

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-50084; File No. SR-NASD-2004-103)

July 26, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. to Modify the Methodology for Applying Nasdaq's Pricing Schedule to Affiliated Members

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on June 29, 2004, the National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. On July 21, 2004, Nasdaq filed Amendment No. 1 to the proposed rule change.<sup>3</sup> Nasdaq has designated this proposal as one establishing or changing a due, fee, or other charge imposed by the self-regulatory organization under Section 19(b)(3)(A)(ii) of the Act<sup>4</sup> and Rule 19b-4(f)(2) thereunder,<sup>5</sup> which renders the proposal effective upon filing with the Commission.

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

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Mary M. Dunbar, Vice President and Deputy General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), dated July 19, 2004, and accompanying Form 19b-4 ("Amendment No. 1"). Amendment No. 1 replaced the original filing in its entirety. For purposes of calculating the 60-day abrogation period, the Commission considers the proposal to have been filed on July 21, 2004, the date Nasdaq filed Amendment No. 1. See Rule 19b-4(f)(2), 17 CFR 240.19b-4(f)(2).

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>5</sup> 17 CFR 240.19b-4(f)(2).

The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

Nasdaq proposes to modify its fee schedule by allowing the aggregation of activity of affiliated members, provided that the members have complete identity of common ownership.

Nasdaq plans to implement the proposed rule change on August 1, 2004.

The text of the proposed rule change appears below.<sup>6</sup> Proposed new language is in italics; proposed deletions are in brackets.

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**7020. [Reserved] Aggregation of Activity of Affiliated Members**

(a) For purposes of applying any provision of Rules 7010(c), (d), (f), (g), (i), or (u) that reflects a charge assessed, or credit provided, by Nasdaq, a member may request that Nasdaq aggregate its activity with the activity of its affiliates. A member requesting aggregation of affiliate activity shall be required to certify to Nasdaq the affiliate status of entities whose activity it seeks to aggregate prior to receiving approval for aggregation, and shall be required to inform Nasdaq immediately of any event that causes an entity to cease to be an affiliate. In addition, Nasdaq reserves the right to request information to verify the affiliate status of an entity.

(b) For purposes of applying any provision of Rules 7010(c), (d), (f), (g), (i), or (u) that reflects a charge assessed, or credit provided, by Nasdaq, references to an entity (including

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<sup>6</sup> The proposed rule change is marked to show changes from the rule as it appears in the electronic NASD Manual available at [www.nasd.com](http://www.nasd.com).

references to a “member,” a “participant,” or a “Nasdaq Quoting Market Participant”) shall be deemed to include the entity and its affiliates that have been approved for aggregation.

(c) For purposes of this Rule 7020, the terms set forth below shall have the following meanings:

(1) An “affiliate” of a member shall mean any wholly owned subsidiary, parent, or sister of the member that is also a member.

(2) A “wholly owned subsidiary” shall mean a subsidiary of a member, 100% of whose voting stock or comparable ownership interest is owned by the member, either directly or indirectly through other wholly owned subsidiaries.

(3) A “parent” shall mean an entity that directly or indirectly owns 100% of the voting stock or comparable ownership interest of a member.

(4) A “sister” shall mean an entity, 100% of whose voting stock or comparable ownership interest is owned by a parent that also owns 100% of the voting stock or comparable ownership interest of a member.

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

In its filing with the Commission, Nasdaq 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. Nasdaq 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

Nasdaq's schedule of fees and credits, as reflected in the Rule 7000 Series of the NASD Manual, contains several provisions in which a member using Nasdaq services pays a fee, or receives a credit, that varies based upon its volume of usage. For example, when members use the order execution services of the Nasdaq Market Center, the fees that they pay to access liquidity, and the credits that they receive for providing liquidity, vary based upon the average daily shares of liquidity provided during a month: higher levels of liquidity provision result in lower fees and higher credits.<sup>7</sup> Other examples of volume-based pricing in the current Nasdaq fee schedule include pricing for transactions in exchange-listed stocks traded through the Nasdaq Market Center,<sup>8</sup> Nasdaq Workstation II display charges,<sup>9</sup> and fees for trade reporting.<sup>10</sup> In several prior pricing filings, Nasdaq has stated that although it would aggregate activity associated with multiple market participant identifiers ("MPIDs") used by a member, Nasdaq would not aggregate one corporate entity's activity with activity associated with MPIDs assigned to subsidiaries or other affiliates with a different Central Registration Depository ("CRD") number.<sup>11</sup> However, a particular member may choose to allocate activity across a group of wholly owned subsidiaries or other affiliates, rather than across multiple MPIDs of the same

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<sup>7</sup> See NASD Rule 7010(i).

<sup>8</sup> See NASD Rule 7010(d).

<sup>9</sup> See NASD Rule 7010(f)(1)(A).

<sup>10</sup> See NASD Rule 7010(g).

<sup>11</sup> See, e.g., Securities Exchange Act Release No. 48972 (December 22, 2003), 68 FR 75301 (December 30, 2003) (notice of filing and immediate effectiveness of File No. SR-NASD-2003-185); and Securities Exchange Act Release No. 47661 (April 10, 2003), 68 FR 19045 (April 17, 2003) (notice of filing and immediate effectiveness of File No. SR-NASD-2003-51).

entity. Nasdaq understands that certain of its competitors allow aggregation of affiliate activity when applying their fee schedules.<sup>12</sup> Accordingly, Nasdaq has decided to revise its present policy by adopting a rule to allow aggregation of activity of affiliated members, provided that the members have a complete identity of common ownership. Thus, a member could request that its activity be aggregated with, for example, the activity of a direct wholly owned subsidiary, or an indirect subsidiary that was wholly owned by a direct wholly owned subsidiary.

