

quote prior to the 9:20 a.m. Trade-or-Move process. The Commission finds that Amendment No. 3 does not change the proposal. Amendment No. 3 merely clarifies the proposal and commits Nasdaq to addressing technological issues within specified time frames. Consequently, the Commission finds good cause, consistent with section 6(b)(5) and section 19(b) of the Act to approve Amendment Nos. 2 and 3 to the proposed rule change on an accelerated basis.

## V. Conclusion

For the foregoing reasons, the Commission finds that the proposal, as amended, is consistent with the requirements of the Act and rules and regulations thereunder.

It is therefore ordered, pursuant to section 19(b)(2) of the Act,<sup>40</sup> that the proposed rule change (SR-NASD-2002-56) and Amendment No. 1 are approved, and Amendment Nos. 2 and 3 are approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>41</sup>

**Margaret H. McFarland,**  
Deputy Secretary.

[FR Doc. 02-22216 Filed 8-29-02; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46416; File No. SR-NASD-2002-98]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 by the National Association of Securities Dealers, Inc. to Eliminate the Regulatory Fee and Institute a New Transaction-Based Trading Activity Fee

August 23, 2002.

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 July 24, 2002, the National Association of Securities Dealers, Inc. ("NASD" or "Association") filed with the Securities and Exchange Commission ("Commission" or "SEC") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the NASD. On August 21, 2002, the NASD amended the proposed

rule change.<sup>3</sup> The NASD designated one portion of the proposed rule change as establishing or changing a due, fee, or other charge pursuant to section 19(b)(3)(A)(ii) of the Act,<sup>4</sup> and Rule 19b-4(f)(2) thereunder,<sup>5</sup> which renders that portion of the proposed rule change effective upon filing with the Commission. The NASD designated the portion of the proposed rule change regarding the corporate name change as administrative pursuant to section 19(b)(3)(A)(iii) of the Act,<sup>6</sup> and Rule 19b-4(f)(3) thereunder,<sup>7</sup> which also renders that portion of the proposed rule change effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The NASD proposes to amend Schedule A to the NASD By-Laws to amend its member regulatory pricing structure. Under the current structure, three types of fees and assessments are used to fund the NASD's member regulatory activities: Regulatory Fee,<sup>8</sup> Personnel Assessment, and Gross Income Assessment.<sup>9</sup> The proposed restructuring is comprised of four amendments: (1) Eliminate the Regulatory Fee; (2) institute a new transaction-based Trading Activity Fee similar to the SEC's Section 31 Fee; (3) increase the rates assessed to member firms under the Personnel Assessment; and (4) implement a simplified three-tiered flat rate for the Gross Income Assessment and eliminate current deductions and exclusions.<sup>10</sup> This proposed rule change is a part of a package of two separate yet related rule

<sup>3</sup> See August 21, 2002 letter from Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, NASD, to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), SEC, and attachments ("Amendment No. 1"). In Amendment No. 1, the NASD provided new proposed rule language that completely replaces and supersedes the original proposed rule language, and also made minor technical changes to the proposed rule change. For purposes of calculating the 60-day abrogation period, the Commission considers the period to have begun on August 21, 2002, the date the NASD filed Amendment No. 1.

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>5</sup> 17 CFR 240.19b-4(f)(2).

<sup>6</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>7</sup> 17 CFR 240.19b-4(f)(3).

<sup>8</sup> The Regulatory Fee is described in Section 8(a) of Schedule A to the NASD By-Laws.

<sup>9</sup> The Personnel Assessment and Gross Income Assessment are described in Section 1 of Schedule A to the NASD By-Laws.

<sup>10</sup> The changes resulting from the proposed restructuring would be revenue neutral.

filings<sup>11</sup> being filed with the Commission as a result of a review of the overall NASD pricing structure,<sup>12</sup> and is intended to address the first two amendments to the NASD pricing restructuring by eliminating the Regulatory Fee and instituting a new transaction-based Trading Activity Fee.

These fees assessed upon and paid by member firms are used by the NASD to fund the NASD's member regulatory activities, including the supervision and regulation of members through examinations, processing of membership applications, financial monitoring, policy, rulemaking, interpretative, and enforcement activities. These amendments to this pricing structure are intended to serve the following purposes: (1) Simplify the NASD's fee structure; (2) ensure fairness in the NASD's fee structure by assessing higher fees to those member firms that require more NASD regulatory services; (3) assess a transaction-based fee in a manner that, unlike the Regulatory Fee, does not influence where members choose to execute trades; (4) reduce the cyclical nature of the current NASD fee structure; and (5) eliminate the NASD's reliance on funds generated from the Regulatory Fee on transactions executed through Nasdaq.

