

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-67617; File No. SR-NASDAQ-2012-058)

August 8, 2012

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving a Proposed Rule Change Relating to the Listing and Trading of Alpha Index-Linked Securities

I. Introduction

On June 11, 2012, The NASDAQ Stock Market LLC (“Exchange” or “NASDAQ”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to list and trade Alpha Index-Linked Securities. The proposed rule change was published for comment in the Federal Register on June 27, 2012.³ The Commission received no comments on the proposed rule change. This order approves the proposed rule change.

II. Description

The Exchange proposes to add Rule 5712 to provide for the listing and trading of Alpha Index-Linked Securities, which are Equity Index-Linked Securities⁴ linked, on an unleveraged

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 67229 (June 21, 2012), 77 FR 38347 (“Notice”).

⁴ Currently, Exchange Rule 5710 provides for the listing and trading of Equity Index-Linked Securities, which are securities that provide for the payment at maturity of a cash amount based on the performance of an underlying equity index or indexes. See Exchange Rule 5710. In particular, Exchange Rule 5710(k)(i)(A) provides for the listing and trading, pursuant to Rule 19b-4(e) under the Act, of Equity Index-Linked Securities with respect to which the underlying indexes have at least 10 component securities and either: (1) have been reviewed and approved for the trading of options or other derivatives by the Commission under Section 19(b)(2) of the Act and rules thereunder, and the conditions set forth in the Commission’s approval order, including comprehensive surveillance sharing agreements for non-U.S. stocks, continue to be satisfied; or (2) meet the specific index criteria set forth in Exchange Rule 5710(k)(i)(A)(2). Each Alpha Index contains only two component securities, and

basis, to the following Alpha Indexes: GOOG vs. SPY (GOOSY) and AAPL vs. SPY (AVSPY) (together, “Specified Alpha Indexes”). By this filing, the Exchange proposes to list and trade only Alpha Index-Linked Securities linked to the Specified Alpha Indexes.⁵

Alpha Indexes are relative performance based equity indexes maintained by The NASDAQ OMX Group.⁶ Alpha Indexes measure relative total returns⁷ of one stock or one exchange-traded fund (“ETF”) share versus another ETF share (each such combination of two components is referred to as an “Alpha Pair”). The first component identified in an Alpha Pair (“Target Component”) is measured against the second component identified in the Alpha Pair (“Benchmark Component”). To calculate an Alpha Index, NASDAQ measures the total return performance of the Target Component relative to the total return performance of the Benchmark Component, based upon prices of transactions on the primary listing exchange of each component.⁸ Further information about the calculation of Alpha Indexes, including the calculation of the daily total returns of Target Components and Benchmark Components, is available in the Notice.⁹

therefore Alpha Index-Linked Securities are ineligible for listing and trading pursuant to Exchange Rule 5710(k)(i)(A).

⁵ See Notice, supra note 3 at n.4. Accordingly, unlike Exchange Rule 5710, new Exchange Rule 5712 is not a generic listing standard.

⁶ The Commission has previously approved the listing and trading of options on certain Alpha Indexes (“Alpha Index Options”) on NASDAQ OMX PHLX LLC (“PHLX”). See Securities Exchange Act Release Nos. 63860 (February 7, 2011), 76 FR 7888 (February 11, 2011) (SR-Phlx-2010-176) and 65149 (August 17, 2011), 76 FR 52729 (August 23, 2011) (SR-Phlx-2011-89).

⁷ The total return measures performance (rate of return) of price appreciation plus dividends over any given evaluation period.

⁸ Daily total return values and Alpha Index values will be updated based upon prices of each reported transaction in the primary listing market.

⁹ See supra note 3.

Listing of Alpha Index-Linked Securities

New Exchange Rule 5712 permits the listing and trading of Alpha Index-Linked Securities linked to the Specified Alpha Indexes if the Target Component and Benchmark Component meet certain criteria. Alpha Index-Linked Securities listed and traded under new Exchange Rule 5712 must meet the requirements of Exchange Rule 5710(a)-(j).¹⁰ At the initial listing of an Alpha Index-Linked Security, options on both components of the Alpha Index must be listed and traded on the NASDAQ Options Market and must meet the requirements of Chapter IV, Section 3 (Criteria for Underlying Securities) of the NASDAQ Options Market rules.¹¹ Additionally, the Target Component's and the Benchmark Component's trading volume (in all markets in which the components are traded) must have each averaged at least 2,250,000 shares per day in the preceding twelve months.¹² Further, no Alpha Index-Linked Security will be listed unless and until options overlying each of the Alpha Index components have been listed and traded on a national securities exchange with an average daily options trading volume during the three previous months of at least 10,000 contracts.¹³ Moreover, to be eligible for listing, the value of the Alpha Index underlying an Alpha Index-Linked Security must be disseminated at least once every second over the NASDAQ OMX Global Index Data Service ("GIDS").¹⁴

¹⁰ According to the Exchange, effectively, the only provision of Exchange Rule 5710 that will not apply to Alpha Index-Linked Securities is subsection (k), which specifies the criteria for listing and trading Linked Securities under Rule 19b-4(e) under the Act, as well as certain continued listing and delisting criteria. Pursuant to new Exchange Rule 5712(a), all other provisions of Exchange Rule 5710 applicable to Equity Index-Linked Securities eligible for listing and trading pursuant to Rule 19b-4(e) will apply to Alpha Index-Linked Securities.

