

establishing clear procedures to coordinate communication among Plan Participants before and during the instance of a trading halt; and (4) clarifying procedures for the resumption of trading after a trading halt.

## V. Conclusion

*It is therefore ordered*, pursuant to Section 11A of the Act<sup>20</sup> and paragraph (c)(2) of Rule 11Aa3-2<sup>21</sup> thereunder, that Amendment 13C to the Plan be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>22</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-50376]

### Order Granting Exemption to National Association of Securities Dealers, Inc. From Certain Reporting Requirements Under Section 31 of the Exchange Act

September 14, 2004.

## I. Introduction

Section 36 of the Securities Exchange Act of 1934 (“Exchange Act”)<sup>1</sup> authorizes the Securities and Exchange Commission (“Commission”)—by rule, regulation, or order—to conditionally or unconditionally exempt any person, security, transaction (or any class or classes of persons, securities, or transactions) from any provision or provisions of the Exchange Act or any rule or regulation thereunder, to the extent such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors. By this Order, the Commission is exempting the National Association of Securities Dealers, Inc. (“NASD”) from certain reporting requirements, described below, that are imposed by Rules 31 and 31T and Form R31,<sup>2</sup> which implement Section 31 of the Exchange Act.<sup>3</sup>

## II. Background

Section 31, among other things, requires NASD to pay the Commission fees based on the aggregate dollar amount of certain sales of securities. Rules 31 and 31T and Form R31 established a procedure for the calculation and collection of Section 31 fees on the “covered sales” of NASD and the national securities exchanges.<sup>4</sup> Paragraph (b)(1) of Rule 31 requires NASD to submit a completed Form R31 for each month by the tenth business day of the following month. NASD must provide on Form R31 the aggregate dollar amount of its covered sales having a “charge date”<sup>5</sup> in the month of the report. The first Form R31 required by Rule 31 covers the month of July 2004 and was due on August 13, 2004. Paragraph (b) of temporary Rule 31T requires NASD to submit a completed Form R31 for each of the months September 2003 to June 2004, inclusive; these forms also were due on August 13, 2004. Based on the data provided by NASD, the Commission will calculate the amount of Section 31 fees owed and send a bill to NASD.

For NASD, the charge date for most covered sales is the trade date (rather than the settlement date).<sup>6</sup> NASD has requested, however, that it be permitted to use a charge date other than the trade date for certain covered sales that are reported on an “as-of” basis.<sup>7</sup> NASD rules generally require its members, during normal market hours, to report securities transactions within 90 seconds after execution. There are situations in which a member fails to report a transaction on the trade date during normal market hours, although NASD trade reporting systems were open, and the member was obligated to do so within 90 seconds. These trades are reported as “as-of” trades.<sup>8</sup> NASD

<sup>4</sup> For NASD, a covered sale is the sale of a security (other than an exempt sale or a sale of a security future) that occurs by or through any NASD member otherwise than on a national securities exchange, if the security is registered on a national securities exchange or is subject to prompt last sale reporting pursuant to NASD rules. See 15 U.S.C. 78ee(c); 17 CFR 240.31(a)(6).

<sup>5</sup> The charge date is the date on which a covered sale occurs for purposes of determining the liability of a national securities exchange or national securities association pursuant to Section 31 of the Exchange Act. See 17 CFR 240.31(a)(3).

<sup>6</sup> The only covered sales for which NASD does not incur liability based on the trade date are those resulting from the exercise of options that are not listed or registered on a national securities exchange, in which case the charge date is the exercise date. See 17 CFR 240.31(a)(3)(ii).

<sup>7</sup> See letter from Marc Menchel, Executive Vice President and General Counsel, NASD, to Margaret McFarland, Deputy Secretary, Commission, dated August 11, 2004.

<sup>8</sup> An “as-of” trade is a trade that is reported to NASD after the date that the actual trade occurred.

considers such “as-of” trades to be late and in violation of NASD rules.<sup>9</sup> An “as-of” report also could result when a trade is executed when NASD trade reporting systems are not open. The trade, therefore, must be reported on the next business day when NASD systems re-open. NASD trade reporting rules allow for the next-day reporting of these transactions; NASD does not consider these trades to be reported late or in violation of NASD rules. NASD reviewed the “as-of” trades reported by its members over a selected period and found that, during the review period, the percentage of trades reported “as-of” was relatively consistent on a month-to-month basis, and the vast majority of “as-of” trades were reported to NASD in the same month that the trades occurred.<sup>10</sup>

NASD has stated that it considered making adjustments to its internal systems to track “as-of” covered sales by trade date but determined that it could not do so prior to August 13, 2004. Even if NASD could make these changes, another problem would arise: a previously submitted Form R31 would be rendered inaccurate if an “as-of” trade were reported in a month different from the month in which the trade was actually effected.<sup>11</sup> Therefore, NASD has requested relief to be permitted to report “as-of” covered sales based on the report date rather than the trade date, as would otherwise be required.