The current structure of assessing Regulatory Fees for Nasdaq transactions is no longer appropriate for three reasons. First, Nasdaq is separating from the NASD and registering as a national securities exchange. Second, the current fee structure is out of step with recent changes in the markets, such as the drastic growth in trading volumes, reductions in average trade size, decimalization, and trading no longer remaining exclusive to the listing exchange. Finally, the Regulatory Fee is only assessed against Nasdaq-listed and other transactions that are reported through the Automated Confirmation Transaction ("ACT") system,<sup>13</sup> although these fees are used to support member regulatory activities across all markets. In addition, the NASD is proposing revisions to the NASD By-Laws that are technical in nature to reflect the NASD's change in corporate name. For example, references to "the Association" have

<sup>11</sup> See also Securities Exchange Act Release No. 46417 (August 23, 2002)(SR-NASD-2002-99).

<sup>12</sup> The NASD, in its pricing restructuring review, proposed changes to the Regulatory Fee in *Special Notice To Members 02-09* and requested comments. NASD received a number of comments. In response to those comments, the proposal set forth in *Special Notice to \* \* \**.

<sup>13</sup> This package of filings proposes rule changes to the NASD's Member Regulation fees. It is not related to the recent Nasdaq filing regarding Nasdaq Regulatory Fee. See SR-NASD-2002-61.

<sup>40</sup> 15 U.S.C. 78s(b)(2).

<sup>41</sup> 17 CFR 200.30-3(a)(12).

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

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

been replaced with "NASD" throughout the By-Laws.

The text of the proposed rule change is below. Proposed additions are in italics; proposed deletions are in brackets.

**Schedule A to [the] NASD By-Laws**

Assessments and fees pursuant to the provisions of Article VI of the By-Laws of [the] NASD shall be determined on the following basis.

\* \* \* \* \*

**Section [8] 2—Member Regulation [Transaction] Fees**

[(a) NASD fee on cleared transactions. Each member shall be assessed a transaction charge of \$.0625 per 1,000 shares, with a minimum charge per side of \$.025 and a maximum charge per side of \$.46875 for each over-the-counter transaction with another member of the Association reportable through ACT in which the member acts either as an agent or a principal for the purchase and/or sale of equity securities.]

[(b) SEC transaction fee. Each member shall be assessed a SEC transaction fee. The amount shall be determined by the SEC in accordance with Section 31 of the Act.]

*(a) Recovery of cost of services. NASD shall, in accordance with this section, collect Member Regulation fees that are designed to recover the costs to NASD of the supervision and regulation of members, including performing examinations, processing of membership applications, financial monitoring, policy, rulemaking, interpretive, and enforcement activities. NASD shall periodically review these revenues in conjunction with these costs to determine the applicable rate. NASD shall publish notices of the fees and adjustments to the assessment rates applicable under this section.*

*(b) Each member shall be assessed a Trading Activity Fee for the sale of covered securities.*

*(1) Covered Securities. For purposes of the rule, covered securities shall mean:*

*(i) All exchange registered securities wherever executed (other than bonds, debentures, and other evidence of indebtedness);*

*(ii) All other equity securities traded otherwise than on an exchange; and*

*(iii) All security futures wherever executed.*

*(2) Transactions exempt from the fee. The following shall be exempt from the Trading Activity Fee:*

*options issued by the Options Clearing Corporation) or offered in accordance with an exemption from registration afforded by Section 3(a) or 3(b) thereof, or a rule thereunder;*

*(ii) Transactions by an issuer not involving any public offering within the meaning of Section 4(2) of the Securities Act of 1933;*

*(iii) The purchase or sale of securities pursuant to and in consummation of a tender or exchange offer;*

*(iv) The purchase or sale of securities upon the exercise of a warrant or right (except a put or call), or upon the conversion of a convertible security; and*

*(v) Transactions which are executed outside the United States and are not reported, or required to be reported, to a transaction reporting association as defined in Rule 11Aa3-1 and any approved plan filed thereunder.*

*NASD may exempt other securities and transactions as it deems appropriate.*

*(3) Fee Rates*

*(i) Each member shall pay to NASD a fee per share for each sale of a covered security.*

*(ii) Each member shall pay to NASD a fee per contract for each sale of an option.*

*(iii) Each member shall pay to NASD a fee for each round turn transaction (treated as including one purchase and one sale of a contract of sale for future delivery) of a security future.*

