

May 30, 2007

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number SR-NASDAQ-2006-065, Proposed Rule Change and Amendments
Nos. 1, 2, and 3 Thereto To Reestablish a Quotation and Trading System for
Securities That Are Designated by The PORTAL[®] Market as PORTAL Securities

Dear Ms. Morris:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates this opportunity to comment on the above-referenced proposed rule change (the “Proposal”) filed by The NASDAQ Stock Market LLC (“Nasdaq”) with the Securities and Exchange Commission (the “SEC” or the “Commission”).

The Proposal would reestablish a quotation and trading system for certain PORTAL-designated securities (“PORTAL Securities”).² Nasdaq notes that PORTAL Securities are effectively limited to securities initially sold to qualified institutional buyers (“QIBs”) pursuant to Rule 144A (“Rule 144A”) under the Securities Act of 1933, as amended (the “Securities Act”).³ Under the Proposal, the contemplated quotation and trading system (“PORTAL System”) would permit certain brokers (“PORTAL Brokers”) and dealers (“PORTAL Dealers”) to post one- or two- sided indicative quotations and indications of interest, and negotiate and execute trades with respect to PORTAL Securities. Indicative quotations and indications of interest, as well as trade report information, would be available to all PORTAL Brokers and Dealers and certain qualified institutions buyers (“PORTAL Qualified Investors”) who sign subscriber agreements. Participation on the PORTAL System would be voluntary.

Nasdaq states that the Proposal is meant to provide “greater market transparency in PORTAL [S]ecurities in the form of centralized quotations and last sale trade information.”⁴ However, SIFMA believes that the Proposal is vague and incomplete in a number of significant

¹ The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA’s mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public’s trust and confidence in the markets and the industry. SIFMA works to represent its members’ interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

² Securities Exchange Act of 1934, as amended (“Exchange Act”) Release No. 34-55669, 72 F.R. 23874 (May 1, 2007).

³ Proposal, 72 F.R. at 23876.

⁴ Proposal, 72 F.R. at 23876.

areas, including, among other things: reporting of information to TRACE and the OTC Reporting Facility; the information to be disseminated to PORTAL Brokers, Dealers and Qualified Investors (collectively, "PORTAL Participants"); regulatory jurisdiction; and the nature of subscriber agreements and other documents that Nasdaq will require of PORTAL Participants. SIFMA respectfully urges the Commission not to approve the Proposal until these matters are clarified and such clarifications are published for further public comment.

Trade Reporting

The Proposal is unclear regarding, among other things, the trades that will be reported to TRACE and the OTC Reporting Facility, who will be responsible for providing the information which will be submitted and when such information will need to be provided to PORTAL.

SIFMA requests that Nasdaq clarify the types of trades that will be reported to TRACE and the OTC Reporting Facility. The Proposal states that "*PORTAL-negotiated trades* will be submitted through the PORTAL System to TRACE and the OTC Reporting Facility."⁵ Does Nasdaq intend to furnish to TRACE and the OTC Reporting Facility details of trades that are negotiated on the PORTAL System, even if not consummated on the PORTAL System?⁶ For instance, would Nasdaq report a trade as to which some negotiation took place on PORTAL but that was subsequently executed by parties outside of the PORTAL System?

In addition, SIFMA requests that Nasdaq clarify how information will be reported to TRACE and the OTC Reporting Facility, and whether trade reporting via the PORTAL System will be mandated or optional. SIFMA notes that the Proposal requires information to be provided "in accordance with applicable self-regulatory organization rules." Thus, only information required by TRACE, in the case of debt securities,⁷ or the OTC Reporting Facility, in the case of equity securities, would be submitted, in the appropriate time periods, to TRACE and the OTC Reporting Facility. How does Nasdaq intend to obtain the information required by such facilities? Will PORTAL Brokers and Dealers be required to provide any additional information beyond that which would be in the PORTAL System by virtue of the negotiation of the trade via the PORTAL System, or will Nasdaq have in the system all of the required data? If PORTAL Brokers and Dealers will be required to provide any information to Nasdaq, when would such information be required to be submitted to Nasdaq, and in what format? In addition, if PORTAL Brokers and Dealers will be providing such information to Nasdaq, will they be given the option to report directly to TRACE and the OTC Reporting Facility, rather than through the PORTAL System? Lastly, SIFMA requests clarification that, to the extent information is submitted to TRACE and the OTC Reporting Facility through the PORTAL System, there will be no additional obligation for a member of the National Association of Securities Dealers (the "NASD") to separately report to TRACE and the OTC Reporting Facility.