NASD also has requested relief from the requirement, for the months September 2003 to June 2004, to report on Form R31 covered sales with a price substantially unrelated to the current market price.<sup>12</sup> Rules 31 and 31T and Form R31 require NASD to include the aggregate dollar amount of such “away-from-the-market” covered sales in Part III of its Form R31. NASD’s rules<sup>13</sup> currently do not require members to report such trades to the Automated Confirmation Transaction Service

<sup>9</sup> See NASD Rules 4632, 4642, 5430, 6420, 6550, 6620, and related interpretive material.

<sup>10</sup> See letter from Patrice M. Gliniecki, Senior Vice President and Deputy General Counsel, NASD, to Margaret McFarland, Deputy Secretary, Commission, dated August 18, 2004. NASD also found that, during the review period, the number of “as-of” trades represented a *de minimus* percentage of the total number of trades.

<sup>11</sup> For instance, assume that an “as-of” covered sale is effected in July 2004 but not reported to NASD until December 2004. In the absence of this Section 36 exemption, the July 2004 Form R31 would no longer contain an accurate tabulation of NASD’s aggregate dollar amount of covered sales for that month.

<sup>12</sup> See letter from Marc Menchel, Executive Vice President and General Counsel, NASD, to Annette L. Nazareth, Director, Division of Market Regulation, Commission, dated August 5, 2004.

<sup>13</sup> See NASD Rules 4632(e)(5), 4642(e)(4), 6420(e)(5), and 6920(e)(2).

<sup>20</sup> 15 U.S.C. 78k-1.

<sup>21</sup> 17 CFR 240.11Aa3-2(c)(2).

<sup>22</sup> 17 CFR 200.30-3(a)(27).

<sup>1</sup> 15 U.S.C. 78mm.

<sup>2</sup> 17 CFR 240.31, 240.31T, and 249.11. The Commission established Rules 31 and 31T and Form R31 in June 2004. See Securities Exchange Act Release No. 49928 (June 28, 2004), 69 FR 41060 (July 7, 2004) (“Rule 31 Adopting Release”).

<sup>3</sup> 15 U.S.C. 78ee.

(“ACT”).<sup>14</sup> Because away-from-the-market covered sales are not captured in ACT, the only way that NASD could obtain data on them would be to require its members to report them manually.

Presently, NASD does not require its members to manually report data on away-from-the-market covered sales, and NASD members do not have practices and procedures in place for collecting such data. NASD argues that, in the absence of such practices and procedures and in light of an earlier Commission interpretation with respect to away-from-the-market covered sales,<sup>15</sup> requesting historical information from NASD member firms on away-from-the-market covered sales for the period from September 2003 to June 2004—which would enable NASD to carry out its reporting obligations under temporary Rule 31T—would be unduly burdensome. NASD believes that the number of away-from-the-market covered sales is *de minimis*, while the cost associated with requiring all member firms to search for such historical data would be high. Therefore, NASD has requested relief from the obligation imposed by Rule 31T to report the aggregate dollar amount of away-from-the-market covered sales on its Form R31 submissions for the months September 2003 to June 2004.

With respect to its ongoing obligations under Rule 31, NASD has represented that it will promptly amend its “self-reporting” form<sup>16</sup> to solicit information from NASD member firms on away-

from-the-market covered sales prospectively. However, NASD has stated that its members would not be able to provide data on away-from-the-market covered sales for the July 2004 reporting period before August 13, 2004. NASD has represented, however, that it will report away-from-the-market covered sales occurring in July 2004 on its August 2004 Form R31.<sup>17</sup> Therefore, NASD also has requested relief from the obligation to report the aggregate dollar amount of its away-from-the-market covered sales occurring in July 2004 in its Form R31 for that month, and instead to report such covered sales along with its August 2004 Part III covered sales in its August 2004 Form R31.

### III. Discussion

After careful consideration, the Commission believes that exercising its exemptive authority under Section 36 of the Exchange Act to grant NASD the relief it has requested is necessary or appropriate in the public interest and consistent with the protection of investors.