*(4) Reporting of Transactions. Members shall report to NASD the aggregate share, contract, and/or round turn volume of sales of covered securities in a manner as prescribed by NASD from time to time.*

**Section 3—SEC Transaction Fee**

*Each member shall be assessed an SEC transaction fee. The amount shall be determined by the SEC in accordance with Section 31 of the Act.*

**Section [2] 4—Fees**

(a) Each member shall be assessed a fee of \$75.00 for the registration of each branch office, as defined in the By-Laws. Each member shall be assessed an annual fee for each branch office in an amount equal to the lesser of (1) \$75.00 per registered branch, or (2) the product of \$75.00 and the number of registered representatives and registered principals associated with the member at the end of [the Association] NASD's fiscal year.

(b) [The] NASD shall assess each member a fee of:

(1) \$85.00 for each initial Form U-4 filed by the member with [the] NASD for the registration of a representative or principal, except that the following discounts shall apply to the filing of

Forms U-4 to transfer the registration of representatives or principals in connection with acquisition of all or a part of a member's business by another member:

Number of registered personnel transferred	Discount
1,000—1,999 .....	10%
2,000—2,999 .....	20%
3,000—3,999 .....	30%
4,000—4,999 .....	40%
5,000 and over .....	50%

(2) \$40.00 for each initial Form U-5 filed by the member with [the] NASD for the termination of a registered representative or registered principal, plus a late filing fee of \$80.00 if the member fails to file the initial Form U-5 within 30 days after the date of termination;

(3) \$20.00 for each amended Form U-4 or Form U-5 filed by the member with [the] NASD;

(4) No Change.

(5) \$10.00 for each fingerprint card submitted by the member to [the] NASD, plus any other charge that may be imposed by the United States Department of Justice for processing such fingerprint card; and

(6) No Change.

(c) through (k) No Change.

(1)(1) Unless a specific temporary extension of time has been granted, there shall be imposed upon each member required to file reports, as designated by this paragraph, a fee of \$100 for each day that such report is not timely filed. The fee will be assessed for a period not to exceed 10 business days. Requests for such extension of time must be submitted to [the Association] NASD at least three business days prior to the due date; and

(2) through (3) No Change.

\* \* \* \* \*

**Section [3]5—Elimination of Duplicate Assessments and Fees**

No Change to rule language.

\* \* \* \* \*

**Section [4]6—Assessments and Fees for New Members, Resigning Members and Successor Organizations**

(a) The assessment of a firm, which is not a member throughout [the Association] NASD's full calendar year from January 1 to December 31, shall be based upon the number of quarter years of membership. The proration for a new member shall include the quarter year in which the member is admitted to membership. The proration for a member which resigns shall include the quarter year in which the member's

letter of resignation is received in [the Association] NASD's Executive Office.

(b) A member [which] *that* is a successor organization to a previous member or members shall assume the unpaid balance of the assessments of its predecessor or predecessors and its next assessment shall be determined, if applicable, upon the assessment data of its predecessors. Such successor member shall not be required to re-register branch offices and personnel of predecessor members or pay registration fees therefor. Whether a member is the successor organization to a previous member or members shall be determined by [the Association] NASD upon a consideration of the terms and conditions of the particular merger, consolidation, reorganization, or succession. A member [which] *that* has simply acquired the personnel and offices of another member under circumstances [which] *that* do not constitute the member a successor organization shall not be required to assume the unpaid assessments of the other member. Such non-successor member shall be required to re-register the branch offices and personnel acquired from the other member and pay applicable registration fees.

**Section [5]7—Gross Revenue for Assessment Purposes**

No Change to rule language.

**Section [6]8—Fees for Filing Documents Pursuant to the Corporate Financing Rule**

(a) There shall be a fee imposed for the filing of initial documents relating to any offering filed with [the] NASD pursuant to the Corporate Financing Rule equal to \$500 plus .01% of the proposed maximum aggregate offering price or other applicable value of all securities registered on an SEC registration statement or included on any other type of offering document (where not filed with the SEC), but shall not exceed \$30,500. The amount of filing fee may be rounded to the nearest dollar.

(b) There shall be an additional fee imposed for the filing of any amendment or other change to the documents initially filed with [the] NASD pursuant to the Corporate Financing Rule equal to .01% of the net increase in the maximum aggregate offering price or other applicable value of all securities registered on an SEC registration statement, or any related Rule 462(b) registration statement, or reflected on any Rule 430A prospectus, or included on any other type of offering document. However, the aggregate of all filing fees paid in connection with an

SEC registration statement or other type of offering document shall not exceed \$30,500.

