



# The Security Traders Association of New York, Inc.

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May 31, 2007

Nancy M. Morris  
Secretary  
Securities and Exchange Commission  
100 F. Street, NE  
Washington, DC 20549-2001

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**RE: Release No. 34-55717; File No. SR-NASD-2007-029  
National Association of Securities Dealers, Inc., Notice of Filing of Proposed Rule  
Change Relating to Access Fee Display Requirements for the OTCBB**

Dear Ms. Morris:

The Security Traders Association of New York, Inc. ("STANY")<sup>1</sup> appreciates the opportunity to comment on Release No 34-55717 filed with the Securities and Exchange Commission ("SEC" or "the Commission") by the National Association of Securities Dealers, Inc. ("NASD"). The filing reflects the NASD's proposed change to NASD Rule 6540 (c) to allow a participating ATS or ECN to not display its access fee in its published quotation on the OTC Bulletin Board ("OTCBB") if the fee is \$0.003 per share or less for a published quotations that is \$1.00 or greater and less than 0.3% of the published quotation on a per share basis if the published quotation is less than \$1.00.<sup>2</sup> STANY is opposed to the rule change and respectfully requests that the Commission reject the NASD's proposal.

STANY's current position is consistent with its long-standing position on the subject of access fees. STANY has repeatedly opposed non-subscriber access fees and has spoken out about the unfair advantage created by these fees for a select group of market participants. We have consistently argued for the elimination of these fees and the leveling of the playing field for market participants, both in the National Market System ("NMS") and OTCBB. STANY has also supported the principles of transparency in pricing and has maintained that, to the extent that a market participant is permitted to charge non-subscriber access fees, those fees should be reflected in published quotations.

Specifically, in a letter submitted to the Commission dated January 24, 2006, STANY opposed the elimination of the access fee display requirement in NASD Rule 6540 (c)<sup>3</sup> noting that non-disclosure of access fees in the OTCBB would reduce market transparency, mislead the public investor and other market participants concerning price, and have a significant impact on the cost of lower priced securities traded on the OTCBB. We noted that ECN access fees distort pricing so that a displayed price is not the true price, artificially narrow spreads and lead to a rise in locked and crossed markets.

<sup>1</sup> The Security Traders Association of New York, Inc. (STANY), established in 1937, represents the shared interests of over 1,500 trading professionals from over 200 firms in New York, New Jersey and Southern Connecticut. STANY is the largest Affiliate of The Security Traders Association (STA). STANY's membership includes individuals employed by order execution facilities, national securities exchanges, national securities associations, ECNs, buy and sell-side trading firms, and national and international banks.

<sup>2</sup> Securities Exchange Act Release No. 55717 (May 7, 2007); 72 FR 26856 (May 11, 2007).

<sup>3</sup> Securities Exchange Act Release No. 53024 (December 27, 2005); 71 FR 159 (January 3, 2006). Amendment 2 to Securities Exchange Act Release No. 52280 (August 17, 2005); 70 FR 49959 (August 25, 2005).

STANY also voiced its objection to the un-level playing field among market participants created by permitting ECNs and ATSS to charge these fees in the first instance.

**Undisclosed access fees are inappropriate in the OTCBB market, as the OTCBB operates without certain protections found in Regulation NMS.**

In proposing the elimination of the access fee display requirement, the NASD appears to be applying standards adopted by the Commission in Reg. NMS to the OTCBB- specifically that provision of Reg. NMS which permits market participants to charge non-subscriber access fees on NMS securities without reflecting those fees in their quotes. The NASD is, however, attempting to apply only one component of Reg NMS to the OTCBB without regard to the significant differences between the NMS and the OTCBB.

An access fee is really nothing more than an agency commission. Historically, and as is now the case in the OTCBB, broker-dealers are only permitted to charge commissions to customers. When broker-dealers execute orders with other firms (not their customer), they can only charge their customer. Firms charge various commission rates, with some firms charging higher commissions than others. If customers do not think that the amount of the commission is appropriate for the level of service they are being provided, they will shift their business to a competitor. A non-subscriber access fee allows an ECN to extract agency commissions from non-customers. A non-customer will only pay such commissions if forced to do so by regulation. The Commission allowed ECNs to charge access fees in Reg NMS in deference to the development of their business models created over many years, but added protections to ameliorate the anti-competitive effect of these fees. No ECN has a business model in the OTCBB that depends on the collection of access fees, and there is no good reason to permit this anti-competitive practice at this late date.