As discussed below, the Commission believes that, in view of the structure of the over-the-counter (“OTC”) markets, using the report date rather than the trade date for “as-of” covered sales is a practical solution that should have no net impact on the Commission’s ability to collect the appropriate amount of Section 31 fees from NASD. While some OTC trading occurs through NASD’s facilities (such as the Nasdaq Stock Market), other trading activity results from direct negotiation between NASD members or their customers. NASD must rely on its members to report these trades in a timely fashion. While the Commission expects NASD to zealously enforce its trade reporting rules to minimize the instances of late reporting by members, sometimes late reporting will occur.

Based on the NASD representations noted above, the Commission believes that, in most instances, using the report date rather than the trade date as the charge date of these “as-of” covered sales will not affect the aggregate dollar amount of NASD’s covered sales reported on Form R31 in a given month.<sup>18</sup> In the limited circumstances when the trade date and the report date

are not in the same month, the aggregate dollar amounts of covered sales reported by NASD in the affected months will change, but the Commission will still collect the same amount of Section 31 fees unless there is a fee rate change in the intervening period.<sup>19</sup> Furthermore, the Commission believes that, in the very limited circumstances when a fee rate change occurs between the trade date and the report date, allowing NASD to report “as-of” trades using report date should not materially affect the amount of Section 31 fees that the Commission collects.<sup>20</sup> On this basis, the Commission believes that granting NASD’s request for an exemption with respect to “as-of” covered sales is necessary or appropriate in the public interest and consistent with the protection of investors.

With respect to away-from-the-market covered sales, NASD previously has not obtained data on such trades, and NASD members do not have practices and procedures to provide NASD with such data. The Commission believes that, based on NASD’s representations,<sup>21</sup> the minimal aggregate dollar amount of such covered sales—and the correspondingly limited Section 31 fees on such covered sales—does not justify the substantial cost of collecting the historical data from NASD (through its members). Therefore, the Commission believes that granting NASD’s request for relief from the requirements of Rules 31 and 31T and Form R31 with respect to away-from-the-market covered sales occurring between September 2003 and June 2004 is necessary or appropriate in the public interest and consistent with the protection of investors. The Commission further believes that reporting July 2004 away-from-the-market covered sales along with NASD’s August 2004 data is a practical solution. NASD will have additional time to obtain this information from its members, and the delayed reporting of one month’s worth of this data will not

<sup>14</sup> ACT is the automated system owned and operated by the Nasdaq Stock Market which compares trade information entered by ACT participants and submits “locked-in” trades to National Securities Clearing Corporation for clearance and settlement; transmits reports of the transactions automatically to the National Trade Reporting System, if required, for dissemination to the public and the industry; and provides participants with monitoring and risk management capabilities to facilitate participation in a “locked-in” trading environment. See NASD Rule 6110(d). ACT is a “trade reporting system” as defined in Rule 31(a)(18). 17 CFR 240.31(a)(18).

<sup>15</sup> In a 1996 release wherein the Commission adopted amendments to prior Rule 31-1 under the Exchange Act, the Commission stated that “no transaction fee will arise from transactions where the buyer and the seller have agreed to trade at a price substantially unrelated to the current market price for the securities, e.g., to enable the seller to make a gift.” Securities Exchange Act Release No. 38073 (December 23, 1996), 61 FR 68590, 68592 n.27 (December 30, 1996).

<sup>16</sup> NASD currently uses this form to collect data from its members on covered sales that: (1) occur in odd lots (*i.e.*, for less than 100 shares), where the trade is not captured by ACT; or (2) result from the exercise of non-exchange-traded options that settle by physical delivery of the underlying securities.

Because these two types of covered sales are not captured in a trade reporting system, NASD must include the aggregate dollar amount of such trades in Part III of Form R31.

<sup>17</sup> The August 2004 Form R31 is due to the Commission by September 15, 2004, the tenth business day of September.

<sup>18</sup> For example, assume that an OTC covered sale is effected on May 3 but is reported “as-of” to NASD on May 13 and there is no fee rate change in the intervening period. The Commission will collect exactly the same amount of Section 31 fees from NASD because NASD’s aggregate dollar amount of covered sales for the month of May is unchanged.