**Section [7]9—Service Charge for Processing Extension of Time Requests**

(a) No Change.

(b) The service charge for processing each initial extension of time request and for all subsequent extension of time requests (1) Involving the same transaction under Regulation T and/or (2) involving an extension of time previously granted pursuant to Rule 15c3-3(n) shall be \$2.00; provided, however, that the service charge shall be \$1.00 for extension of time requests filed electronically by members using [the Association] NASD's Automated Regulatory Reporting System.

\* \* \* \* \*

**Section [9]10—Subscription Charges for Firm Access Query System (FAQS)**

No Change to rule language.

**Section [10]11—Request for Data and Publications**

No Change to rule language.

**Section [11]12—Reserved**

No Change to rule language.

\* \* \* \* \*

**Section [12]13—Application and Annual Fees for Member Firms with Statutorily Disqualified Individuals**

(a) Any member firm seeking to employ or continuing to employ as an associated person any individual who is subject to a disqualification from association with a member as set forth in Article III, Section 4 of [the Association] NASD's By-Laws shall, upon the filing of an application pursuant to Article III, Section 3, paragraph (d) of [the Association] NASD's By-Laws, pay to [the Association] NASD a fee of \$1,500.00. Any member firm whose application filed pursuant to Article III, Section 3, paragraph (d) of [the Association] NASD's By-Laws results in a full hearing for eligibility in [the Association] NASD pursuant to the Rule 9640 Series, shall pay to [the Association] NASD an additional fee of \$2,500.00.

(b) Any member firm continuing to employ as an associated person any individual subject to disqualification from association with a member as set forth in Article III, Section 4 of [the Association] NASD's By-Laws shall pay annually to [the Association] NASD a fee of \$1,500.00 when such person or individual is classified as a Tier 1 statutorily disqualified individual, and a fee of \$1,000.00 when such person or

individual is classified as a Tier 2 statutorily disqualified individual.

**Section [13]14—Review Charge for Advertisement, Sales Literature, and Other Such Material filed or Submitted**

There shall be a review charge for each and every item of advertisement, sales literature, and other such material, whether in printed, video or other form, filed with or submitted to [the Association] NASD, except for items that are filed or submitted in response to a written request from [the Association] NASD's Advertising Regulation Department issued pursuant to the spot check procedures set forth in [the Association] NASD's Rules as follows: (1) for printed material reviewed, \$75.00, plus \$10.00 for each page reviewed in excess of 10 pages; and (2) for video or audio media, \$75.00, plus \$10.00 per minute for each minute of tape reviewed in excess of 10 minutes.

Where a member requests expedited review of material submitted to the Advertising Regulation Department there shall be a review charge of \$500.00 per item plus \$25 for each page reviewed in excess of 10 pages. Expedited review shall be completed within three business days, not including the date the item is received by the Advertising Regulation Department, unless a shorter or longer period is agreed to by the Advertising Regulation Department. The Advertising Regulation Department may, in its sole discretion, refuse requests for expedited review.

\* \* \* \* \*

**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 NASD 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 Item IV below. The Association 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**

The Regulatory Fee, Personnel Assessment and Gross Income Assessment are currently used to fund NASD's member regulatory activities,

including the supervision and regulation of members through examinations, processing of membership applications, financial monitoring, policy, rulemaking, interpretive, and enforcement activities. This fee structure has become outdated, given the separation of NASD from Nasdaq, market developments, and market conditions. The proposed changes are revenue neutral and strive to better align NASD's Member Regulation fees with its functions, efforts, and costs.

The amendments to this pricing structure are intended to serve the following purposes: (1) Simplify NASD's fee structure; (2) ensure fairness in NASD's fee structure by assessing higher fees to those member firms that drive regulatory costs; (3) assess a transaction-based fee in a manner that, unlike the Regulatory Fee, does not influence where members choose to execute trades; (4) reduce the cyclical nature of the current NASD fee structure; and (5) eliminate NASD's reliance on funds generated from the Regulatory Fee on transactions executed through Nasdaq.

