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June 1, 2007

Via Electronic Mail (rule-comments@sec.gov)

Ms. Nancy M. Morris
Secretary
Office of the Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: File Number SR-NASD-2007-029

Dear Ms. Morris:

The Security Trader's Association ("STA") welcomes the opportunity to comment on the National Association of Securities Dealers, Inc.'s ("NASD") proposal to amend NASD Rule 6540(c) to exclude from the access fee display requirements access fees below a specified level. Specifically, the NASD proposes 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 \$1.00.¹ For the reasons discussed below, we respectfully oppose the proposal and request that the Commission reject it.

The STA is a worldwide professional trade organization that works to improve the ethics, business standards and working environment for our members. There are approximately 5,200 members, all engaged in the buying, selling, and trading of securities. Members participate in STA through 27 national and international affiliate organizations and represent the interests of the trading community and institutional investors. The STA provides a forum for our traders, representing institutions, broker-dealers, ECNs, and floor brokers to share their unique perspectives on issues facing the securities markets. They work together to promote their shared interest in efficient, liquid markets as well as in investor protection.

¹ Securities Exchange Act Release No. 55717 (May 7, 2007); 72 FR 26856 (May 11, 2007).

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Procedural History

NASD Proposal to Restrict Sub-Penny Quoting in the OTCBB and Repeal NASD Rule 6540(c).

On July 28, 2005, the NASD proposed to amend NASD Rule 6750 to prohibit NASD members from displaying, ranking, or accepting a bid or offer, an order, or an indication of interest in any non-Nasdaq OTC equity securities in any quotation medium priced in an increment smaller than \$0.01 if such bid or offer, order, or indication of interest is priced equal to or greater than \$1.00 per share.¹ Only two comment letters were submitted in response to the proposal.²

On December 27, 2005, the NASD, based on a comment from Archipelago Trading Services, Inc. ("ArcaEdge")³ that the proposed rule would conflict with NASD Rule 6540(c) which requires alternative trading systems and electronic communications networks to reflect non-subscriber access or post-transaction fees in their posted quote in the OTCBB, filed Amendment No. 2 to the proposal that sought to delete the text of NASD Rule 6540(c).⁴

But for a subsequent comment letter filed by ArcaEdge in support of the proposal,⁵ all submitted comment letters universally urged the SEC to reject the proposal.⁶ The comment letters urged rejection for the following reasons:

¹ Securities Exchange Act Release No. 52280 (August 17, 2005); 70 FR 49959 (August 25, 2005).

² Letter from Kevin J. P. O'Hara, Chief Administrative Officer and General Counsel, Archipelago Trading Services, Inc., to Nancy M. Morris, Secretary, Commission, dated September 23, 2005 ("ArcaEdge I Letter"); Letter from Phylis M. Esposito, Executive Vice President, Chief Strategy Officer, Ameritrade, Inc., to Nancy M. Morris, Secretary, Commission, dated October 31, 2005 ("Ameritrade I Letter").

³ ArcaEdge I Letter.

⁴ Securities Exchange Act Release No. 53024 (December 27, 2005); 71 FR 159 (January 3, 2006).

⁵ Letter from Andrew B. Stevens, Assistant General Counsel, NYSE Group, Inc and Greg O'Connor, Director of Compliance, Archipelago Trading Services, Inc., to Nancy M. Morris, Secretary, Commission, dated February 14, 2007 ("ArcaEdge II Letter")

⁶; Letter from Julian Rainero, on behalf of Pershing LLC, to Nancy M. Morris, Secretary, Commission, dated March 6, 2006; Letter from Patrick E. Brake, Jr., General Counsel, Hill, Thompson, Magid & Co., Inc., to Nancy M. Morris, Secretary, Commission, dated February 21, 2006; Letter from Jerry O'Connell, Chairman, Trading Committee, Securities Industry Association, to Nancy M. Morris, Secretary, Commission, dated February 17, 2006; Letter from William Yancey, Chairman, and John C.

