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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-79200]

Order Granting a Limited Exemption from Rule 102 of Regulation M Concerning NASDAQ Stock Market LLC's New Product Support Incentives Pursuant to Regulation M Rule 102(e)

October 31, 2016

On September 23, 2016, NASDAQ Stock Market LLC ("Exchange" or "NASDAQ") filed with the Securities and Exchange Commission ("Commission") a proposal to amend NASDAQ Rule 7014(f) to, among other things, change their Lead Market Maker Program (now renamed the "Designated Liquidity Provider ("DLP") Program") to include a new rebate, the New Product Support Incentive ("NPSI").[1] Under the NPSI, the Exchange will pay a higher rebate to market makers that act as DLPs in newly launched exchange-traded products ("ETPs")

1 Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Nasdaq's Fees at Rule 7014(f), Exchange Act Release No. 78912 (Sep. 23, 2016); 81 FR 67019 (Sep. 29, 2016) ("NPSI Release").

that meet certain conditions.[2] The proposal became effective upon filing pursuant to Section 19(b)(3)(A)(ii) of the Securities Exchange Act of 1934, as amended ("Exchange Act").[3]

Specifically, the Exchange will pay an NPSI rebate to a DLP of $0.0070 per executed share in the first year from the ETP's launch, on a decreasing scale until the NPSI is phased out as the ETP ages, terminating three years from the ETP's launch.[4] In contrast, the largest rebate that a DLP can collect under the DLP Program's "Basic Rebate" for a non-NPSI ETP is $0.0047 per executed share.[5] NASDAQ represents that the NPSI is designed for the purpose of incentivizing DLPs to support trading in newly launched ETPs.[6]

With the implementation of the NPSI, issuers of newly launched ETPs that choose to list on NASDAQ are automatically enrolled in the NPSI and would indirectly benefit from this

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2 ETPs eligible to be qualified securities for the DLP Program are exchange-traded funds or index-linked securities listed on NASDAQ pursuant to NASDAQ Rules 5705 (Exchange Traded Funds: Portfolio Depository Receipts and Index Fund Shares), 5710 (Securities Linked to the Performance of Indexes and Commodities, Including Currencies), 5720 (Trust Issued Receipts), 5735 (Managed Fund Shares), or 5745 (NextShares). In addition, the ETPs must have at least one DLP. Further, to qualify for the NPSI, the DLP must be at the national best bid or offer at least 20% of the time on average in the assigned ETP, the ETP must have a three-month ADV of less than 500,000, and the ETP must be less than 36 months old. See NASDAQ Rule 7014(f)(1) and (4). Collectively, securities for which rebates under the NPSI are made are referred to in this order as "NPSI Securities."

3 15 U.S.C. 78s(b)(3)(A)(ii). See also NPSI Release.

4 NASDAQ Rule 7014(f)(5)(B). The rebate decreases to $0.0065 per executed share in the second year and $0.0055 per executed share in the third. After the third year, no rebate is paid under the NPSI. These rebates collectively are referred to in this order as "NPSI Rebates."

5 See NASDAQ Rule 7014(f)(4)-(5)(A). In addition to the Basic Rebate and NPSI, a DLP in qualifying ETPs can also receive the "Additional Tape C ETP Incentive," which provides $0.0003 to $0.0005 per executed share, depending on how many ETPs the DLP is assigned to and other conditions are met. See NASDAQ Rule 7014(f)(5)(C).

6 NPSI Release.

liquidity support, which is intended to incentivize market makers to engage in more quotation and trading activity than might otherwise be undertaken in the absence of payments under the NPSI in order to help facilitate the distribution of newly launched ETPs. As such, the Commission believes that participating in the NPSI could constitute an indirect attempt by the issuer to induce a bid for or purchase of a covered security during a restricted period potentially in violation of Rule 102 of Regulation M.[7] NASDAQ represents that the NPSI may incentivize DLPs to support trading in newly launched ETPs.[8]

The Commission has provided limited, conditional exemptions from Rule 102 for issuers to participate in a number of similar programs, such as the NASDAQ MQP, which also involved an indirect attempt by the issuer to induce a bid for or a purchase of a covered security during a restricted period.[9] Like the NPSI, these programs are designed to incentivize market makers to

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[7] 17 CFR 242.102. The Commission notes in this regard the focus of the NPSI on newly launched ETPs. Cf. Order Instituting Proceedings to Determine Whether to Approve or Disapprove Proposed Rule Changes Relating to Market Maker Incentive Programs for Certain Exchange-Traded Products, Exchange Act Release No. 67411 (Jul. 11, 2012), 77 FR 42052 (Jul. 17, 2012) (regarding the similar NASDAQ Market Quality Program ("MQP"), stating that "[t]he Commission believes that issuer payments made under the SRO Proposals would constitute an indirect attempt by the issuer of a covered security to induce a purchase or bid in a covered security during a restricted period in violation of Rule 102" and noting that "under the NASDAQ Proposal, the issuer payments would 'be used for the purpose of incentivizing one or more Market Makers in the MQP Security,' which could induce bids or purchases for the issuer's security during a restricted period").