¹¹ See new Exchange Rule 5712(a)(ii).

¹² See id.

¹³ See id.

¹⁴ See id. GIDS is the NASDAQ OMX global index data feed service, offering real-time updates, daily summary messages, and access to widely followed indexes and ETFs. See

Following the initial listing of an Alpha Index-Linked Security, options on both components of the Alpha Index must continue to meet the continued listing standards set forth in Chapter IV, Section 4 (Withdrawal of Approval of Underlying Securities) of the NASDAQ Options Market rules.¹⁵ Additionally, the Target Component's and the Benchmark Component's trading volume (in all markets in which the components are traded) must have each averaged at least 2,000,000 shares per day in the preceding twelve months.¹⁶ Further, options on each component of the Alpha Index must continue to meet the options average daily volume standard set forth in Exchange Rule 5712(a)(ii).¹⁷

Delisting of Alpha Index-Linked Securities

New Exchange Rule 5712(c) governs the delisting and removal of Alpha Index-Linked Securities and provides commencement of such proceedings – unless the Commission has approved the continued trading — with respect to any Alpha Index-Linked Security where: (1) the aggregate market value or principal amount of the Alpha Index-Linked Securities publicly held is less than \$400,000; (2) the value of the underlying Alpha Index is no longer calculated or widely disseminated on at least a one second basis, provided, however, that if the official index value does not change during some or all of the period when trading is occurring on NASDAQ, then the last calculated official index value must remain available throughout NASDAQ trading hours; (3) such other event occurs or condition exists which, in the opinion of NASDAQ, makes

e-mail from Carla Behnfeldt, Associate General Counsel, Exchange, to Christopher Chow, Special Counsel, Commission, and Yue Ding, Attorney-Adviser, Commission, dated August 3, 2012 (“Nasdaq e-mail”). GIDS provides investment professionals with the daily and historical information needed to track or trade NASDAQ OMX indexes, listed ETFs, or third-party partner indexes and ETFs. See id.

¹⁵ See new Exchange Rule 5712(b).

¹⁶ See id.

¹⁷ See id.

further dealings on NASDAQ inadvisable; (4) any of the standards set forth in Exchange Rule 5712(b) are not continuously maintained; or (5) an underlying Alpha Index fails to satisfy the maintenance standards or conditions for such index as set forth by the Commission in its order under Section 19(b)(2) of the Act approving the index for the trading of options or other derivatives.¹⁸

Trading Rules and Procedures

Trading in Alpha Index-Linked Securities will be governed by the same trading rules and procedures that apply to other Equity Index-Linked Securities listed pursuant to Exchange Rule 5710. Pursuant to Exchange Rule 5710(i), FINRA will implement on behalf of NASDAQ written surveillance procedures for Alpha Index-Linked Securities. The Exchange states that surveillance will be in place for the launch of Alpha Index-Linked Securities.¹⁹ Pursuant to Exchange Rule 5710(j), Alpha Index-Linked Securities will be treated as equity instruments and, for purposes of fee determination, shall be deemed and treated as Other Securities.

Pursuant to Exchange Rule 5710(h), if the value of an Alpha Index is not being disseminated as required, the Exchange may halt trading during the day on which such interruption occurs and will halt trading no later than the beginning of trading following the trading day when the interruption commenced if such interruption persists at that time.

¹⁸ See new Exchange Rule 5712(c). In the case of a corporate event that eliminates one of the underlying components of an Alpha Pair, NASDAQ will cease calculation of the Alpha Index for that Alpha Pair and commence delisting or removal proceedings for the overlying Alpha Index-Linked Securities pursuant to Exchange Rule 5712(c). See Notice, supra note 3, 77 FR at 38348.

¹⁹ See id. at 38349.

III. Discussion and Commission Findings

The Commission has carefully reviewed the proposed rule change and finds that it is consistent with the requirements of Section 6 of the Act²⁰ and the rules and regulations thereunder applicable to a national securities exchange.²¹ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,²² which requires, among other things, that the Exchange's rules be 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, 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 Commission notes that Alpha Index-Linked Securities linked to the Specified Alpha Indexes must comply with the requirements of new Exchange Rule 5712 to be listed and traded on the Exchange.

The Commission further finds that the proposed rule change is consistent with Section 11A(a)(1)(C)(iii) of the Act,²³ which sets forth Congress's finding that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure the availability to brokers, dealers, and investors of information with respect to quotations for, and transactions in, securities. Quotation and last-sale information for the Alpha Index-Linked Securities will be disseminated via UTP Level 1, NASDAQ Basic, NASDAQ Level 2

²⁰ 15 U.S.C. 78f.

²¹ In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

²² 15 U.S.C. 78f(b)(5).

