November 11, 2009

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File Nos. 10-193 and 10-194

Dear Ms. Murphy:

The NASDAQ OMX Group, Inc. ("NASDAQ OMX") appreciates the opportunity to submit written comments on the Notice of Filing of Applications, as Amended, by EDGX Exchange, Inc. ("EDGX") and EDGA Exchange, Inc. ("EDGA", and collectively with EDGX, the "Applicants") for Registration as National Securities Exchanges under Section 6 of the Securities Exchange Act of 1934, Securities Exchange Act Release No. 60651 (September 11, 2009), 74 FR 47827 (September 17, 2009) (File Nos. 10-193 and 10-194) (the "Applications").

NASDAQ OMX is concerned that several aspects of the Applications raise legal policy issues that must be fully examined by the Securities and Exchange Commission (the "Commission") before the Applications may be approved.

- First, the Applications fail to describe the ownership and governance structure of the Applicants in sufficient detail to allow the Commission to determine whether concentration of control in the hands of a small number of broker-dealers will conflict with the Applicants' regulatory obligations. Specifically, the Applications contain no discussion of how the Applicants will implement policies and procedures to manage conflicts of interest that may exist between their obligations as exchanges and the interests of their owners. NASDAQ OMX believes that, in the absence of a full discussion of these issues, the record does not provide an adequate basis for the Commission to determine that the Applications are consistent with the Securities Exchange Act of 1934 (the "Act").

- Second, the Applications propose several rules that are inconsistent with policies recently announced by the Commission or its staff with regard to flash orders and registration of associated persons of exchange members.[1] Accordingly, we believe that the Commission

[1] We also note that because the Applications do not contain proposed fees, the Commission and the public are not yet in a position to evaluate whether the adoption of fees similar to those currently in effect for the two trading venues operated by the Applicants' affiliate, Direct Edge ECN LLC ("Direct Edge ECN"), would be consistent with the Act if adopted by the Applicants.

will need to evaluate legal and policy issues associated with these rules before approving exchange registration applications that include them.

In light of these deficiencies, the Commission should either reject the Applications as incomplete or institute proceedings to disapprove them.

Ownership and Governance

Licensed cash equities exchanges in the U.S. are subject to limits on governance and ownership imposed by the Commission. Accordingly, in evaluating an exchange application, it is important for the Commission to evaluate governance and control structures and determine whether they promote diverse representation on exchange boards and limit concentrated control of exchange assets. Exhibit K of the Applications states that the Applicants "will be wholly-owned by Direct Edge Holdings LLC. Direct Edge Holdings will exercise 'control' over the Exchange[s], as that term is defined in the Form 1 instructions." Because this response fails to provide meaningful information about the persons that actually will control the Applicants, NASDAQ OMX believes that the Applications are not in technical compliance with the requirements of Form 1. Moreover, insofar as the Applicants fail to provide any discussion or analysis about how they and their actual owners will manage conflicts of interest that may exist in the proposed ownership structure, we believe that the Commission will need to evaluate whether the Applicants have met their burden of demonstrating that they are organized in a manner that will allow them to comply with the requirements of Section 6 of the Act, including the requirements to be so organized and have the capacity to be able to carry out the purposes of the Act; to enforce compliance by members with the Act and the rules of the exchange; 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 to avoid unfair discrimination between customers, issuers, brokers, or dealers.

To find information about the Applicants' actual control persons, one must open the "Fourth Amended and Restated Limited Liability Company Operating Agreement of Direct Edge Holdings LLC", filed as part of Exhibit C, and parse through 101 pages of dense contractual language.[2] In doing this, one learns that three major broker-dealers each own 19.9% and collectively own 59.7% of the ownership interests in Direct Edge Holdings LLC ("Holdings") and also collectively control 6 out 11 of the seats of its board of directors. Five other broker-dealers collectively own 8.74% and control one board seat. International Securities Exchange Holdings, Inc. ("ISE"), a subsidiary of Eurex, which is itself jointly owned by Deutsche Börse AG and SIX Swiss Exchange AG, owns 31.54% of Holdings and controls 3 board seats. Finally, a board seat is reserved for the Chief Executive Officer of Holdings, who is also slated to serve as Chief Executive Officer of the Applicants.

