

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-52291; File No. SR-NASD-2005-011)

August 18, 2005

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing of Proposed Rule Change and Amendment Nos. 1, 2, and 3 Thereto to Limit the Eligibility for Quotation on the OTCBB of the Securities of an Issuer That Is Repeatedly Delinquent In Its Periodic Reporting Obligations

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 January 28, 2005, 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. Nasdaq submitted Amendment No. 1 to this filing on May 10, 2005.³ Nasdaq submitted Amendment No. 2 to this filing on June 24, 2005.⁴ Nasdaq submitted Amendment No. 3 to this filing on August 15, 2005.⁵ The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 1, which replaced the original filing in its entirety, clarified the proposed rule text in response to comments received from the Commission staff, clarified how Nasdaq will notify issuers about the proposed rule, and stated that the proposed rule would be implemented for those filings for periods ending on or after June 1, 2005.

⁴ Amendment No. 2, which replaced the original filing and Amendment No. 1 in their entirety, further clarified the proposed rule text in response to comments received from the Commission staff, and set forth in the proposed rule text that filings for reporting periods ending before June 1, 2005 will not be considered under the proposed rule change.

⁵ Amendment No. 3, which supplemented the filing as modified by Amendment No. 2, amended the proposed rule text to provide that filings for reporting periods ending before October 1, 2005 will not be considered under the proposed rule change.

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

Nasdaq proposes to limit the eligibility for quotation on the Over-the-Counter Bulletin Board (“OTCBB”) of the securities of an issuer that is repeatedly late in filing required periodic reports. Nasdaq proposes to implement the proposed rule in connection with filings for reporting periods ending on or after October 1, 2005.⁶

The text of the proposed rule change, as amended, is set forth below. Proposed new language is in *italics*, deletions are in [brackets].

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6530. OTCBB-Eligible Securities

A member shall be permitted to quote the following categories of securities in the Service:

(a) any domestic equity security that satisfies the requirements of subparagraph (1) and either subparagraph (2) or (3) or (4) below:

(1) – (3) No change.

⁶ The Commission notes that the NASD has submitted a proposed rule change (SR-NASD-2005-089), which was published for public comment in the Federal Register on July 29, 2005, that would amend the NASD’s Plan of Allocation and Delegation of Functions by the NASD to Subsidiaries (“Delegation Plan”) and amend several NASD rules with respect to the OTCBB. Currently, the Delegation Plan allocates responsibility for activities related to or in support of the trading in over-the-counter (“OTC”) equity securities, including the OTCBB, to Nasdaq. Under the NASD’s proposal, the NASD would assume direct authority for OTC equity securities, rather than delegate it to Nasdaq. Nasdaq would, however, continue to provide certain operational systems and support to the OTCBB pursuant to contract. See Securities Exchange Act No. 52119 (July 25, 2005), 70 FR 43918 (July 29, 2005) (public notice of File No. SR-NASD-2005-089).

(4) the issuer of the security is a bank or savings association (or a holding company for such an entity) that is not required to file reports with the Commission pursuant to Section 13 or 15(d) of the Act and, subject to a sixty calendar day grace period, the issuer of the security is current with all required filings with its appropriate Federal banking agency or State bank supervisor (as defined in 12 U.S.C. 1813).

(b) – (d) No change.

(e) [Paragraphs (a)(2) and (3) and (4) above will not apply with respect to any domestic equity security quoted in the Service on the effective date of this rule change until six months after that date.] Notwithstanding the foregoing paragraphs, a member shall not be permitted to quote a security if:

(1) while quoted on the OTCBB, the issuer of the security has failed to file a complete required annual or quarterly report by the due date for such report (including, if applicable, any extensions permitted by SEC Rule 12b-25) three times in the prior two-year period; or

(2) the security has been removed from the OTCBB due to the issuer's failure to satisfy paragraph (a)(2), (3) or (4), above, two times in the prior two-year period.

Following the removal of an issuer's securities pursuant to this paragraph (e), such securities shall not be eligible for quotation until the issuer has timely filed in a complete form all required annual and quarterly reports due in a one-year period. For purposes of this paragraph, a report filed within any applicable extensions permitted by SEC Rule 12b-25 will be considered timely

filed. Furthermore, filings for reporting periods ending before October 1, 2005 will not be considered for purposes of this paragraph (e).