<sup>19</sup> For example, assume that the covered sale occurs on May 13 but is reported “as-of” to NASD on June 13 and that no fee rate change occurs in the intervening period. Although the dollar amount of this “as-of” covered sale will be included in the June rather than the May Form R31 figures, the fees due in the billing period will be unchanged because May and June are in the same billing period. See 17 CFR 240.31(a)(2).

<sup>20</sup> NASD has reported that, in a sample period, the number of “as-of” trades reported to ACT is relatively consistent on a month-to-month basis. Therefore, the “as-of” covered sales that are “lost” to a future period where a different fee rate applies (*i.e.*, the trade is effected in the current period but the “as-of” report to NASD is not made until the next period) should be roughly offset by the “as-of” trades “gained” from a previous period (*i.e.*, the trade was effected in a prior period but was reported to NASD “as-of” in the current period).

<sup>21</sup> See *supra* note 12.

affect the amount of Section 31 fees that NASD will owe the Commission.<sup>22</sup> Therefore, the Commission believes that granting NASD's request for relief from the requirements of Rules 31 and 31T and Form R31 with respect to away-from-the-market covered sales occurring in July 2004 is necessary or appropriate in the public interest and consistent with the protection of investors. After August 2004, NASD must report away-from-the-market covered sales occurring in a given month in the Form R31 due by the tenth business day of the following month, as required by Rule 31.

#### IV. Conclusion

It is hereby ordered, pursuant to section 36 of the Exchange Act, that NASD: (1) May use the report date rather than the trade date as the charge date of any covered sale reported to NASD "as-of"; (2) is not required to include in its Form R31 submissions for the months September 2003 to July 2004, inclusive, the aggregate dollar amount of any away-from-the-market covered sales; and (3) may report in its August 2004 Form R31 the aggregate dollar amount of away-from-the-market covered sales that occurred in July 2004 and August 2004.

By the Commission.

**Margaret H. McFarland,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-50399; File No. SR-DTC-2004-09]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Amending the By-Laws of The Depository Trust Company

September 16, 2004.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> notice is hereby given that on September 7, 2004, the Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change described in items I, II, and III below, which items have been prepared primarily by DTC. The Commission is publishing this notice to solicit

comments on the proposed rule change from interested parties.

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

The proposed rule change consists of changes to the By-Laws of The Depository Trust Company ("DTC") to provide for indemnity for non-director members of DTC board committees.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, DTC 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. DTC has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.<sup>2</sup>

##### (A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In order to help assure the fair representation of the users of DTC, the DTC board of directors has delegated significant responsibilities to the DTC Equity Operations and Planning Committee, the DTC Fixed Income Operations and Planning Committee, and the DTC Membership and Risk Management Committee and has appointed to these committees, in addition to directors, non-director DTC-user representatives.<sup>3</sup>

The purpose of the proposed rule change is to revise DTC's By-Laws to specify that non-director members of DTC board committees will be indemnified in the same manner as DTC directors and officers.

DTC believes that the proposed rule change is consistent with the requirements of section 17A of the Act<sup>4</sup> and the rules and regulations thereunder applicable to DTC because the proposed change strengthens DTC's board committee structure and thereby helps DTC provide its participants with

<sup>2</sup> The Commission has modified the text of the summaries prepared by DTC.

<sup>3</sup> The changes to the DTC By-Laws are modeled on the current indemnification provisions contained in the By-Laws of both the Fixed Income Clearing Corporation and Emerging Markets Clearing Corporation. The National Securities Clearing Corporation has filed a proposed rule change similar to this proposed rule change. Securities Exchange Act Release No. 50398 (September 16, 2004) (File No. SR-NSCC-2004-05).

<sup>4</sup> 15 U.S.C. 78q-1.

fair representation in the administration of its affairs.

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

DTC perceives no impact on competition by reason of the proposed rule change.

##### (C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Written comments from DTC participants or others have not been solicited or received on the proposed rule change.

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

The foregoing rule change has become effective upon filing pursuant to section 19(b)(3)(A)(iii) of the Act<sup>5</sup> and Rule 19b-4(f)(3)<sup>6</sup> thereunder because the proposed rule is concerned solely with the administration of DTC. At any time within 60 days of the filing of such 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 proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>) or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-DTC-2004-09 on the subject line.

##### Paper Comments

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609.

All submissions should refer to File Number SR-DTC-2004-09. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use

<sup>5</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>6</sup> 17 CFR 240.19b-4(f)(3).

<sup>22</sup> July 2004 and August 2004 are in the same billing period and the same fee rate applies to covered sales occurring in these months.

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