[2] Given its importance to understanding the control and governance structure of the Applicants, the Operating Agreement must be deemed a rule of the Applicants if they are granted exchange status.

An examination of the proposed by-laws for the Applicants indicates that this ownership structure will also be reflected, in somewhat more muted form, in the structure of the Board of Directors of each of the Applicants. There, although a majority of the Board seats are reserved for directors that do not have a material relationship with the Applicants, their members, or their affiliates, 25% percent of the Board seats are reserved for corporate insiders. An additional 20% of the seats are reserved for exchange members. Thus, nine out of nineteen seats on each board will be held by broker-dealers and/or corporate insiders.

As exchanges began to move away from a mutual form of ownership, in which all members hold equity interests in the exchange, the Commission recognized that dominance of an exchange by a controlling owner could have deleterious effects on the exchange's regulatory obligations:

> It is common for members who trade on an exchange to have ownership interests in the exchange. However, a member's interest could become so large as to cast doubt on whether the exchange can fairly and objectively exercise its self-regulatory responsibilities with respect to that member. A member that is also a controlling shareholder of an exchange might be tempted to exercise that controlling influence by directing the exchange to refrain from diligently surveilling the member's conduct or from punishing any conduct that violates the rules of the exchange or the federal securities laws. An exchange also might be reluctant to surveil and enforce its rules zealously against a member that the exchange relies on as its largest source of capital.[3]

Based on these concerns, the Commission has imposed restrictions on ownership of exchanges that seek to demutualize or that register de novo as for-profit entities. The Commission has also imposed similar restrictions on entities such as the affiliates of the Applicants that operate as privately owned facilities of exchanges. Specifically, the restrictions generally provide that no single member may own more than 20% of the exchange, and no single owner may own more than 40%. In addition, with respect to exchange holding companies, the Commission has imposed restrictions on the percentage of the company's stock that can be voted by a single stockholder. NASDAQ OMX notes, however, that because these restrictions have not been the product of a Commission rulemaking, they have not been consistently applied, nor have they been consistently explained. For example, there is no clear basis in SEC rules for NASDAQ OMX being subject to a 5% limit on the voting of its stock by a single stockholder, while NYSE Euronext is subject to a 10% limit and newer exchanges such as the BATS Exchange are not subject to any voting limitation separate from a 20%/40% ownership limit.

NASDAQ OMX believes that the time is ripe for the Commission to re-examine these restrictions and adopt a consistent rule applicable to all exchanges (as well as alternative trading systems, which would be required to register as exchanges but for the exemption provided by Regulation ATS). Moreover, we believe that the Commission should consider not only the risk of inadequate surveillance and enforcement, but also the risk that exchanges will be operated for

---

[3] Securities Exchange Act Release No. 49067 (January 13, 2004), 69 FR 2761 (January 20, 2004) (SR-BSE-2003-19).

the benefit of a small number of member/owners with consolidated ownership well in excess of the 20% limit applicable to a single member or the 40% limit applicable to a single non-member owner.

The Commission has previously focused on the risk that a controlled exchange would willfully turn a blind eye to infractions by its members. We believe that the Commission should also focus on the risk that a subtle yet pervasive bias will infect the relationship between the exchange and its member/owners, such that business decisions by both the exchange and the member/owners are continually influenced by the relationship, to the detriment of the customers of both and to the detriment of a competitive national market system. Moreover, although the restrictions previously approved by the Commission recognize that an owner could not remain in compliance with the 20%/40% limits by splitting ownership interests across other entities that it controls, we do not believe that the Commission has evaluated the possibility that multiple owners, each owning 20%, could have a commonality of interest that causes them to act in concert on a consistent basis.

The conflict of interest inherent in concentrated control of market infrastructure has recently received attention from Congress. In last month's mark-up of the Over-the-Counter Derivatives Markets Act of 2009, the House Financial Service Committee voted in favor of restricting voting control by over-the-counter derivatives dealers of facilities that clear or trade these instruments.[4] We believe that these restrictions are motivated by a concern that large dealers should not be in a position to write the rules that govern the operation of key facilities, and we share this concern. Numerous aspects of clearinghouse and trading facility operations – including openness to competing members, construction of margin requirements, and willingness to offer services that increase market transparency – could be adversely affected by vertical integration of dealers with market infrastructure.