Any diminution in the level of ownership below 100% of the voting stock or other comparable ownership interest would prevent the member from aggregating its activity with related members, even if a control relationship between the entities still existed. Thus, for example, if one member (“Member A”) owned 90% of the voting stock of a subsidiary member (“Member B”), which in turn owned 100% of the voting stock of another subsidiary member (“Member C”), Members B and C would be eligible for aggregation of their activity with one another, but Member A would not be permitted to aggregate its activity with either Member B or Member C, even though it exercised a control relationship with respect to them. Nasdaq believes that a bright line, set at the 100% level, is necessary to ensure that aggregation can occur without the need for a subjective analysis of the degree of control exercised by one entity over another.

Aggregation of activity could also be requested by a subsidiary with respect to parent corporations and/or sister corporations. Thus, for example, if Member A was wholly owned by Member B, which also owned 100% of Member C, Member A could request that its activity be aggregated with activity of both Members B and C. Finally, it should be noted that not all corporations in an ownership structure would be required to be members for the activity of the members to be aggregated, provided a wholly owned relationship existed among the members in

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<sup>12</sup> See, e.g., <http://www.inetats.com/prodserv/bd/fee/fee.asp>.

the structure. Thus, for example, if a non-member holding company owned 100% of the stock of two members, the activity of the two members could be aggregated.

A member seeking to aggregate activity with that of other members would be required to send an application to Nasdaq informing Nasdaq as to the names and relationships of the entities for which aggregation is requested. In the application, the member would also certify that each entity for which aggregation is requested is, in fact, an affiliate within the meaning of Rule 7020. The member would be required to inform Nasdaq immediately if any entity ceased to be an affiliate.<sup>13</sup> Finally, Nasdaq reserves the right to require members requesting aggregation to provide information to verify the affiliate status of entities (although Nasdaq would not generally require such background information unless it had reason to question a firm's certification).

In applying Nasdaq's schedule of credits and fees, references to an entity (including references to a "member," a "participant," or a "Nasdaq Quoting Market Participant") shall be deemed to include the entity and its affiliates that have been approved for aggregation. Thus, for example, under the fee schedule for order executions of Nasdaq-listed securities through the Nasdaq Market Center, if two members that are affiliates provide an average daily volume of 15 million and 6 million shares of liquidity, respectively, during a month, each member would be entitled to receive a credit of \$0.0025 per share of liquidity provided, rather than the \$0.002 per share that each would currently receive. The activity of affiliated members would also be aggregated when applying Nasdaq's revenue sharing programs.<sup>14</sup> Finally, under NASD Rule

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<sup>13</sup> Nasdaq states that a false certification, or a failure to provide a timely notice that an entity has ceased to be an affiliate, would be deemed a violation of Nasdaq's rules and would be referred to NASD for investigation.

<sup>14</sup> See NASD Rules 7010(c) and (u).

7010(i)(1), a member would not be charged for order executions when its order accesses its own Quote/Order or the Quote/Order of an affiliate.

Volume-based discounts that apply after certain thresholds are passed during the course of a month will be allocated to affiliates based on aggregate usage on an ongoing basis. For example, under NASD Rule 7010(i), there is a \$10,000 per month cap on the \$0.001 per share charge for accessing liquidity from ECNs. Each of two affiliates would pay \$0.001 per share until the \$10,000 cap had been reached by the affiliates in the aggregate; thereafter, each affiliate would pay no fee for the remainder of the month. Volume-based discounts that apply to marginal usage of a service that is provided on a monthly, rather than a daily, basis (e.g., the discount on the monthly fee for Nasdaq Workstation logons in excess of 150 logons) will be allocated to affiliates on a pro rata basis.

## 2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,<sup>15</sup> in general, and with Section 15A(b)(5) of the Act,<sup>16</sup> in particular, in that it provides for the equitable allocation of reasonable dues, fees, and other charges among members and issuers and other persons using any facility or system which the NASD operates or controls. Nasdaq believes the proposed rule change will allow members to receive the benefits of volume-based discounts in Nasdaq's fee schedule when they choose to allocate their activity across a group of wholly owned subsidiaries or other affiliates, rather than across multiple MPIDs of the same member. Accordingly, Nasdaq believes the change will result in a wider availability of the discounts provided by the fee schedule.

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<sup>15</sup> 15 U.S.C. 78q-3.

<sup>16</sup> 15 U.S.C. 78q-3(b)(5).

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

Nasdaq does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

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

Written comments were neither solicited nor received.

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act<sup>17</sup> and subparagraph (f)(2) of Rule 19b-4 thereunder,<sup>18</sup> because it establishes or changes a due, fee, or other charge imposed by the self-regulatory organization. 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.<sup>19</sup>

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

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<sup>17</sup> 15 U.S.C. 78s(b)(3)(a)(ii).

<sup>18</sup> 17 CFR 240.19b-4(f)(2).

<sup>19</sup> For purposes of calculating the 60-day abrogation period, the Commission considers the proposal to have been filed on July 21, 2004, the date Nasdaq filed Amendment No. 1.



- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASD-2004-103 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-2004-103. 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 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 Section, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of the 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-2004-103 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.<sup>20</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>20</sup> 17 CFR 200.30-3(a)(12).