²³ 15 U.S.C. 78k-1(a)(1)(C)(iii).

and NASDAQ TotalView[®].²⁴ To be eligible for listing, the value of all Alpha Indexes underlying Alpha Index-Linked Securities must be disseminated at least once every second over GIDS.²⁵ Information regarding market price and trading volume of the Alpha Index-Linked Securities will be continually available on a real-time basis throughout the day on brokers' computer screens and other electronic devices, and the previous day's closing prices and trading volume information for the Alpha Index-Linked Securities will be published daily in the financial section of newspapers.²⁶ The Commission also notes that information concerning the components of the Specified Alpha Indexes is widely available.

In addition, the Exchange will commence delisting or removal proceedings if the value of the underlying Alpha Index is no longer calculated or widely disseminated on at least a one second basis, provided, however, that if the official index value does not change during some or all of the period when trading is occurring on NASDAQ, then the last calculated official index value must remain available throughout NASDAQ trading hours.²⁷ Further, pursuant to Exchange Rule 5710(h), if the value of an Alpha Index is not being disseminated as required, the Exchange may halt trading during the day on which such interruption occurs, and will halt trading no later than the beginning of trading following the trading day when the interruption commenced if the interruption persists at that time.²⁸

The Commission believes that the listing standards for Alpha Index-Linked Securities should minimize the potential for manipulation. Specifically, for initial listing, the Target

²⁴ See Nasdaq e-mail, supra note 14.

²⁵ See new Exchange Rule 5712(a)(ii).

²⁶ See Nasdaq E-Mail, supra note 14.

²⁷ See new Exchange Rule 5712(c)(ii).

²⁸ The Commission notes that Exchange Rules 4120 and 4121 also govern trading halts on the Exchange.

Component's and the Benchmark Component's trading volume – in all markets in which the components are traded – must have each averaged at least 2,250,000 shares each day in the preceding twelve months.²⁹ Further, options overlying each of the components must have been listed and traded on a national securities exchange with an average daily trading volume of at least 10,000 contracts during the three previous months.³⁰ Following the initial listing, each component's trading volume (in all markets in which the components are traded) must have averaged at least 2,000,000 shares each day in the preceding twelve months.³¹ Options overlying each of the components must maintain an average daily trading volume of at least 10,000 contracts over the three previous months.³² Moreover, the Exchange will commence delisting or removal proceedings with respect to any Alpha Index-Linked Security if the aggregate market value or principal amount of the Alpha Index-Linked Security publicly held is less than \$400,000.³³

In support of this proposal, the Exchange has made representations, including:

- (1) The Exchange deems Alpha Index-Linked Securities to be equity securities, and therefore trading in Alpha Index-Linked Securities will be subject to the Exchange's existing rules governing the trading of equity securities.³⁴

²⁹ See new Exchange Rule 5712(a)(ii).

³⁰ See id.

³¹ See new Exchange Rule 5712(b).

³² See id.

³³ See new Exchange Rule 5712(c)(i). The Commission also notes that Alpha Index-Linked Securities must have a minimum public distribution of 1,000,000 trading units, unless they are traded in \$1,000 denominations or are redeemable at the option of the holders on at least a weekly basis. See Exchange Rule 5710(a), incorporating Exchange Rule 5730(a)(1)(C).

³⁴ See Notice, supra note 3, 77 FR at 38349.

- (2) The Exchange has appropriate rules to facilitate transactions in the Alpha Index-Linked Securities during all trading sessions.³⁵
- (3) Trading of Alpha Index-Linked Securities will be subject to surveillance procedures, and such procedures are adequate to properly monitor trading in the Alpha Index-Linked Securities and to deter and detect violations of Exchange rules and applicable federal securities laws.³⁶
- (4) Prior to the commencement of trading, the Exchange will inform its members in an information circular of the special characteristics and risks associated with trading the Alpha Index-Linked Securities.³⁷ Specifically, the information circular will discuss the following: (a) Nasdaq Rule 2310, which imposes suitability obligations on Nasdaq members with respect to recommending transactions in the Alpha Index-Linked Securities to customers; (b) that Nasdaq members should be mindful of applicable prospectus delivery requirements under the federal securities laws with respect to transactions in Alpha-Index Linked Securities; and (c) trading information.³⁸
- (5) The Exchange may obtain information via the Intermarket Surveillance Group (“ISG”) from other exchanges that are members of ISG or with which the Exchange has entered into a comprehensive surveillance sharing agreement.³⁹

³⁵ See Nasdaq E-Mail, supra note 14.

³⁶ See Notice, supra note 3, 77 FR at 38349.

³⁷ See Nasdaq E-Mail, supra note 14.

³⁸ See id.

³⁹ See Notice, supra note 3, 77 FR at 38349.

Target Components, Benchmark Components, and options on the Target and Benchmark Components are traded on exchanges that are ISG members.⁴⁰

This approval order is based on all of the Exchange's representations and description of Alpha Index-Linked Securities, including those set forth above and in the Notice.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁴¹ that the proposed rule change (SR-NASDAQ-2012-058) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴²

Kevin M. O'Neill
Deputy Secretary

⁴⁰ See id.

⁴¹ 15 U.S.C. 78s(b)(2).

⁴² 17 CFR 200.30-3(a)(12).