Similarly, in the case of the Applicants, the bias inherent in concentrated dealer control has the potential to affect numerous aspects of the operations of both the exchange and its member/owners. This means that as the Commission reviews each and every rule filing of a controlled exchange, it must consider whether the filing is the product of bias. For example:

- When a controlled exchange files fees that it will charge to members, the Commission will have to assess the relative effect of the fee change on member/owners and other members to determine if the change reflects an equitable allocation of reasonable fees and does not impose a burden on competition, as required by Section 6 of the Act. Has a price cut been structured so that it is disproportionately beneficial to the member/owners, either because no other members have the volume required to benefit from the cut, or because the cut is focused on market activity in which other members do not engage? If a price cut filed by an independent exchange that is available to a limited number of members would be equitable, can the same conclusion be reached if the price cut is available only to the member/owners whose representatives sit on the board of directors

[4] See http://www.house.gov/apps/list/speech/financialsvcs_dem/lynch_035.pdf.

that approved the price cut? Will a price increase have a disproportionate impact on competitors of the member/owners?

- Is a change to market structure, such as a new order type or execution algorithm, designed to complement aspects of the member/owners' business models? In this regard, we note that the Applicants' predecessor, Direct Edge ECN, pioneered the widespread use of "flash orders," which allow the member/owners and other subscribers to see and access orders that Direct Edge ECN cannot execute before they are cancelled or routed to other venues. Although the Commission recently proposed banning flash orders, Direct Edge ECN continues to use them and the Applicants' rules contemplate their continued use. Thus, the question arises whether Direct Edge ECN's use of flash orders provides specific advantages to the member/owners. We believe that the Commission will have to examine questions such as these whenever it reviews proposed market structure changes by the Applicants.

- In a time when most brokers are members of multiple exchanges, a single exchange has little ability unilaterally to alter the overall regulatory burdens on its members. Nevertheless, changes by one exchange may put pressure on others to follow suit. Thus, whenever the Applicants propose to alter rules that regulate member conduct, the question may arise as to whether the proposal is a stalking horse for changes that the member/owners are seeking in the industry to benefit their business models.

The Commission should also consider whether the linkage between the Applicants and their member/owners could provide either with unfair advantages by allowing the member/owners and the Applicants to exchange information. The Applicants have proposed various rules that purport to restrict the flow of confidential information between the Applicants and other persons, such as Rules 2.10 and 2.11 and Article XI of each set of proposed by-laws for the Applicants. However, the Applicants fail to explain how these restrictions will actually be implemented, given the likely presence of representatives of each of the controlling owners on the boards of directors of the Applicants. Thus, Article XI, Section 3 provides that board meetings pertaining to the self-regulatory function of the Applicants are closed to all persons other than directors, officers, employees, agents or advisors. It also provides that no members of the board of managers of Holdings, or its officers, employees, agents or advisors, may participate in a board meeting of the Applicants unless that person is also a director, officer, employee, agent or advisor of the Applicants. In other words, the restriction does not apply at all if the individual in question is wearing the same hat on behalf of both the Applicant and its parent corporation. Section 11.2 of the Operating Agreement of Holdings provides that books and records reflecting confidential information pertaining to the self-regulatory function of the Applicants that come into possession of Holdings shall be held in confidence by Holdings and its Members. In this context, the word "members" means the owners of Holdings, including the member/owners. This appears to be a very leaky barrier indeed: information can flow from the Applicants to Holdings through common directors, officers, or employees, and can then flow from Holdings to the member/owners, as long as they hold the information in confidence. Moreover, there does not appear to be any restriction on the flow of business information, such as plans for changes to

market technology or new market structure initiatives, from the Applicants to the member/owners, nor does there appear to be a restriction on flows in the opposite direction, such that the Applicants would have advance knowledge of new initiatives by the member/owners.

