, these Directors are not considered to be Industry Directors for purposes of the compositional requirements of the By-Laws. Instead, NASDAQ OMX proposes a separate definition of “Staff Director” as “an officer of the Corporation that is serving as a Director.”<sup>12</sup> As discussed below, however, Section 4.3 of the By-Laws is to be amended to provide that only one Staff Director may serve on the Board, unless the Board consists of ten or more Directors, in which case no more than two Staff Directors may serve. Thus, the change will further restrict

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<sup>12</sup> The definition of “Industry Director” will continue to exclude Staff Directors, who might otherwise be considered Industry Directors by virtue of affiliation with NASDAQ Exchange Services LLC and NASDAQ Options Services, LLC, registered broker-dealers that are members or NASDAQ and BX and member organizations of Phlx.

the number of possible Staff Directors in instances where the Board is smaller than ten Directors, while retaining the current limit for a larger Board.

(2) NASDAQ OMX is adopting a new definition of “Issuer Director” and “Issuer committee member”. The By-Laws currently provide that the number of “Non-Industry Directors” (i.e., Directors who are not Industry Directors) must equal or exceed the number of Industry Directors, and shall include at least one “issuer representative,” unless the Board consists of ten or more Directors, in which case it must include at least two issuer representatives. NASDAQ OMX and the Exchange believe that requiring the representation of issuers on the Board is consistent with the goal of promoting a diversity of viewpoints and skills among Directors and the requirement of Section 6(b)(3) of the Act<sup>13</sup> to provide for representation of issuers among the directors of a national securities exchange. The term “issuer representative” is not directly defined in the By-Laws, but is implicitly defined in the definition of “Non-Industry Director” as “an officer, director, or employee of an issuer of securities listed on a national securities exchange operated by any Self-Regulatory Subsidiary.” The new proposed definition is “a Director (excluding any Staff Director) or committee member who is an officer or employee of an issuer of securities listed on a national securities exchange operated by any Self-Regulatory Subsidiary, excluding any Director or committee member who is a director of such an issuer but is not also an officer or employee of such an issuer.” The exclusion of Staff Directors from the definition is necessary because NASDAQ OMX is listed on NASDAQ, but the purposes of the By-Laws in requiring issuer representation to promote a diversity of viewpoints among Directors would not be well served by deeming Staff Directors also to be Issuer Directors. The definition is also being changed to exclude persons who are directors of

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<sup>13</sup> 15 U.S.C. 78f(b)(3).

issuers but not also officers or employees. This change is intended to make it clear that a Director is not barred from being considered a Public Director<sup>14</sup> merely because the Director serves as an independent director of another listed company.

(3) The definition of “Public Director” and “Public committee member” is being restated as follows: “a Director or committee member who (1) is not an Industry Director or Industry committee member, (2) is not an Issuer Director or Issuer committee member, and (3) has no material business relationship with a member or member organization of a Self-Regulatory Subsidiary, the Corporation or its affiliates, or FINRA.” The definition currently covers a person who “has no material business relationship with a broker or dealer, the Corporation or its affiliates, or FINRA.” Thus, the changes make it clear that any Industry Director or Issuer Director would not be considered a Public Director. As noted above, however, an independent director of an issuer of securities listed on NASDAQ could be considered a Public Director. In addition, in keeping with the change to the definition of Industry Director discussed above, the final clause of the definition is being revised to focus on the existence of a material business relationship with a member or member organization of a Self-Regulatory Subsidiary, rather than any broker or dealer. Thus, for example, a Director that had a material business relationship with a non-U.S. broker or dealer that was not a member or a member organization of a Self-Regulatory Subsidiary might be eligible to be a Public Director.

(4) The definition of “Non-Industry Director” or “Non-Industry committee member” is proposed to be amended to cover any “Director (excluding any Staff Director) or committee member who is (1) a Public Director or Public committee member; (2) an Issuer Director or Issuer committee member; or (3) any other individual who would not be an Industry Director or

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<sup>14</sup> The definition of Public Director is discussed below.