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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

In January of 1999, the Commission approved amendments to NASD Rules 6530 and 6540 requiring all issuers of securities quoted on the OTCBB to be current in their filings with the Commission or other appropriate regulator (the “Eligibility Rule”).⁷ When a security becomes ineligible for quoting on the OTCBB due to the Eligibility Rule, either because a filing is not made or because a filing is incomplete,⁸ Nasdaq appends an additional character “E”

⁷ See Securities Exchange Act Release No. 40878 (January 4, 1999), 64 FR 1255 (January 8, 1999) (SR-NASD-98-51). These amendments were fully implemented for all securities quoted on the OTCBB as of June 2000.

⁸ In order for a filing to be complete, it must, for example, contain all required certifications, attestations, and financial statements, including an auditor’s review pursuant to SAS-100 (for quarterly reports) or an unqualified auditor’s opinion (for annual reports). See, e.g., Rule 13a-14 under the Act, 17 CFR 240.13a-14, and Rules 10-01(d) and 2-02(c) of Regulation S-X, 17 CFR 210.10-01(d) and 2-02(c). In addition, the auditor must be registered with the Public Company Accounting Oversight Board. See Section 102(a) of the Sarbanes-Oxley Act of 2002, 15 U.S.C. 7212(a).

designator to the security's symbol.⁹ This identifier notifies investors and other market participants that the issuer is not current in its reporting obligations. If the issuer does not comply within the applicable grace period provided by the Eligibility Rule (typically 30 days),¹⁰ Nasdaq removes the issuer's securities from quotation on the OTCBB. Approximately 80% of issuers achieve compliance within the grace period, while 20% are removed.

Nasdaq reports that it has identified a high level of non-compliance with the Eligibility Rule. Specifically, over the two-year period ended August 31, 2004, Nasdaq identified over 3,000 instances of delinquent or otherwise incomplete filings by 1,806 OTCBB issuers, of which 1,067 were still quoted as of August 31, 2004. Of the 1,806 issuers, 1,035 were late in filing one time, 548 issuers were delinquent twice and 223 were delinquent three or more times. Given this high rate of recidivism, Nasdaq proposes to make certain securities ineligible for quotation on the OTCBB for a period of one year.

First, Nasdaq proposes to make the securities of those OTCBB issuers that are delinquent in a required filing three times in a two-year period ineligible for quotation on the OTCBB for a period of one year.¹¹ Accordingly, the securities of a company would be removed from the

⁹ Nasdaq also appends an "E" to a security's symbol when it fails to receive notice that an issuer, which files with a regulator other than the Commission, has timely filed. In the case of those issuers, the Nasdaq generally receives notice of a regulatory filing from the applicable market maker or the issuer itself, and will investigate any instance where it has not received such notice. See Telephone conversation between Tim Fox, Attorney, Commission, and Arnold Golub, Associate Vice President, Nasdaq on May 20, 2005.

¹⁰ The Eligibility Rule provides a 60-day grace period to banks, savings association and insurance companies that do not file with the Commission, but are required to file with other regulators. See NASD Rule 6530(a)(3) and (4).

¹¹ A filing would not be considered delinquent if made within any applicable extensions permitted pursuant to Rule 12b-25 under the Act. Nasdaq also appends an "E" to a security's symbol when it does not receive notice that an issuer that files with a regulator other than the Commission has timely filed. Nasdaq will not consider such occurrences to be a delinquent filing for purposes of the proposed rule if the issuer did, in fact, timely file with the appropriate regulator. Nonetheless, these issuers can help alleviate confusion by providing Nasdaq with a copy of the filing made with the appropriate regulator on or before its due date.

OTCBB the third time that the company does not file by the due date (including, if applicable, any extensions permitted by Rule 12b-25 under the Act) in a two-year period, without the benefit of any grace period for this third delinquency.¹² In applying the look-back associated with this provision, Nasdaq would consider reports characterized by due dates (including, if applicable, any extensions permitted by Rule 12b-25 under the Act) that fell within the prior two-year period.

Second, Nasdaq also proposes to make the securities of those OTCBB issuers whose securities are removed from the OTCBB for failure to file two times in a two-year period ineligible for quotation on the OTCBB for a period of one year.¹³ The heightened test for this category reflects the greater length of the filing delinquencies, *i.e.*, these issuers were unable to regain compliance, even within the applicable “grace” period. In applying the look-back associated with this provision, Nasdaq would consider the date the security is removed, without regard to when the delinquent reports were actually due.