- There are no Regulation NMS safeguards in the OTCBB marketplace that would allow for a Regulation NMS type access fee solution including, but not limited to, prohibitions against locking or crossing the market, sub-penny pricing, limit order display and fair access requirements.
- Repeal of NASD rule 6450(c) would result in an unlevel playing field in the OTCBB market, that allowed only an ECN/ ATS to charge access fees to non-subscribers and not display that fee in their posted quotes on the OTCBB (the NASD's current proposal would cause the same problem but does not address this issue).
- Non-disclosure of access fees would reduce market transparency and integrity (the NASD's current proposal would cause the same problem but does not address this issue).
- The charging of access fees has a more significant effect on lower priced securities as those traded in the OTCBB.⁷
- Elimination of this requirement would distort the time/price auction with undue parity given to an inferior net price
- Non-disclosure of access fees would mislead public investors and other market participants that ECN/ATS and market maker quotations were the same when the ECN/ATS quotation is inferior.

NASD Withdraws Proposal to Restrict Sub-Penny Pricing in the OTCBB and Repeal NASD Rule 6549(c) and Files New Proposal to Amend NASD Rule 6540(c).

Giese, President and Chief Executive Officer, Security Traders Association, to Nancy M. Morris, Secretary, Commission, dated February 8, 2006; Letter from R. Cromwell Coulson, Chief Executive Officer, Pink Sheets LLC, to Nancy M. Morris, Secretary, Commission, dated January 26, 2006; Letter from Phylis M. Esposito, Executive Vice President, Chief Strategy Officer, Ameritrade, Inc., to Nancy M. Morris, Secretary, Commission, dated January 24, 2006; Letter from Leonard J. Amoruso, Knight Capital Group, Inc., to Nancy M. Morris, Secretary, Commission, dated January 24, 2006; Letter from Michael Santucci, President, Kimberly Unger, Executive Director, and Stephen J. Nelson, Co-Chair, Security Traders Association of New York, Inc., to Nancy M. Morris, Secretary, Commission, dated January 24, 2006; Letter from Phylis M. Esposito, Executive Vice President, Chief Strategy Officer, Ameritrade, Inc., to Nancy M. Morris, Secretary, Commission, dated October 31, 2005;

⁷ See, Letter from Leonard J. Amoruso, Knight Capital Group, Inc., to Nancy M. Morris, Secretary, Commission, dated January 24, 2006

On April 20, 2007 the NASD withdrew its proposed rule change relating to restrictions on sub-penny quoting in OTC equity securities. The NASD has not re-proposed a rule change restricting sub-penny quoting in OTC equity securities and, as a result, the original impetus for repealing and/or amending NASD Rule 6540(c), the conflict between restricting sub-penny quoting and NASD Rule 6540(c), is no longer an issue that requires a change to NASD Rule 6540(c).

On May 7, 2007, the SEC sought public comment on the instant rule proposal to allow a participating ATS or ECN to not display its access fee in its published quotation on the OTC Bulletin Board 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

The Arguments Submitted by the NASD in Support of its Proposal do not Require the Amendment of NASD Rule 6540(c).

The NASD has put forth two reasons in support of its proposal to change NASD Rule 6450(c). First, the NASD argues that the operation of NASD Rule 6540(c) conflicts with NASD Rule 2320(g)(2) which requires a member that displays priced quotations for the same non-exchange listed security in two or more quotation mediums that permit updates on a real-time basis to display the same priced quotation in each system. Second, because the ECN/ATS executes its subscriber order without an access fee and transactions with a non-subscriber with an access fee, two trade reports would be required where once only one was because the transactions at different prices would make them ineligible for riskless principal transaction reporting.

These Arguments do not Raise new Concerns

The reasoning put forth by the NASD does not raise new issues or concerns. At the time that NASD Rule 6540(c) was adopted, NASD Rule 2320(g)(2) had been on the books for two years. Moreover, the trade reporting issue was addressed by the Commission in the adoption of NASD Rule 6540(c) when it stated **"In addition, the Commission expects that the NASD will address how transactions on the OTCBB that result from the posted quote of an ATS or ECN will be reported, cleared, and confirmed in light of the fact that such quote must include non-subscriber access or post-transaction fees, if any."**⁸ Obviously, the NASD has not yet addressed this issue and the STA respectfully argues that the NASD move forward in a manner consistent with the Commission's previously stated expectations and address how such

⁸ Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. To Allow Electronic Communications Networks and Alternative Trading Systems To Participate in the Over-the-Counter Bulletin Board, Securities Exchange Act Release No. 46916 (May 10, 2002); 67 FR 35171, 35173 (May 17, 2002).

transactions should be reported instead of gutting the current requirements of NASD Rule 6540(c).

