

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-50274; File No. SR-NASD-2004-129)

August 26, 2004

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend, and Provide an Interpretation to, Section 3 of Schedule A to NASD By-Laws and Amend NASD's Permanent Self-Reporting Form

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on August 23, 2004, the National Association of Securities Dealers, Inc. ("NASD" or "Exchange") filed with the Securities and Exchange Commission ("SEC" or the "Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by NASD. NASD has designated the proposed rule change as constituting a "non-controversial" rule change pursuant to Rule 19b-4(f)(6) under the Act,³ which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

NASD is proposing to amend Section 3 of Schedule A to NASD By-Laws to remove references to the "SEC." In addition, NASD filed portions of a Notice to Members relating to interpretations of Section 3 of Schedule A to NASD By-Laws. NASD also filed two self-reporting forms that are to be used by members to report trade data that is not captured by NASD's trade reporting systems. The text of the proposed rule change and the self-reporting forms and the relevant portions of the Notice are available at NASD and at the Commission.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 17 CFR 240.19b-4(f)(6).

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

In its filing with the Commission, 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. NASD 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

Section 31 of the Act⁴ requires that NASD, as a national securities association, and the national securities exchanges pay transaction fees and assessments to the Commission that are designed to recover the costs related to the government’s supervision and regulation of the securities markets and securities professionals. On June 28, 2004, the Commission established new procedures governing the calculation, payment, and collection of fees and assessments on securities transactions owed by national securities exchanges and associations to the Commission pursuant to Section 31 of the Act.⁵ The new procedures became effective on August 6, 2004. In accordance with the new procedures, NASD must now provide the Commission with trade data, which the Commission will use to calculate the amount of fees and assessments due by NASD. Accordingly, the calculation of fees and assessments owed by NASD pursuant to Section 31 of the Act will now be performed exclusively by the Commission.

⁴ 15 U.S.C. 78ee.

⁵ See Final Rule Regarding Collection Practices Under Section 31, Securities Exchange Act Release No. 49928 (June 28, 2004), 69 FR 41059 (July 7, 2004) (“Adopting Release”).

To recover the costs of NASD's Section 31 obligation, NASD assesses a transaction fee on its member firms under Section 3 of Schedule A to NASD By-Laws.

In response to the new procedures adopted by the Commission and interpretive guidance provided in the Adopting Release, NASD has filed with the Commission: (1) a proposed rule change to amend Section 3 of Schedule A to NASD By-Laws to remove references to the "SEC"; (2) portions of a forthcoming Notice to Members relating to interpretations of Section 3 of Schedule A; and (3) two self-reporting forms that are to be used by members to report trade data that is not captured by NASD's trade reporting systems.

Pursuant to Section 3 of Schedule A, NASD assesses a transaction fee on its member firms, the amount of which is determined periodically in accordance with Section 31 of the Act, to recover the costs of NASD's Section 31 obligation. The current title of Section 3 of Schedule A is "SEC Transaction Fee," and the text of Section 3 of Schedule A states: "[e]ach member shall be assessed an SEC transaction fee. The amount shall be determined by the SEC in accordance with Section 31 of the Act." The current title and text of Section 3 of Schedule A were filed with the Commission for notice and review in 2002.⁶

NASD is proposing to amend Section 3 of Schedule A in response to statements made by the SEC in its Adopting Release that "it is misleading to suggest that a customer or [a self-regulatory organization] member incurs an obligation to the Commission under Section 31."⁷ While NASD notes that the Commission has previously reviewed Section 3, formerly Section 8,

⁶ See Securities Exchange Act Release No. 46168 (July 8, 2002), 67 FR 46558 (July 15, 2002) (notice of filing and immediate effectiveness of SR-NASD-2002-65); Securities Exchange Act Release No. 47946 (May 30, 2003), 68 FR 34021 (June 6, 2003) (order approving SR-NASD-2002-148).

⁷ See supra note 5 at 41072.

of Schedule A to NASD By-Laws and deemed it to be consistent with the Act,⁸ to avoid any possible confusion as discussed in the Adopting Release, NASD is now amending Section 3 of Schedule A to delete any references to the “SEC”. In addition, in conformity with the Adopting Release, NASD is proposing to refer to the transaction fee as a “Regulatory Transaction Fee” in the title and text of Section 3 of Schedule A. The transaction fee assessed by NASD will continue to be set, as it is today, in accordance with Section 31 of the Act.⁹ Therefore, NASD is not amending the reference to Section 31 in Section 3 of Schedule A to NASD By-Laws.

Though the requirements of Section 31, including the new procedures established by the Commission, apply directly to NASD and the national securities exchanges, and not their membership, the requirements will affect the obligations of member firms under Section 3 of Schedule A to NASD By-Laws. Therefore, NASD is issuing a Notice to Members to inform member firms of the new procedures relating to Section 31 and to remind member firms of their continuing obligation to pay the transaction fees assessed by NASD so that it can recover the costs of its Section 31 obligation. NASD believes that certain provisions in the forthcoming Notice may constitute interpretations of Section 3 of Schedule A to NASD By-Laws that, due to

⁸ See Securities Exchange Act Release No. 38133 (January 7, 1997), 62 FR 1940 (January 14, 1997) (notice of filing and immediate effectiveness of SR-NASD-96-57); Securities Exchange Act Release No. 46168 (July 8, 2002), 67 FR 46558 (July 15, 2002) (notice of filing and immediate effectiveness of SR-NASD-2002-65); Securities Exchange Act Release No. 46416 (August 23, 2002), 67 FR 55901 (August 30, 2002) (notice of filing and immediate effectiveness of SR-NASD-2002-98); Securities Exchange Act Release No. 47946 (May 30, 2003), 68 FR 34021 (June 6, 2003) (order approving SR-NASD-2002-148).