Securities in the OTCBB trade differently than those in the NMS. The OTCBB is less automated than the NMS and is not subject to the safeguards addressed by the Commission in Reg. NMS. The OTCBB operates without a limit order display rule, with no rules relating to locked and crossed markets, and without an order protection rule.

These safeguards were implemented in order to correct disruptive behavior that had developed in the market for NMS securities, such as locked/crossed markets, rebate trading, high ECN access costs, and lack of transparency. To eliminate the access fee display requirement in the OTCBB without simultaneously dealing with such issues would invite disruptive behavior in the OCT market. The Commission has itself acknowledged the issues involved in access fees, and many of the changes in Reg NMS were designed to correct the harm caused by access fees. For example, through Reg. NMS the Commission has required each SRO to promulgate rules that would discourage market participants from engaging in locking and crossing markets. No such protection applies to the OTCBB. Without such protections, market participants may be inclined to intentionally lock markets in order to gain economic benefits. STANY is also concerned with potential gaming and other abuses which could result from the non-disclosure of non-subscriber access fees. Without the added protections that are available in the NMS, we strongly oppose the NASD's proposal to permit quotations with non-disclosed fees in the OTCBB market.

Furthermore, in addressing the issue of non-subscriber access fees in Reg. NMS securities, the Commission (while declining to eliminate these fees) "leveled the field" and specifically allowed all market participants to charge for access to their quotations. The instant proposal makes no such provision and would clearly advantage the ATS and ECN business models over business models of other market participants. Currently, neither market makers nor ECNs and ATSS that participate in the OTCBB charge non-subscriber fees for access to their published quotes. Allowing ECNs and ATSS the exclusive right to charge access fees is anti-competitive and would only lead to those problems that the Commission acknowledged and attempted to resolve through Reg. NMS.

Permitting all market participants to charge access fees in the OTCBB is one way to address this anti-competitive issue. STANY appreciated the Commission's efforts to see this unfair competitive advantage eliminated in the NMS market and to the extent that access fees are charged to non-subscribers in the OTCBB, we believe that all market participants should have the same right to levy these charges.

Rather than encouraging non-subscriber access fees in the OTCBB across all market participants, we believe that no market participant in the OTCBB should be permitted to charge these fees. The levying and collection of access fees by all market participants ultimately result in a net neutral revenue position for most firms. However, the costs of billing and collection impose a transaction cost on the system that benefits no one and ultimately ends up being passed along to investors in higher commission rates. We cannot conceive of any benefit that will be realized by the investing public by introducing access fees into the market for OTC equity securities. Currently, no ECN or ATS charges access fees in the OTCBB. However, if charging non-subscriber access fees becomes the practice in the OTCBB, it is imperative that those fees be disclosed and reflected. Failure to require the posting of those fees will result in misleading quotations.

**Amendment of NASD Rule 6450 (c) is not required or warranted.**

The NASD withdrew its proposal to restrict sub-penny pricing in the OTCBB in April of this year. Without the restriction in sub-penny pricing, the perceived need to repeal the display requirement in NASD Rule 6540 (c)<sup>4</sup> ceased to exist and the NASD withdrew that proposal as well. Although nothing has changed in the OTCBB market, in May 2007, the NASD filed a new proposal to amend NASD Rule 6540 (c).

The NASD's articulated reasons for supporting the proposal to amend NASD Rule 6450 (c)- that the operation of the rule conflicts with NASD Rules 2320 (g) (2) which requires members, that display priced quotations for the same non-exchange listed securities in two or more quotation mediums with real time updates, to display the same priced quotations in each medium and that ECNs and ATSS that charge access fees to non-subscribers will be required to submit two trade reports- do not raise any new issues or concerns that would require the amendment.

NASD Rule 2320 (g) (2) had been in place for two years prior to the adoption of NASD Rule 6540 (c). At the time of the adoption of NASD Rule 6540 (c), the Commission directed the NASD to address how transactions involving posted quotes of ECNs or ATSS on the OTCBB would be handled for purposes of reporting, clearing and confirmation. Rather than amend NASD Rule 6450 (c), the NASD should, as intended by the Commission, address reporting, clearing and confirmation issues directly.