A decade ago, when mutualized exchanges first began to consider selling stock to the public, questions were raised about the potential for conflict between exchanges adopting a for-profit model and their regulatory obligations. We believe that experience has instead shown the benefits of demutualization. As exchanges have achieved greater independence from their members, the risk of serious regulatory issues associated with inadequate member surveillance – such as problems associated with NASD/NASDAQ market makers in the 1990s or New York Stock Exchange specialists earlier in this decade – has actually diminished. Market incentives reinforce the regulatory mandate for effective market oversight, since a loss of confidence in a market operated by a public company would be highly detrimental to its profitability. The Applicants, by contrast, represent a trend toward remutualization of exchanges not as industry-owned utilities, but rather as liquidity pools operated to advance the interest of a narrow set of owners. Under this model, the Commission must be prepared to provide the active oversight necessary to ensure that it does not degrade market quality, place burdens on competition, or lead to failures of regulatory oversight. To ensure that the issues are fully examined before the Commission takes action on the Applications, NASDAQ OMX urges the Commission to reject the Applications as incomplete and require the Applicants to file for public comment a description of their relationship to their owners and a comprehensive discussion of the policies and procedures that they intend to implement to manage that relationship.

Inadequacies in the Rulebooks of the Applicants

Flash Orders. NASDAQ OMX notes at least two significant deficiencies in the rulebooks of the Applicants. First, the Applicants persist in proposing the flash order functionality that Direct Edge ECN popularized in the cash equities markets, and that the Commission has recently proposed banning. Although there is nothing impermissible at present about Direct Edge ECN's usage of this order type, we question whether the Commission should approve an exchange rule, as well as an exchange application including a rule, that would become illegal if the Commission's flash order ban is adopted.[5]

As the Commission explained in its notice of proposed rulemaking, "[t]he flashing of order information could lead to a two-tiered market in which the public does not have access, through the consolidated quotation data streams, to information about the best available prices for U.S.-listed securities that is available to some market participants through proprietary data feeds. In addition, flash orders may significantly detract from incentives for market participants to display

[5] We also note that Direct Edge ECN's initial introduction of flash orders was never the subject of a rule filing because that entity's operations were exempted from rule filing requirements, initially due to its status as an alternative trading system and subsequently due to a protracted exemption from Section 19 of the Act that was granted when Direct Edge ECN became a facility of the International Securities Exchange.

their trading interest publicly, though flash orders do offer potential benefits to certain types of market participants."[6]

NASDAQ OMX intends to file a comment letter supporting the Commission's flash order rulemaking, and therefore does not propose to engage in a comprehensive discussion of the demerits of flash orders in its comment letter on the Applications. Rather, we note that the decision to include this order type as a prominent feature of the Applications seems designed to place the Commission in an uncomfortable position: either it must formally approve usage of an order type that it elsewhere proposing to ban; it must disapprove the Applications even though there is not yet a firm rule upon which to base that disapproval; or it must defer action on the Applications until the completion of the flash trade rulemaking, even if this means bypassing the 90-day deadline for action that Congress enacted in Section 19 of the Act. If the Commission chooses not to reject the Applications for the reasons discussed above, then given these alternatives, we believe that the Commission should institute disapproval proceedings unless the Applicants remove flash orders from their proposal, in the expectation that the flash order rulemaking will be completed while the disapproval proceeding is pending.

Membership Rules. Earlier this year, Commission staff sent a letter to various self-regulatory organizations urging them to review their rules governing registration of associated persons of members. The letter suggested that such rules should require all associated persons conducting a securities business to register with the self-regulatory organization through Form U4 and be subject to appropriate examination, training and continuing education requirements. In addition, staff concluded that all self-regulatory organizations should have rules that require registration as a principal of one or more associated persons at each member firm. NASDAQ OMX supports industry-wide adoption of these standards, to provide a comprehensive and consistent system for supervision, registration, examination, and training of securities industry personnel. We believe that several self-regulatory organizations, including The NASDAQ Stock Market ("NASDAQ") and the Financial Industry Regulatory Authority, have rules that comply with these precepts. We understand that other exchanges are working with Commission staff on rule proposals that would modify rules to meet these requirements as soon as practicable.

The Applicants have proposed rules that do not clearly require the registration of all associated persons, and that in any event, do not contemplate the registration of any associated persons with the Applicants in the capacity of a principal. The Applicants should be required to amend their rules to address this deficiency, or, in the alternative, the Commission should institute proceedings to disapprove the Applications.