⁵ Proposal, 72 F.R. at 23877.

⁶ For example, is Nasdaq intending to report information regarding transactions that are negotiated on the PORTAL System, but subsequently executed over-the-counter?

⁷ Therefore, PORTAL Securities that are not TRACE-eligible under NASD rules will not be reported.

Dissemination of Information

The Proposal states that, among other things, trade report information for trades that are “*negotiated via PORTAL*” will be disseminated in PORTAL to PORTAL Participants, but in the case of debt securities, “would not aggregate or otherwise follow the dissemination protocols applicable to debt trades reported to TRACE.”⁸ SIFMA believes that Nasdaq should first consider whether dissemination of any trade report information regarding PORTAL Securities is necessary or beneficial. SIFMA notes that other trading systems may not distribute trade report information to system participants, or, to the extent actual trade information is distributed, may disseminate on a delayed basis, such as at the end of the day. The PORTAL System provides a significant degree of transparency through the posting of indicative quotes and indications of interest. Through such postings, the PORTAL System provides a forum for information regarding the market. PORTAL Securities, unlike registered securities, generally tend to be less liquid. The dissemination of trade report information to PORTAL Participants provides marginal, if any, additional benefits, and could potentially result in further decreased liquidity as it would reduce the willingness of dealers and their customers to commit capital, and to assume risk positions, in these securities.⁹ It may become more difficult to trade at acceptable prices if parties have immediate access to trading patterns and intentions of market participants, as revealed by actual transaction data.¹⁰ In addition, any trade report information would only be disseminated to sophisticated parties. Such parties by definition have access to a variety of resources and have the ability to independently assess the value of securities.

To the extent that information is to be distributed to PORTAL Participants, SIFMA requests that Nasdaq clarify its statements. SIFMA requests that Nasdaq indicate what trades will be disseminated to PORTAL Participants. Does Nasdaq intend to disseminate to PORTAL Participants trade information regarding trades negotiated via PORTAL, but subsequently executed through another medium, including over the counter? SIFMA believes that such dissemination would be inappropriate, as it is well established that transactions that are executed over the counter are governed by the NASD rules. In addition, what information is intended to be distributed? SIFMA believes that, to the extent any information should be disseminated to PORTAL Participants, no more information than is currently publicly disseminated through TRACE, in the case of debt securities, or the OTC Reporting Facility, in the case of equity securities, should be distributed. Thus, SIFMA believes that at a minimum, as many of these securities are relatively illiquid, volume information regarding the PORTAL Securities should be capped and information regarding certain PORTAL Securities should not be disseminated.¹¹ Furthermore, SIFMA believes that, given the relative illiquidity of the market

⁸ Proposal, 72 F.R. at 23877.

⁹ Dealers and investors in the debt markets commit capital and assume risk positions based upon an expectation that their positions can be traded or unwound at reasonable market levels.

¹⁰ For example, investors in corporate bonds often trade portions of large positions through a series of smaller trades in order to avoid signaling to the market their trading activities. In this situation, the investor would be disadvantaged by the posting of individual trades before the entire position was fully liquidated.

¹¹ TRACE currently provides that the volumes for investment grade securities are capped at \$5 million, and volumes for non-investment grade securities are capped at \$1 million. In addition, TRACE currently does not provide information regarding, among other things, mortgage- or asset-backed securities and collateralized mortgage obligations.

and the sophisticated nature of the investors, it is appropriate to delay the dissemination of any such information.¹²

On a related point, proposed Rule 6511(a) provides that third-party data vendors may have some role in distributing data to PORTAL Participants, but the role of such third-parties, the terms of data distribution and any related costs are not addressed.

SIFMA believes that all aspects of market data distribution are significant, both because these matters affect the liquidity and general operation of the trading markets for these securities, but also because it affects the costs and operations of its members and other broker-dealers and investors.

Regulatory Jurisdiction

The Proposal states that NASD would continue to surveil trade reports in PORTAL Securities that are submitted to TRACE and the OTC Reporting Facility. In addition, Nasdaq's MarketWatch Department will perform real-time surveillance of quoting and trading activity in the PORTAL System. Thus, the Proposal involves a situation in which multiple regulators will have overlapping and potentially inconsistent authority. This is a move in the wrong direction. SIFMA believes that rationalization of SRO oversight functions is beneficial to the market, and that the SEC and the Self-Regulatory Organizations should be working together to avoid duplication of regulatory processes and standards of conduct, encourage specialized knowledge in a particular regulator, and eradicate conflicting claims regarding ownership of market data and duplicative regulatory fees. These same principles are as applicable to the PORTAL market as they are to traditional markets, and SIFMA would encourage Nasdaq, the NASD and the SEC to bring the regulatory jurisdiction over all aspects of this market under a common regulatory umbrella.

