

incurred by market participants to use Nasdaq services, it proposes to reduce order execution fees for members that provide liquidity through the NNMS. These fees would be reduced in a manner that would make the per share fee charged to a member to access liquidity during a particular month depend on the extent to which such member provided liquidity through the NNMS during that month (regardless of whether such member charges an access fee). Liquidity provision would be measured by adding the number of shares executed through transactions in which the member's Quote/Order was accessed by another market participant.<sup>7</sup> Thus, during a month in which a member provided a daily average of more than 5,000,000 shares of liquidity through the NNMS, the member would pay \$0.0025 per share executed in trades in which the member accessed liquidity provided by a market participant that does not charge an access fee (*i.e.*, in which the member's Non-Directed or Preferred Orders accessed the Quotes/Orders of other market participants).<sup>8</sup> During a month in which a member provided a daily average of 400,001 to 5,000,000 shares of liquidity, the member would pay \$0.0027 per share executed in trades in which the member accessed liquidity provided by a market participant that does not charge an access fee.<sup>9</sup> Finally, in a month in which a member provided a daily average of 400,000 or fewer trades, the member would pay the current fee of \$0.003 per share executed.<sup>10</sup>

Similarly, the fee paid by a member to access the Quote/Order of a market participant that charges an access fee would depend upon the shares of liquidity provided by the member during the month. During a month in which a member provided a daily average of more than 400,000 shares of liquidity, the member would pay \$0.001

per share executed for trades in which the member accessed liquidity provided by a market participant that charges an access fee;<sup>11</sup> however, the member's total monthly charge would be capped at \$10,000. During a month in which a member provided a daily average of 400,000 shares of liquidity or less, the member would also pay the current fee of \$0.001 per share, but no monthly cap would be applicable.<sup>12</sup>

Nasdaq states that although the proposal will result in members paying fees to access liquidity that vary depending on the extent to which they provide liquidity, Nasdaq strongly believes that the proposal is consistent with the Act and with Commission precedent. Nasdaq believes that the extent to which members provide liquidity through SuperMontage is the single most important factor in determining whether SuperMontage provides an attractive destination, and in turn, whether SuperMontage will generate sufficient revenues to cover the costs of operating and regulating a market. Nasdaq believes a member that offers significant liquidity at prices that establish, or that are near, the national best bid/best offer, makes SuperMontage a more attractive destination for market participants seeking to access liquidity. While many liquidity destinations have used increases in liquidity provider rebates to attract liquidity, Nasdaq believes that higher liquidity rebates are creating distortions in market structure that lead to increased instances of locked and crossed markets. Although Nasdaq's proposed pricing schedule must, for competitive reasons, continue to provide payments for liquidity providers, Nasdaq believes that it is more appropriate to recognize the value of liquidity provision through discounts on the fee for accessing liquidity.

The costs of operating SuperMontage and regulating the Nasdaq market are overwhelming fixed, rather than variable, costs. As SuperMontage's volume increases (*i.e.*, as more and more liquidity is provided through SuperMontage), Nasdaq's costs, on a per share basis, decrease. Accordingly, Nasdaq believes that it is appropriate and equitable to allocate these costs in a manner that takes account of the lower per share costs associated with higher volumes of liquidity provision. Put another way, lower volumes would translate into higher per share costs for market participants; higher volumes reduce per share costs, and Nasdaq

believes that the benefits of these reduced costs can and should be made available to those market participants that make the higher volumes possible in the first place. Moreover, there are economies of scope associated with higher volumes of liquidity provision, because trades executed through SuperMontage also have market data revenue and (in some cases) Automated Confirmation Transaction ("ACT") fees associated with them.

Nasdaq notes that on several occasions in the past, the Commission has approved or allowed the immediate effectiveness of SRO proposals to establish tiered pricing in which the price that different members pay for a service varies, depending on a related variable. For example, Rule 11.10(c) of the NSX (formerly the Cincinnati Stock Exchange) provides that the fee a member pays for agency limit orders depends upon the percentage of public agency market order shares executed during a trading month. Similarly, according to Nasdaq, the New York Stock Exchange's Price List<sup>13</sup> reflects a display device charge for professional subscribers to market data feeds that varies on a per device (rather than a marginal) basis, depending on the number of devices. Thus, a subscriber with few devices pays high fees for each of its devices, while a subscriber with more devices pays lower fees for each of its devices. Nasdaq believes that such pricing structures, like the pricing proposed herein, are entirely appropriate, provided they base the price that a particular member pays upon cost and/or revenue factors associated with providing services to that member.

## 2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,<sup>14</sup> in general, and with Section 15A(b)(5) of the Act,<sup>15</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 the NASD operates or controls. The proposed rule change bases the fees applicable to accessing liquidity through SuperMontage on the extent to which a member provides liquidity, thereby taking account of the lower per share costs and the economies of scope associated with higher volumes of liquidity provision.

<sup>7</sup> If a particular corporate entity has multiple market participant identifiers ("MPIDs") associated with the Central Registration Depository ("CRD") number under which it conducts business, Nasdaq will aggregate shares of liquidity provided through all of its MPIDs. However, Nasdaq will not aggregate one corporate entity's trade reports with those associated with MPIDs assigned to subsidiaries or other affiliates with a different CRD number.

<sup>8</sup> As is true today, a low-priced trade would be subject to a fee cap applicable to trades in excess of 40,000 shares. Accordingly, when the fee that the member pays is \$0.0025, the maximum per transaction charge for a low-priced trade would be \$100.

<sup>9</sup> When the fee that the member pays is \$0.0027, the maximum per transaction charge for a low-priced trade would be \$108.

<sup>10</sup> When the fee that the member pays is \$0.003, the maximum per transaction charge for a low-priced trade would be \$120.

<sup>11</sup> The maximum per transaction charge for a low-priced trade would be \$40.

<sup>12</sup> The maximum per transaction charge for a low-priced trade would be \$40.

<sup>13</sup> See [www.nyse.com/pdfs/2003pricelist2.pdf](http://www.nyse.com/pdfs/2003pricelist2.pdf).

<sup>14</sup> 15 U.S.C. 78o-3.

<sup>15</sup> 15 U.S.C. 78o-3(b)(5).