Amending NASD Rule 2320(g)(2) Will Address the NASD's Concern About the Publication of Different Quotations in Different Quotation Systems for the Same Security.

The NASD established NASD Rule 2320(g)(2) because it believed that if members displayed differently priced quotations in different quotation mediums for the same security it would be confusing and misleading to other market participants.⁹ We respectfully believe that the publication of quotes inclusive of access fees in the OTCBB while quotes in an ECN/ATS' internal subscriber quotation system do not reflect such fees (or different ones) does not create the potential for confusion contemplated by the NASD and is less misleading to the marketplace. The inclusion of access fees in an ECN/ATS' OTCBB quotation informs public non-subscriber investors and other market participants of the true cost of the transaction. If the fees are not included, a public non-subscriber investor or other market participant could be misled into believing that an ECN/ATS quotation at the inside market is the same cost as another quotation at the inside when, in reality, it is more expensive. Under the current proposal, even if an investor or other market participant suspected that a fee was being charged, they would be unaware of the amount until after the transaction. Further, ECN/ATS subscribers will not be confused by the different quotations as it will confirm their understanding that it may be less expensive to transact business with the ECN/ATS as a subscriber.

Based on the foregoing, the proposed rule would create more confusion and mislead public investors because the actual costs of the transaction will be concealed. Instead of amending NASD Rule 6540(c), we respectfully believe this potential conflict would be better addressed by amending NASD Rule 2320(g)(2) to read as follows:

- (2) Members that display priced quotations on a real-time basis for a non-exchange-listed security in two or more quotation mediums that permit quotation updates on a real-time basis must display the same priced quotations for the security in each medium, **except when required by NASD Rule 6540(c).**

Amending NASD 2320(g)(2) in this manner will remove any conflict with NASD Rule 6540(c) and at the same time ensure and maintain market transparency and integrity.

⁹ In 2004, the NASD repealed a similar rule regarding Nasdaq securities because it was no longer needed, given the market structure and regulation for such securities. Notice of Filing of Proposed Rule Change by the National Association of Securities Dealers, Inc. to repeal Rule 4613A(e)(1) Requiring Same-Priced Quotations on Multiple Markets," 69 FR 5632, (February 5, 2004); Security Exchange Act Release No. 49152 (January 29, 2004). We believe the reason the NASD has maintained NASD Rule 2320(g)(2) is a recognition of, as discussed in this letter, the OTCBB marketplace lacks the protections of a Reg NMS marketplace.

The NASD's Transaction Reporting Concerns Should Have Been Addressed at the Time NASD Rule 6540(c) was Adopted and They can be Addressed now without Amending NASD Rule 6540(c).

The second reason put forward by the NASD to support its proposal is a trade reporting issue that the Commission expected the NASD to address when NASD Rule 6540(c) was adopted five years ago. The NASD's failure to address this issue since that time is not a reason to gut a rule that is so important to the maintenance of transparency and market integrity in the OTCBB. The NASD can address this issue in several ways. First, for OTC Equity Securities it could amend the definition of riskless principal transaction to recognize this situation. This could be accomplished by adding a parenthetical after the statement that both legs of the transaction must be executed at the same price that reads "except when required by NASD Rule 6540(c)." This would allow such transactions to be reported as riskless principal transactions requiring only one trade report. If for some reason, the definition could not be amended, the NASD could create a new trade reporting modifier identifying this type of transaction and allowing for only one trade report.

ArcaEdge's Argument That Regulation NMS' Solution for the Access Fee Issue Should Apply to the OTCBB is Misguided and Ignores Differences Between the Markets That Would Threaten Investor Protection

The other reasons ArcaEdge raised in support of its argument that NASD Rule 6540(c) be repealed was that Reg NMS has dealt with the access fees issue and that it had requested of the Commission when NASD Rule 6540(c) was adopted that when the access fees issue was resolved in the Nasdaq market that the same resolution be applied to the OTCBB.

In the current proposal, the NASD does not address this issue (although it relies on the access fee limits stated in Rule 610(c) of Regulation NMS for the disclosure limits in its proposal) and does not (other than a concern about excessive fees) address any of the concerns raised in the above referenced comment letters submitted to the Commission regarding its proposal to repeal NASD Rule 6540(c) such as the potential for increased locked and crossed markets, rebate trading and other efforts to game the market.