One illustration of how overlapping regulators create unnecessary burdens is existing Nasdaq Rule 6531 (which the Proposal would renumber as Rule 6503). This Rule provides that no member may sell a PORTAL security otherwise than in compliance with Rule 144A or some other exemption to registration under the Securities Act and also requires each Nasdaq member to maintain in its files "information demonstrating that the transaction is in compliance with Rule 144A or with any other applicable exemption from registration under the Securities Act." This rule is not limited to transactions on PORTAL or even to PORTAL Participants. Naturally, broker-dealers should be scrupulous in abiding by the registration requirements of the Securities Act, but why is it Nasdaq's role to police and establish recordkeeping requirements for its members' activities which have nothing to do with Nasdaq, other than that Nasdaq may have designated a particular security as a Nasdaq security?¹³

¹² SIFMA recommends that, at a minimum, dissemination be delayed until the end of the day.

¹³ SIFMA notes that Section 6(b)(5) of the Exchange Act precludes a national securities exchange from regulating, by virtue of any authority conferred by the Exchange Act, matters not related to the purposes of the Exchange Act or the administration of the Exchange. SIFMA questions whether existing Nasdaq Rule 6531/proposed Rule 6503 is consistent with this standard. *C.f.*, SR-DTC 2007-04, footnote 6 (registered clearing agency does not have the jurisdiction or power to enforce provisions of the Securities Act).

In a similar vein, one of the most discouraging aspects of the Proposal is that, in order to qualify as a PORTAL Broker or Dealer, a broker-dealer will need to be a member of Nasdaq.¹⁴ Formerly, when PORTAL was a facility of the NASD, membership would not have presented issues, since virtually all SEC-registered broker-dealers are NASD members. It is not clear, however, that most of the broker-dealers who are active in the trading of Rule 144A securities are members of Nasdaq. Joining and maintaining membership in a new SRO is costly and burdensome. It would be regrettable (and perhaps counterproductive to the success of PORTAL) if the SEC and Nasdaq proceed with the Proposal's insistence on Nasdaq membership as a pre-condition to participation as a PORTAL Broker or Dealer.

A further jurisdictional concern pertains to PORTAL Qualified Investors. In proposed Rule 6513, Nasdaq implies that it has the authority to discipline PORTAL Participants (which, by definition, includes, PORTAL Qualified Investors).¹⁵ Generally, a national securities exchange's authority to sanction a non-member is quite limited, and requires the SEC to issue a rule or order under Section 6(f) of the Exchange Act. Clearly, PORTAL Qualified Investors are not members of Nasdaq (as that term is used in Section 3(a)(3) of the Exchange Act). Accordingly, Nasdaq should either clarify the scope of its authority over PORTAL Qualified Investors under proposed Rule 6513 or seek an SEC order or rulemaking under Section 6(f) of the Exchange Act.

Finally, SIFMA notes the proposed Rules are vague regarding the extent to which PORTAL Qualified Investors, who are not necessarily broker-dealers or persons associated with them, are permitted to access directly (other than through a member) the facilities of PORTAL. Specifically, although the descriptive portion of the Proposal appears to limit the ability of PORTAL Qualified Investors to directly post indicative quotations and indications of interest, and *implies* that quotations may only be accessed by a PORTAL Qualified Investor through a PORTAL Broker or Dealer, the proposed Rules, themselves, do not make clear whether or how a PORTAL Qualified Investor may directly execute or negotiate directly through PORTAL. PORTAL is now a facility of a national securities exchange.¹⁶ Although SIFMA is mindful of the restrictions on PORTAL Qualified Investors, SIFMA believes that Nasdaq should, when responding to these comments, specifically address the extent to which PORTAL Qualified Investors may directly access the trading and negotiation functionality of the PORTAL system, and, to the extent that such direct access is permitted, explain the legal rationale for such direct access by non-broker-dealers. SIFMA also notes that some trading platforms have permitted participants to access certain quotes only if such participants are given permission to access quotes by the particular broker or dealer posting such quotes.