Industry committee member.” The revised definition is generally consistent with the current definition, but reflects the adoption of a definition for “Issuer Director or Issuer committee member”.

(5) NASDAQ OMX is making conforming changes to the letter designations of paragraphs in Article I of the By-Laws.

### **Qualifications of Directors**

NASDAQ OMX is proposing to amend Section 4.3 of the By-Laws, which governs the qualifications and compositional requirements of the Board of Directors, to (i) increase the required number of Public Directors from one to two, (ii) replace the requirement to include at least one issuer representative (or at least two issuer representatives if the Board consists of ten or more Directors) with a requirement to include at least one, but no more than two, Issuer Directors, and (iii) provide that the number of Staff Directors may not exceed one, unless the Board consists of ten or more Directors, in which case the number may not exceed two. The section will continue to require that the number of Non-Industry Directors equals or exceeds the number of Industry Directors. Although these changes will not significantly modify the Board’s compositional requirements, they will continue to ensure a diversity of representation among Industry, Staff, Issuer, and Public Directors, will place more stringent caps on the number of Issuer and Staff Directors, and will increase the requirement for Public Directors. NASDAQ OMX also proposes to make a conforming change to add the term “Issuer Director” to Section 4.8 and Section 4.13(h), which govern the filling of vacancies on the Board and the determination of Directors’ qualifications by NASDAQ OMX’s Secretary.

The changes to the compositional requirements imposed specifically by the By-Laws do not alter in any respect the compositional requirements imposed by NASDAQ listing standards

on NASDAQ OMX as a public company. Specifically, NASDAQ Rule 5605 requires that the board of directors of a company listed on NASDAQ must have a majority of directors that are “independent” within the meaning of that rule. As provided in NASDAQ Rule 5605(a)(2) with respect to a company listed on NASDAQ (a “Company”), “ ‘Independent Director’ means a person other than an Executive Officer<sup>15</sup> or employee of the Company or any other individual having a relationship which, in the opinion of the Company’s board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.” The rule goes on to provide that directors having certain defined relationships with a Company may not be considered independent. Thus, while Staff Directors are clearly not independent within the meaning of Rule 5605, other Directors may or may not be considered independent, depending on the specific facts of their relationship to NASDAQ OMX. The proposed rule change does not alter in any respect the obligations of the NASDAQ OMX Board under NASDAQ Rule 5605.

### **Composition of Executive Committee**

NASDAQ OMX is proposing a minor amendment to the compositional requirements of its Executive Committee. Currently, Section 4.13(d) of the By-Laws provides that the percentage of Public Directors on the Executive Committee must be at least as great as the percentage of Public Directors on the whole Board. As noted above, however, the By-Laws currently require only one Public Director on the whole Board (a requirement that NASDAQ OMX is proposing to raise to two Public Directors). Thus, the By-Laws currently reflect a standard under which voluntary inclusion of additional Public Directors on the full Board translates into a requirement to include ever increasing numbers of Public Directors on the

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<sup>15</sup> NASDAQ Rule 5605(a)(1) provides that “ ‘Executive Officer’ means those officers covered in Rule 16a-1(f) under the Act.” 17 CFR 240.16a-1(f).

Executive Committee, even though the requirements for the full Board itself may be satisfied with only one Public Director. Accordingly, NASDAQ OMX is proposing to make the requirements consistent by requiring at least two Public Directors on the Executive Committee.

### **Composition of the Audit Committee**

Earlier this year, the Commission approved changes to the provisions of NASDAQ OMX's By-Laws pertaining to the composition of the Management Compensation Committee of its Board of Directors. NASDAQ OMX is now proposing comparable changes to the compositional requirements of its Audit Committee. Specifically, NASDAQ OMX is proposing to amend Section 4.13(g) to replace a requirement that the Audit Committee be composed of a majority of Non-Industry Directors with a requirement that the number of Non-Industry Directors on the committee equal or exceed the number of Industry Directors. Thus, in the case of a committee composed of four Directors, the current By-Law provides that only one Director may be an Industry Director, while the amended By-Law would allow up to two Directors to be Industry Directors. The proposed compositional requirement for the committee with regard to the balance between Industry Directors and Non-Industry Directors would be the same as that already provided for in the By-Laws with respect to the Executive Committee, the Nominating and Governance Committee, the Management Compensation Committee, and the full Board of Directors.