The NASD's membership population varies greatly with regard to factors that drive the cost of required regulation. Historically, member regulatory fees were derived primarily from industry revenues and Nasdaq transactions, while the NASD derived minimal fees from the registration of member firm personnel. One key priority during the review process is to link the costs of regulating NASD member firms to the fees generated by the member firms. The costs to regulate member firms include funding for examinations, processing of membership applications, financial monitoring, policy, rulemaking, interpretive, and enforcement activities.<sup>14</sup> The proposed amendments to the fee structure should result in a direct link of the cost of regulating a member firm to the fees assessed to and paid by that member firm. Therefore, as before, the three critical factors used to measure regulatory cost for NASD member firms are overall size of the member firm, level of trading activity and number of registered representatives. However, the weight from each as well as the benchmark used to measure industry revenues and transactions has been shifted under the proposed amendments to better link the fees assessed under these factors with NASD's costs. This proposal will

maintain the current amount of fees received by NASD overall but promotes a more equitable method for assessing fees, thereby creating a level playing field.

*Trading Activity Fee.* The NASD currently assesses a Regulatory Fee upon its members, through approximately 250 clearing and self-clearing firms, on all transactions reported through Nasdaq's ACT system. This fee is only assessed against Nasdaq and other over-the-counter transactions, although the revenues are used to support member regulatory activities across all markets. The Regulatory Fee as assessed also has become a factor in determining upon which market members choose to execute trades. NASD, by its fee assessment, should not promote or disadvantage one trading venue over alternative trading venues. Therefore, the proposed rule change would eliminate the existing Nasdaq market-based Regulatory Fee and would institute a transaction-based Trading Activity Fee similar to the SEC's Section 31 Fee. The proposed fee would be assessed on the sell-side of all member transactions in all covered securities regardless of where the trade is executed.

The NASD anticipates that revenue from the collection of the Trading Activity fee will be reduced by approximately 50%. To offset the reduction in the Trading Activity Fee, the NASD filed SR-NASD-2002-99, which increases the rates for the Personnel Assessment. This increase will result in making the Personnel Assessment a more appropriate base to measure the cost of regulating member firms and fund member regulatory activities.

*Phase-In.* The NASD's overall proposal will be revenue neutral to the NASD. However, due to the link of revenues to regulatory services provided, there will be impacts, both negative and positive, on individual member firms. To minimize the impact on member firms, the restructuring of fees will be phased in over a three-year period. Specifically, for the Trading Activity Fee, since the revenue generated from this fee would be reduced by approximately 50%, the fee reduction will be phased in at a rate of 33% in Year 1, 67% in Year 2 and 100% in Year 3.

## 2. Statutory Basis

The NASD believes that the proposed rule change is consistent with the Act, including section 15A(b)(5) of the Act,<sup>15</sup> which requires, among other things, that

the NASD's rules provide 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 Trading Activity fee is objectively allocated to NASD members. Moreover, the level of the fee is reasonable because it relates to the recovery of the costs of supervising and regulating members.

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

The NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

## 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 on the current proposal.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The portion of the proposed rule change regarding fees has become effective pursuant to section 19(b)(3)(A)(ii) of the Act<sup>16</sup> and subparagraph (f)(2) of Rule 19b-4 thereunder,<sup>17</sup> because the proposal establishes or changes a due, fee, or other charge. The NASD will not implement this rule change until October 1, 2002.

The portion of the proposed rule change regarding the corporate name change to the NASD is effective pursuant to section 19(b)(3)(A)(iii) of the Act,<sup>18</sup> and Rule 19b-4(f)(3) thereunder,<sup>19</sup> because it is concerned solely with the administration of the NASD.

At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making

<sup>14</sup> The NASD's member regulatory revenues have funded its costs on average within 5% over the past five years. In years where shortfalls occurred, prices were not increased. In years where overage occurred, rebates were given to Members.

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

<sup>16</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>17</sup> 17 CFR 240.19b-4(f)(3).

<sup>18</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>19</sup> 17 CFR 240.19b-4(f)(3).

written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. 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 inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to file number SR-NASD-2002-98 and should be submitted by September 20, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>20</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

[FR Doc. 02-22217 Filed 8-29-02; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46411; File No. SR-NASD-2002-92]

### Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving Proposed Rule Change Relating to the Establishment of Day and Good-Till-Cancelled Order Designations for Non-Directed Orders in the Nasdaq SuperMontage

August 23, 2002.

#### I. Introduction

On July 1, 2002, the National Association of Securities Dealers, Inc. ("NASD" or "Association"), through its subsidiary, the Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("SEC" or "Commission"), 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> a proposed rule change to establish "Good-till-Cancelled" ("GTC") and "Day" designations for Non-Directed Orders and clarify the processing of such orders when held in Nasdaq's future Order Display and Collector Facility

("SuperMontage"). The proposed rule change was published for comment in the **Federal Register** on July 5, 2002.<sup>3</sup> The Commission did not receive any comment letters regarding the proposal. This order approves the proposed rule change.