¹⁴ See proposed Rule 6505.

¹⁵ See proposed Rule 6501(k). SIFMA notes that the potential sanctions appear to go beyond termination of participation (which is otherwise addressed in proposed Rule 6507).

¹⁶ Historically, direct participation on national securities exchanges by persons other than broker-dealers and their associated persons has been limited in part by the operation of Sections 6(b)(2) and 6(d) of the Exchange Act, which effectively restrict exchange *membership* to broker-dealers and their associated persons.

Subscriber Agreements

SIFMA notes that the Proposal requires PORTAL Dealers, Brokers and Qualified Investors to enter into subscriber agreements¹⁷ and (in the case of PORTAL Dealers and Brokers) possibly other documents or agreements.¹⁸ The Proposal does not contain information regarding the provisions of the subscriber agreements or other documents, including any representations, covenants, indemnities or other terms. SIFMA believes that subscriber agreements, applications and other documents upon which participation is conditioned are material, and that such documents should be made available for public consideration, comment and review before approval of the Proposal by the Commission.

Compliance with the Exchange Act

The Proposal states that Nasdaq is seeking an exemption from registration under Sections 12(g) and 12(b) of the Exchange Act. Securing such exemptions are mandatory in order for brokers and dealers to participate on the PORTAL System. In addition, the Proposal also states that Nasdaq is seeking exemptive relief in respect of Rule 15c2-11 of the Exchange Act. Given their significance, SIFMA requests that Nasdaq make its exemptive request letters available publicly for comment before the Commission issues any exemptive relief or approves the Proposal so that SIFMA and its members can review the legal analysis and policy basis for the requests and consider whether there are any precedential or other considerations. SIFMA also notes that, to the extent the Commission grants any such relief, other organizations may wish make similar requests. Furthermore, SIFMA requests confirmation that Nasdaq intends to receive an exemption from Rule 15c2-11 of the Exchange Act prior to the time that the PORTAL's proposed new functionality will be operational. Failure to achieve an exemption will likely hamper use of the PORTAL System.

Separately, SIFMA notes that Section 12(g) of the Exchange Act requires issuers to file with the Commission a registration statement to register equity securities (which would include PORTAL Securities that are equity) if a class of equity securities are held of record by more than the number of persons specified by Section 12(g) of the Exchange Act. SIFMA requests that Nasdaq state if it intends to monitor and limit the number of holders of PORTAL Securities so as to avoid registration requirements pursuant to Section 12(g) of the Exchange Act and if so, how it intends to accomplish this.

Order Size

The Proposal states that orders in whole shares up to 999,999 shares may be entered into the PORTAL System for normal processing. SIFMA requests that Nasdaq explain the rationale for limiting orders for shares to this number, and in addition, requests that Nasdaq clarify whether any limitations on order sizes for normal processing will be imposed on bonds.

¹⁷ See Proposed Rules 6505(a)(2)(A), 6505(b) and 6506(a)(2)(A), respectively.

¹⁸ See proposed Rule 6505(a)(2)(D) and 6505(b).

Technical Question Regarding Nasdaq's Intention to Remove Certain Securities From PORTAL

The Proposal requires that any applicant submitting a request for PORTAL designation of a security must notify Nasdaq of the submission to the SEC of a Securities Act registration statement that would register securities to be exchanged for a PORTAL Security.¹⁹ Presumably, this is intended to be a trigger for some action by Nasdaq. SIFMA notes that, in many registered exchange offers, a portion of bonds remains untendered. SIFMA requests clarification whether Nasdaq intends to remove all PORTAL Securities that are eligible to be exchanged pursuant to a registered exchange offer and, if so, whether such removal would be effected when the registration statement becomes effective or at some other point in time.

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As discussed above, SIFMA requests clarification on a number of important questions, and believes that such questions should be addressed, and opportunity should be provided for review and comment, before the Proposal is approved.

We appreciate this opportunity to comment on the Proposal. If you have any questions concerning these comments, or would like to discuss these comments further, please feel free to contact me at 646.637.9220 or via email at mkuan@sifma.org.

Sincerely,



Mary Kuan
Managing Director and
Assistant General Counsel

cc: Ms. Katherine England, Assistant Director, Division of Market Regulation,
U.S. Securities and Exchange Commission

Mr. Thomas Moran, Associate Vice President and Associate General Counsel,
The Nasdaq Stock Market

¹⁹ See proposed Rule 6502(a)(3)(A).