NASDAQ OMX and the Exchange believe that the change will provide greater flexibility to NASDAQ OMX with regard to populating a committee that includes Directors with relevant expertise and that is not excessively large in relation to the size of the full Board of Directors, while continuing to ensure that Directors associated with members and member organizations of the Self-Regulatory Subsidiaries do not exert disproportionate influence of the governance of

NASDAQ OMX. As required by Section 10A of the Act,<sup>16</sup> SEC Rule 10A-3 thereunder,<sup>17</sup> and NASDAQ Rule 5605(c), the committee would continue at all times to be composed solely of Directors who are independent within the meaning of those provisions.

2. Statutory Basis

NASDAQ believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,<sup>18</sup> in general, and with Sections 6(b)(1) and (b)(5) of the Act,<sup>19</sup> in particular, in that the proposal enables NASDAQ to be so organized and to have the capacity to be able to carry out the purposes of the Act and to comply with and enforce compliance by members and persons associated with members with provisions of the Act, the rules and regulations thereunder, and NASDAQ rules, and 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.

In particular, NASDAQ believes that the change to the definition of Industry Director is warranted to ensure that it is appropriately focused on the mitigation of potential conflicts of interest associated with Directors who are currently or were very recently employed by members or member organizations of Self-Regulatory Subsidiaries, or that otherwise have material affiliations with such members or member organizations, without unnecessarily restricting highly

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<sup>16</sup> 15 U.S.C. 78j-1.

<sup>17</sup> 17 CFR 240.10A-3.

<sup>18</sup> 15 U.S.C. 78f.

<sup>19</sup> 15 U.S.C. 78f(b)(1), (5).

qualified individuals with extensive knowledge of the financial services industry from serving on the Board. NASDAQ further believes that the other definitional changes and the changes to the compositional requirements of the NASDAQ OMX Board and the Executive Committee will enhance the clarity of these provisions and promote a diversity of backgrounds and viewpoints on the NASDAQ OMX Board. The Exchange believes that these changes will collectively promote the capacity of the NASDAQ OMX Board to fulfill its responsibilities.

With respect to the proposed changes to the Audit Committee's compositional requirements, NASDAQ believes that the change will provide greater flexibility to NASDAQ OMX with regard to populating a committee that includes Directors with relevant expertise and that is not excessively large in relation to the size of the full Board of Directors, while continuing to ensure that Directors associated with members and member organizations of Self-Regulatory Subsidiaries do not exert disproportionate influence of the governance of NASDAQ OMX. The change would not affect NASDAQ OMX's compliance with Section 10A of the Act,<sup>20</sup> SEC Rule 10A-3 thereunder,<sup>21</sup> and NASDAQ Rule 5605(c), as the committee would continue at all times to be composed solely of Directors who are independent within the meaning of those provisions.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes [sic] the Act. Specifically, the Exchange believes that the By-Laws of its holding company, NASDAQ OMX, do not directly affect competition between the Exchange and others that provide the same goods and services as the Exchange, since they do not affect the availability or pricing of such goods and services. To the extent that the proposed change to the By-Laws may be construed to have

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<sup>20</sup> 15 U.S.C. 78j-1.

<sup>21</sup> 17 CFR 240.10A-3.

any bearing on competition, the Exchange believes that the change will promote competition between the Exchange and the subsidiaries of NYSE Euronext, since the change will allow NASDAQ OMX to have greater flexibility in the selection of its Directors in a manner similar to the flexibility available to NYSE Euronext under its Independence Policy.

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 (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission shall: (a) by order approve or disapprove such 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 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-2012-142 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-2012-142. 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, D.C. 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 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-2012-142, 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>22</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>22</sup> 17 CFR 200.30-3(a)(12).