[8] NPSI Release.

[9] See Order Granting a Limited Exemption from Rule 102 of Regulation M Concerning the NASDAQ Stock Market LLC Market Quality Program Pilot Pursuant to Regulation M Rule 102(e), Exchange Act Rel. No. 69196 (Mar. 20, 2013); 78 FR 18410 (Mar. 26, 2013); Order Granting a Limited Exemption from Rule 102 of Regulation M Concerning the NYSE Arca, Inc.'s Exchange Traded Product Incentive Program Pilot Pursuant to Regulation M Rule 102(e), Exchange Act Rel. No. 69707 (Jun. 6, 2013); 78 FR 35330 (Jun. 12, 2013); Order Granting a Limited Exemption from Rule 102 of Regulation M Concerning the NYSE Arca, Inc.'s Crowd Participant Program Pilot, Exchange Act Rel. No. 71805 (Mar. 26, 2014); 79 FR 18365 (Apr. 1, 2014); and Order Granting a Limited

make markets in specific securities. The Commission's exemptions for these programs are intended to ensure that investors purchasing ETPs that are being quoted or traded as a result of incentive payments are notified in advance of the potential consequences of such payments on the prices and liquidity of such ETPs. The Commission believes that it is appropriate to exempt issuers from Rule 102 to permit participation in the NPSI with similar disclosure to investors.

The Commission believes that potential investors in NPSI Securities should be provided with sufficient information regarding the potential impact of the NPSI on the price and liquidity of the ETPs, particularly given the temporary and limited nature of each ETP's enrollment in the program. Accordingly, the Commission is granting a limited exemption from Rule 102 of Regulation M solely to permit issuers to participate indirectly in the NPSI Rebates, subject to certain conditions described below.

Rule 102 of Regulation M

Rule 102 of Regulation M prohibits issuers, selling security holders, or any affiliated purchaser of such persons, directly or indirectly, from bidding for, purchasing, or attempting to induce any person to bid for or purchase a covered security[10] during the applicable restricted period in connection with a distribution of securities effected by or on behalf of an issuer or selling security holder, except as specifically permitted in the rule.[11] As mentioned above, the Commission believes that issuers participating in the NPSI could constitute an indirect attempt to

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Exemption from Rule 102 of Regulation M Concerning the BATS Exchange, Inc.'s Pilot Supplemental Competitive Liquidity Provider Program, Exchange Act Rel. No. 72693 (Jul. 28, 2014); 79 FR 44875 (Aug. 1, 2014).

10 Covered security is defined as any security that is the subject of a distribution, or any reference security. 17 CFR 242.100(b).

11 17 CFR 242.102(a).

induce a bid for or purchase of a covered security during the applicable restricted period. Accordingly, absent exemptive relief, issuers of NPSI Securities ("NPSI Issuers") that list on NASDAQ while the NPSI is in effect may violate Rule 102.

On the basis of the conditions set out below, which in general are designed to help inform investors about the potential impact of the NPSI to potential investors of NPSI Securities, the Commission finds that it is appropriate in the public interest, and is consistent with the protection of investors, to grant a limited exemption from Rule 102 of Regulation M solely to permit NPSI Issuers to list NPSI Securities on NASDAQ while the NPSI is in effect and thus, to participate indirectly in the payment of the NPSI Rebates to DLPs.[12]

This limited exemption is conditioned on the NPSI Issuer, or sponsor if applicable, making specific disclosures, as set forth below. The disclosures are designed to alert potential investors that the trading market for NPSI Securities may be affected by these payments. Specifically, these disclosures are designed to inform potential investors about the potential impact of the NPSI on the natural market forces of supply and demand prior to making an investment decision in these newly launched securities products. These disclosures are expected to promote greater investor protection by helping to ensure that investors adequately informed as to this potential impact. We also note that, to the extent that information about the NPSI is material, disclosure of this kind may already be required by the federal securities laws.