Fees. The Applications do not include the fees, dues and other charges that the Applicants intend to charge. As a threshold matter, NASDAQ OMX believes that this omission makes the Applications deficient, since the Applicants have not actually filed all of the rules under which they propose to operate. As a result, the Commission and the public have no insight into whether the Applicants intend to charge fees comparable to those currently charged by the two trading

[6] Securities Exchange Act Release No. 60684 (September 18, 2009), 74 FR 48632 (September 23, 2009) (File No. S7-21-09).

venues operated by Direct Edge ECN. Direct Edge ECN's pricing for each venue provides discounts based on activity on the other venue, effectively treating both as a combined whole for pricing purposes. If the fees that the Applicants will propose are comparable, the Commission will have to evaluate the conditions under which pricing of one self-regulatory organization may reference activity of a member on another affiliated self-regulatory organization. If this is an issue that the Commission believes to be important, then the Applicants should be required to file their pricing now so that it can be evaluated before the Commission takes final action on their Applications.

The issue is also implicated by a NASDAQ Stock Market filing that has been pending in an unpublished state since June of this year. In SR-NASDAQ-2009-054 (June 24, 2009), NASDAQ proposed adoption of discounts for trading cash equities that would be available to members providing certain volumes of liquidity on NASDAQ and trading certain volumes of options on NASDAQ OMX PHLX. Although the filing qualifies for immediate effectiveness under Section 19(b)(3)(a)(ii) of the Act, NASDAQ acceded to a request by Commission staff to submit the filing for notice and comment in order to allow the Commission to provide its views on any novel issues presented by the filing. NASDAQ justified the proposal by noting that (i) many firms trade both cash equities and options as part of a unified approach to investing and risk management, and they should be entitled to receive pricing that also reflects a unified approach, and (ii) NASDAQ and NASDAQ OMX PHLX now operate using a common technology (although they do not share physical hardware), and market participants should receive benefits from associated synergies.

If the Commission does not require the Applicants to file proposed pricing before becoming registered as exchanges, the Applicants will certainly have to submit pricing filings under Section 19 of the Act before becoming operational as exchanges. NASDAQ OMX would expect that any actions taken on such filings would be consistent with actions with respect to SR-NASDAQ-2009-054. Thus, if the Commission allows the Applicants to file combined pricing on an immediately effective basis, NASDAQ OMX would expect to be permitted to withdraw SR-NASDAQ-2009-054 and refile it on an immediately effective basis. Alternatively, if the Commission determines that notice and comment is required with respect to proposals by the Applicants, NASDAQ OMX would expect that the Commission would not publish the Applicants' filings without also publishing NASDAQ's proposal. Finally, we would expect that any determinations made by the Commission in connection with any of these filings would be comprehensive and universally applicable.

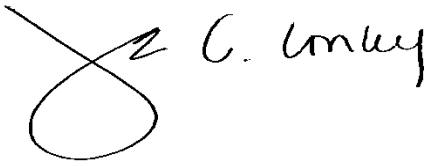
Conclusion

NASDAQ OMX believes that the time is ripe for the Commission to evaluate the trend of remutualization of exchanges subject to the control of a small subset of brokers. We believe that the Applicants must take special measures to manage conflicts of interest and bias arising from their relationship with their owners, and must thoroughly describe those measures in advance of registration to allow the Commission and the public to evaluate them. Accordingly, the Commission should reject the Applications' as incomplete until such time as the Applicants file

their relevant policies and procedures. Likewise, the Commission should require the Applicants to file their proposed fees and rectify their deficient rules regarding flash orders and membership.

If you have any questions, please do not hesitate to contact me at (301) 978-8735.

Sincerely,



Joan C. Conley
Senior Vice President and Corporate Secretary

cc: Mary L. Shapiro, Chairman
Kathleen L. Casey, Commissioner
Elisse B. Walter, Commissioner
Luis A. Aguilar, Commissioner
Troy A. Parades, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
James Brigagliano, Deputy Director, Division of Trading and Markets
Daniel Gallagher, Deputy Director, Division of Trading and Markets
Elizabeth King, Associate Director, Division of Trading and Markets
David Shillman, Associate Director, Division of Trading and Markets