⁹ NASD also is amending Section 3 of Schedule A to NASD By-Laws to reflect that the applicable fee rate assessed by NASD is periodically adjusted in accordance with Section 31. In the past, NASD has notified members, through Member Alerts or other means, of any periodic adjustments to the fee rate made by the Commission. NASD will continue to notify members of any such adjustments in the future since NASD seeks to recover the costs of its Section 31 obligation from its members.

their nature, should be filed as a proposed rule change. The provisions in question relate to: (1) members' obligation to self report securities sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security and where consideration is given for the securities; (2) members' obligation to submit certain self-reporting forms and applicable payments to NASD by certain deadlines; (3) the manner in which members should use rounding to calculate the transaction fees on self-reported trades; and (4) guidance regarding the appropriate terminology when referring to the transaction fees assessed by NASD under Section 3 of Schedule A to NASD By-Laws. The relevant portions of the Notice to Members are available at NASD and at the Commission.

Finally, NASD has revised its Permanent Self-Reporting Form so that going forward members can report covered sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security, with the exception of securities transactions where no consideration is given for the securities. NASD previously had not assessed a transaction fee on such sales because the Commission had stated that transactions where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security were not subject to Section 31 fees.¹⁰ As stated in the Adopting Release, however, the Commission now believes that such securities sales are subject to Section 31 fees where consideration is given for the securities, and, therefore, such covered sales must be

¹⁰ See Final Rule Regarding Securities Transactions Exempt From Transaction Fees, Securities Exchange Act Release No. 38073 (December 23, 1996), 61 FR 68590, 68592 n.27 (December 30, 1996).

reported to the Commission.¹¹ Accordingly, NASD is making conforming changes to the Permanent Self-Reporting Form, and filed the form with the Commission. The Permanent Self-Reporting Form will become effective on October 1, 2004, and members must use this form to report covered sales for the month of September 2004 and for each month thereafter. As discussed below, NASD is using a different self-reporting form for the collection of certain other trade data.

NASD has created an Interim Self-Reporting Form to facilitate the collection of trade data and payments for covered sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security for the months of July and August 2004. The Interim Self-Reporting Form will be used once only in September 2004. Members must use the Interim Self-Reporting Form to report, for the month of August 2004, covered sales in odd-lot transactions, covered sales resulting from the exercise of over-the-counter options that settle by physical delivery, and covered sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security. Members also must use the Interim Self-Reporting Form to report covered sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security for the month of July 2004. NASD must receive the Interim Self-Reporting Form, including any applicable payment,

¹¹ Pursuant to SEC Rule 31T, as written, NASD is obligated to submit trade data on such covered sales for each of the months in the September 2003 to June 2004 period, but NASD has sought an exemption from the SEC with respect to NASD's retroactive reporting obligation. NASD has requested an exemption so that it would not be obligated to report such covered sales on a retroactive basis for the September 2003 to June 2004 period, and it would not be obligated to report to the SEC such covered sales for the month of July 2004 until the September 15, 2004 reporting date.

by September 7, 2004. NASD also filed the Interim Self-Reporting Form with the Commission.

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹² which requires, among other things, that NASD's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed changes to Section 3 of Schedule A to the NASD By-Laws and to the manner by which member firms refer to the fee assessed by NASD when passing it on to their customers is consistent with the protection of investors and the public interest in that it will avoid any confusion by members and their customers. In addition, the proposed rule change, including the portions of the Notice that are intended to assist members in complying with Section 3 of Schedule A to the NASD By-Laws, is consistent with Section 15A(b)(5) of the Act,¹³ which requires, among other things, that 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 that NASD operates or controls.

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

NASD does not believe that the proposed rule change would impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

¹² 15 U.S.C. 78o-3(b)(6).

¹³ 15 U.S.C. 78o-3(b)(5).

C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

NASD has neither solicited nor received written comments on the proposed rule change.

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

The proposed rule change has been filed by NASD as a “non-controversial” rule change pursuant to Section 19(b)(3)(A)(i) of the Act¹⁴ and Rule 19b-4(f)(6) thereunder¹⁵ because it does not:

- (i) significantly affect the protection of investors or the public interest;
- (ii) impose any significant burden on competition; and
- (iii) become operative for 30 days from the date of filing, or such shorter time as the

Commission may designate if consistent with the protection of investors and the public interest; provided that the self-regulatory organization has given the Commission written notice of its intent to file the proposed rule change at least five business days prior to the filing date of the proposed rule change.

NASD has requested that the Commission waive the five-day pre-filing notice requirement and the 30-day pre-operative period, which would make the proposed rule operative immediately.

The Commission believes that it is consistent with the protection of investors and the public interest to waive the five-day pre-filing requirement and the 30-day pre-operative period in this case. Allowing the rule change to become operative immediately will permit NASD to

¹⁴ 15 U.S.C. 78s(b)(3)(A)(i).

¹⁵ 17 CFR 240.19b-4(f)(6).

satisfy its obligation under Section 31 of the Act on a timely basis and will avoid any confusion on the part of NASD members and their customers.¹⁶

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 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. Please include File Number SR-NASD-2004-129 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-NASD-2004-129. 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 only one method. The Commission will post all comments

¹⁶ For the purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 also will be available for inspection and copying at the principal office of NASD. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASD-2004-129 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁷

Margaret H. McFarland
Deputy Secretary

¹⁷ 17 CFR 200.30-3(a)(12).