Conclusion

IT IS THEREFORE ORDERED, pursuant to Rule 102(e) of Regulation M, that NPSI Issuers are hereby exempted from Rule 102 of Regulation M solely to permit NPSI Issuers to

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[12] Rule 102(e) allows the Commission to grant an exemption from the provision of Rule 102, either unconditionally or on specified terms and conditions, to any transaction or class of transactions, or to any security or class of securities.

participate in the NPSI as set forth in NASDAQ Rule 7014(f), subject to the condition that the NPSI Issuer (or the sponsor, if applicable) shall make the following disclosures in a press release, as well as prominently and continuously on its website, for each specific ETP that it intends to list, or has listed, on NASDAQ:

(1) At the beginning of the restricted period, as defined in Rule 100 of Regulation M,[13] for the NPSI Security, the following disclosure shall be continuously provided until the disclosure in (2) below is required: "[Specific ETP name] intends to list on NASDAQ on or around [anticipated date]. Once listed, [Specific ETP] is automatically eligible for NASDAQ's New Product Support Incentives Rebate ("NPSI Rebate"), which is a payment made to certain market makers depending on how actively they quote and trade [Specific ETP]. Market makers quoting and trading [Specific ETP] on NASDAQ will receive such payments for up to three years from the launch date for [Specific ETP] if they meet the requirements for such payments.";

(2) Immediately after launch, or immediately at the beginning of the period in which a market maker's trading activity can qualify for an NPSI Rebate in an NPSI Security, as applicable, the following disclosure shall be continuously maintained and updated until termination of the NPSI Rebate, and shall, as necessary, be supplemented with the disclosure in (3) below: "The [Specific ETP name] is listed on NASDAQ. As such, it is enrolled in NASDAQ's New Product Support Incentives Rebate ("NPSI Rebate"), which is a payment made to certain market makers depending on how actively they quote and trade [Specific ETP]. The [Specific ETP] has participated in

[13] 17 CFR 242.100(b).

the NPSI Rebate since [date], and will no longer be eligible to participate in the program on [date], which is three years from the launch date (unless the program is terminated or modified before then or if [Specific ETP] becomes too liquid to participate in the NPSI before then). Certain market makers quoting and trading [Specific ETP] on NASDAQ will be eligible to receive NPSI Rebates until that date, unless, again, the program is terminated or modified before then or if [Specific ETP] becomes too liquid to participate in the NPSI before then. The payment of the NPSI Rebates is intended to help provide liquidity support for newly launched exchange-traded products by generating more quotes and trading than might otherwise exist absent these payments. Investors should be aware that when these payments cease, there may be an adverse impact on the price and liquidity of [Specific ETP], which could adversely impact a purchaser's subsequent sale of the security."; and

(3) No less than 30 days before the expected termination date, or as soon as practicable after the NPSI Issuer becomes aware or should become aware that the NPSI Security will no longer be eligible to participate in the NPSI and before the end of such eligibility, the following disclosure shall be added to the disclosure required in (2) above: "UPDATE: [Specific ETP] is expected to no longer qualify for the NPSI rebates on [or around] [date]. This may impact the price or liquidity of [Specific ETP], which could adversely impact a purchaser's subsequent sale of the security."

This exemptive relief shall terminate upon the event of any material change to the NPSI, including a change to the types of securities permitted to participate in the program or to the terms or amount of the payments made pursuant to the NPSI.[14] Further, this exemptive relief is

[14] Accordingly, we expect NASDAQ to contact staff in the Office of Trading Practices in

subject to modification or revocation at any time the Commission determines that such action is necessary or appropriate in furtherance of the purposes of the Exchange Act. This exemptive relief is limited solely to the issuer's indirect participation in the payment of the NPSI Rebates as set forth in NASDAQ Rule 7014(f)(5)(B) for an NPSI Security, and does not extend to any other activities of the issuer, any other security of the issuer or sponsor, or any other issuers.[15] In addition, persons relying on this exemption are directed to the anti-fraud and anti-manipulation provisions of the Exchange Act, particularly Sections 9(a) and 10(b), and Rule 10b-5 thereunder. Responsibility for compliance with these and any other applicable provisions of the federal securities laws must rest with the persons relying on this exemption. This order does not represent Commission views with respect to any other question that the proposed activities may raise, including, but not limited to the adequacy of the disclosure required by federal securities laws and rules, and the applicability of other federal or state laws and rules to, the proposed activities.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[16]

Brent J. Fields
Secretary

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the Division of Trading and Markets before making any material change to the NPSI.

15 Other activities, such as ETF redemptions, are not covered by this exemptive relief.

16 17 CFR 200.30-3(a)(6).

[FR Doc. 2016-26646 Filed: 11/3/2016 8:45 am; Publication Date: 11/4/2016]