STANY does not agree that requiring ECNs and ATSS to include access fees in their quotes away from their own systems, while showing quotes without fees for the same securities in a system available to subscribers would result in confusion about pricing. Subscribers to ECNs and ATSS know that they will not be accessed fees. It would, however, be misleading and confusing to the investing public and other market participants required to pay fees, to show quotes without those fees. It is clear that elimination of the access fee display requirement in the OTCBB is inconsistent with the Commission's emphasis on clearer disclosure of transaction costs and conflicts of interest. We agree that it is in the best interests of public customers, as well as all market participants, that it be easy to gauge true transaction costs. Eliminating the access fee display requirement in OTC Equity Securities would obscure, as opposed to illuminate, transaction costs associated with OTCBB securities.

Finally, the argument made by ArcaEdge<sup>5</sup> that there are two different prices, depending on whether the transaction is made with a customer or a market participant is inapposite. The fact is that customers of every firm pay for the services of the firm they use to execute their orders. This is how it should be, and firms compete on the basis of speed, cost, capacity and other factors. A firm has no reason to improve its services to non-customers because business from non-customers is artificially generated by regulation or some other factor unrelated to competition. Customers pay for a firm's services, in this and other industries, while non-customers do not. Competition favors firms that provide the best mix of services to investors.

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<sup>4</sup> In Securities Exchange Act Release No. 52280 (August 17, 2005); 70 FR 49959 (August 25, 2005) the NASD proposed restricting sub-penny quotations in the OTCBB. In a comment letter, Archipelago Trading Services, Inc. (ArcaEdge), noted that restricting sub-penny quotations would conflict with the requirements that ATSS and ECNs reflect their non-subscriber access fees in their quotes as provided by in NASD Rule 6540 (c). In response to this comment letter, the NASD filed Amendment 2 to the proposal seeking to delete the display requirement in Rule 6540 (c). See, Securities Exchange Act Release No. 53024 (December 27, 2005); 71 FR 159 (January 2, 2006)

<sup>5</sup> See letter from Andrew B. Stevens and Greg O'Connor, dated February 12, 2007.

Access fees permit ECNs to extract fees from non-customers. There is no reason why a non-customer should pay a fee to an ECN, or any other firm. Non-customers will pay such fees only when forced to do so by regulation, which is what this proposal would facilitate. Because ECNs obtain such fees by regulation, rather than competition, they have no incentive to improve their services to non-customers. Access fees promote the ECN business model without providing any corresponding benefits to the market or the investing public.

### **Conclusion**

Securities on the OTCBB trade according to different rules than those applicable to the NMS. We urge the Commission to be mindful of these differences when considering the NASD's proposal to amend NASD Rule 6540 (c) to allow participating ATSS or ECNs to not display their access fees in their published quotations on the

OTCBB of the fee is \$0.003 per share or less for published quotations under \$1.00 or greater and less than 0.3% of the published quotation on a per share basis if the published quotation is less than \$1.00. Our concern for the integrity of the markets and for transparency in pricing causes us to respectfully request that the Commission reject the NASD's proposal. We believe that the possible negative consequences attendant to passage of this proposal, such as a rise in the incidence of locked and crossed markets, an increased possibility of gaming and the potential loss of customer confidence that could result from confusing and/or hidden pricing far outweigh any perceived or stated benefits to the rule amendment. Moreover, we do not believe that the NASD has demonstrated a need for the proposed rule change and suggest that there are other, less harmful ways in which to address the issues that appear to concern the NASD.

STANY respectfully urges the Commission to reject the proposal. We appreciate the opportunity to provide our opinions and comments. Should the Commissioners or Commission staff have any questions about STANY's position, we hope that they do not hesitate to call upon us.

Respectfully submitted,

Stephen Kay  
President

Kimberly Unger, Esq.  
Executive Director

cc: The Honorable Christopher Cox, Chairman  
The Honorable Paul S. Atkins, Commissioner  
The Honorable Roel C. Campos, Commissioner  
The Honorable Annette L. Nazareth, Commissioner  
The Honorable Kathleen L. Casey, Commissioner  
Erik R. Sirri, Director, Division of Market Regulation, SEC  
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