The STA Has Consistently Opposed Access Fees

First, the STA has been consistent in its argument against access fees.¹⁰ Previously, the STA has stated that the principle of transparency in quotes has a direct bearing on market

¹⁰ See Letter from William Yancey, Chairman, and John C. Giese, President and Chief Executive Officer, Security Traders Association, to Nancy M. Morris, Secretary, Commission, dated February 8, 2006; STA Letter- to the Honorable William Donaldson, Chairman, Securities and Exchange Commission Re: ECN Access Fees, from John Giese, President, STA, April 16, 2003; STA Special Report: Fulfilling the Promise of the National Market System, Recommendation 3, p. 8.; STA Comment- on Regulation NMS (SEC File No. S7-10-04), June 30, 2004; See STA Letter to the Honorable William Donaldson, Chairman, Securities and Exchange Commission Re: Amended Regulation NMS (SEC File No. S7-10-04) January 25, 2005.

integrity and the market confidence which flows from such integrity and that failing to display the access fee leads to greater opacity. Equally important in terms of transparency is that the failure to display access fees in OTC quotes will inevitably lead to gaming the system. Simply put, the access fees could conceivably exceed the price quoted on the security itself.

Further, as discussed above and in previous STA Letters, the current proposal will lead to price distortion. When ECNs and market makers are both at the inside market, ECN net prices are inferior to market maker prices by the increment of the access fee. If the fee is not disclosed, market participants, including investors, suffer from the belief that the inside market rather than the net price is the fully disclosed cost. Failure to display fees will create the illusion of ECN and market maker parity, rather than fostering investor trust through full disclosure.

The OTCBB Market Does not Maintain the Same Protections Found in Regulation NMS

ArcaEdge's reliance on Regulation NMS and its resolution of the access fees issue in that market is misplaced. As previously stated, we believe that the circumstances that apply in the trading of non-Nasdaq OTC equity securities are different from Nasdaq and exchange listed equities, and that these securities represent a different class of securities, traded with different legitimate historical and marketplace practices.

First, the OTCBB marketplace does not maintain the myriad of Regulation NMS and other protections that the exchange listed marketplace does. For instance, there is no Limit Order Display Rule, Locked and Crossed Market Prohibition, Sub-Penny prohibition or fair access requirements. The marketplace is much less automated, there are no market-wide electronic execution linkages and order processing generally takes a longer period of time.

Second, the STA is very concerned that the non-disclosure of access fees below the levels stated in the proposal will lead to increased locked and crossed market activity, an activity that is allowable because the OTCBB market, unlike the Regulation NMS market, does not prohibit locked and crossed markets. The proliferation of such activity will mislead public investors, create confusion in the marketplace and have a harmful effect on the integrity of the marketplace.

Regulation NMS resolved the access fees issue by allowing any trading center to charge such fees up to a capped amount. This rule does not apply to the OTCB market and shouldn't because it is a much different marketplace that, as described above, does not operate with all the protections of the National Market System and Regulation NMS. ArcaEdge's request that the resolution in Regulation NMS be applied to the OTCB is shortsighted and does not consider investor protection as a factor. The fact that this resolution would allow market makers to charge such fees does not change this conclusion. Allowing market makers to charge fees may level the playing field, but it does not address the fact that allowing the imposition of undisclosed fees in a market that does not contain the investor protections of the National Market System would be harmful. Allowing market makers to charge such fees would only exacerbate these issues.

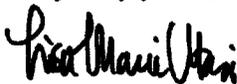
Ms. Nancy M. Morris
May 31, 2007
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Conclusion

The STA respectfully believes that, as discussed above, the arguments submitted by the NASD in support of its proposal to amend NASD Rule 6540(c) do not warrant the deleterious effects of amending the rule on market transparency, market integrity and investor protection and the concerns raised by those arguments may be easily addressed without amending the rule as proposed. Moreover, the NASD's proposal fails to account for the vast differences between the OTCBB and the Regulation NMS marketplace and the lack of investor and marketplace protection that could be exploited by the imposition of undisclosed access fees. As a result, the STA respectfully requests that the SEC reject the NASD's proposal to amend 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

If we can provide further clarification or further information on this proposal, please do not hesitate to contact us at (212) 867-7002

Very truly yours,



Lisa M. Utasi
Chairman of the Board



John C. Giese
President and CEO

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
Robert L.D. Colby, Deputy Director, Division of Market Regulation, SEC
Brian Cartwright, General Counsel, Office of General Counsel, SEC

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