#### II. Description of the Proposed Rule Change

Nasdaq proposes to establish Day and GTC order designations for Non-Directed Orders in SuperMontage. Under the proposal, a Day order would be held in SuperMontage for potential display and/or execution (unless cancelled by the entering party) until the 4:00 p.m. Eastern Standard Time ("EST") Nasdaq market close. At the market close, the order, if not fully executed, would be removed from the system and returned to the entering party. A GTC order would be held in the SuperMontage for potential display and/or execution (unless cancelled by the entering party) for up to one year. At the market close of the one-year anniversary date, the order, if not fully executed, would be removed from the Nasdaq system and returned to the entering party. If this anniversary date fell on a date when the Nasdaq market was closed, the GTC order would be purged after the close of the next business day.

Market makers, Electronic Communication Networks ("ECNs"), and Unlisted Trading Privileges Exchanges (collectively "Quoting Market Participants") could designate a non-directed limit order as Day, GTC, or Immediate or Cancel ("IOC"). If a Quoting Market Participant entered a non-directed limit order without a designation, such an order would be designated as IOC, the system's default designation.<sup>4</sup>

Under the proposal, whenever a Non-Directed Order designated as Day or GTC is entered into the system, it would receive a time stamp to be used in determining the order's price/time priority consistent with the current SuperMontage rules.<sup>5</sup> Day and GTC

<sup>3</sup> See Securities Exchange Act Release No. 46155 (July 1, 2002), 67 FR 44914.

<sup>4</sup> An IOC order if not immediately executed is canceled from the system and returned to the order entry participant.

<sup>5</sup> As contemplated, SuperMontage will have four distinct time periods over the course of the trading day: (1) The Pre-Market Session (7:30 a.m. to 9:29:29 a.m. EST), (2) the Pre-Open Unlocking/Uncrossing Process (9:29:30 a.m. to 9:29:59 a.m. EST), (3) Normal Market Hours (9:30 a.m. to 4:00 p.m. EST), and (4) the After-Hours Session (4:00 p.m. to 6:30 p.m. EST). See Securities Exchange Act Release No. 46410, (August 23, 2002) (approving amendments to SuperMontage Pre-Market Session including the Pre-Open Unlocking/Uncrossing Process) and File No. NASD-2002-114 (extending the Nasdaq After-Hours Pilot to SuperMontage).

orders would be executed pursuant to the execution algorithm selected (price/time (default), price/time taking into account access fees, and price/size/time) by the entering market participant.<sup>6</sup> Day orders could be entered into SuperMontage during the Pre-Market Session through Normal Market Hours. GTC orders could be entered into SuperMontage during the Pre-Market Session through the After Hours Session. Day and GTC orders would be eligible for execution during the Nasdaq Unlocking/Uncrossing Session (beginning at 9:29:30 a.m. EST) throughout the Normal Market Hours (ending at 4:00 p.m. EST). At the close of Normal Market Hours, unexecuted Day orders would expire and be returned to the entering participant. GTC orders that are not executed or cancelled would continue residing in the system at the close of Normal Market Hours, however, such orders would not be eligible for execution through the Non-Directed Order process during the Nasdaq After-Hours Session. Thus, after the 4:00 p.m. EST market close, GTC orders residing in the system would not be eligible for execution through the Non-Directed Order process until the following business day at 9:29:30 a.m. EST.

To clarify that the SuperMontage will accept, retain, display, and execute orders at multiple price levels, Nasdaq also proposed to remove the term "marketable" from the text of Rule 4706(a)(1)(B).

#### III. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.<sup>7</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 15A.<sup>8</sup> Specifically, the Commission finds that the proposed rule change is consistent with section 15A(b)(6) of the Act because it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principals of trade, to foster cooperation

<sup>6</sup> If a Non-Directed Order is entered by a Market Maker or ECN, SuperMontage will, before sending it to a Quoting Market Participant, first attempt to match the order off against the entering party's own quote/order, if that quote/order is at the best price in Nasdaq. See Rule 4710(b)(1)(B)(iv)(a). Parties entering Non-Directed Orders also have an option to preference such orders to a particular market participant. See Rule 4710(b)(1)(B)(iv)(b).

<sup>7</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>8</sup> 15 U.S.C. 78o-3.

<sup>20</sup> 17 CFR 200.30-3(a)(12).

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

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