Under the proposed rule change, as amended, only filings for which the grace period ends while the issuer is quoted on the OTCBB would be considered.¹⁴ Following its removal for

¹² Prior to such removal, Nasdaq intends to provide issuers with 7 calendar days to request review of the determination by a hearings panel. See File No. SR-NASD-2005-067, which proposes to clarify the availability of a process to review eligibility determinations under NASD Rule 6530. This filing, which has not yet been published by the Commission for public comment, is available on Nasdaq’s Web site at www.nasdaq.com.

¹³ An issuer that is not removed because it files a late report after requesting a hearing pursuant to the NASD Rule 9700 Series but before a decision has been issued in the matter would not be considered to have failed to file pursuant to proposed NASD Rule 6530(e)(2), but it would still be considered to have filed late for purposes of proposed NASD Rule 6530(e)(1).

¹⁴ Thus, for example, an OTCBB-quoted issuer that has no prior late filings fails to file its Form 10-K for the period ended December 31, 2005, prior to the end of the applicable grace period. The issuer is removed from the OTCBB under existing NASD Rule 6530(a)(2), and thereafter also files its Form 10-Q for the period ended March 31, 2006, after the due date. The issuer is subsequently re-included on the OTCBB. Only the late filing for the period ended December 31, 2005, would count for purposes of the proposed rule change because the issuer was not quoted on the OTCBB when the grace period for the March 31, 2006 filing expired. See Telephone

violating one of the proposed requirements, a security would not be eligible for re-inclusion unless the issuer has timely filed in a complete form all required annual and quarterly reports for a period of one year. Thus, the securities of an issuer could not be re-included for a minimum of one year and the securities of, for example, most domestic issuers would not be eligible for re-inclusion until the issuer has timely filed at least one Form 10-K and three Forms 10-Q. Under the proposed rule change, as amended, while a late filing during the period when an issuer is ineligible would reset the ineligibility period, once an issuer that is removed for violating one of the proposed requirements is re-included, Nasdaq would not consider late filings due prior to the date of re-inclusion under the proposed rule.¹⁵

Nasdaq proposes to implement the proposed rule in connection with filings for periods ending on or after October 1, 2005.¹⁶ Filings for periods ending before October 1, 2005 would not be considered in determining the number of times a company has made late filings. Upon implementation, a company would be provided notification whenever Nasdaq determines that it is late in a periodic filing. Such notice would explain the effect of such a late filing under the proposed rule. Nasdaq would also provide information about the proposed rule on the issuer section of the OTCBB Web site, at <http://www.otcbb.com>.

Finally, Nasdaq proposes to clarify its current position that the 60-day grace period applicable to banks and savings associations also applies to holding companies for such entities. Nasdaq believes that this clarification is appropriate because, like banks and savings

conversation between Tim Fox, Attorney, Division of Market Regulation, Commission, and Arnold Golub, Associate Vice President, Nasdaq, on August 17, 2005.

¹⁵ See Telephone conversation between Tim Fox, Attorney, Division of Market Regulation, Commission, and Arnold Golub, Associate Vice President, Nasdaq, on August 17, 2005.

¹⁶ See Amendment No. 3.

associations, these holding companies must also file publicly available periodic reports with the appropriate state or federal regulator.

2. Statutory Basis

Nasdaq believes that the proposed rule change, as amended, is consistent with the provisions of Section 15A of the Act,¹⁷ in general, and with Section 15A(b)(6) of the Act,¹⁸ in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, remove impediments to a free and open market and a national market system, and, in general, to protect investors and the public interest. Nasdaq represents that the proposed rule change, as amended, is designed to increase the quality and timeliness of disclosure available to investors by OTCBB issuers and to prevent the securities of issuers that repeatedly fail to timely comply with their obligations under the securities laws from being quoted on the OTCBB.

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

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

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 by Nasdaq.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds

¹⁷ 15 U.S.C. 78q-3.

¹⁸ 15 U.S.C. 78q-3(b)(6).

such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) by order approve such proposed rule change, as amended, or
- (B) institute proceedings to determine whether the proposed rule change, as amended, should be disapproved.

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:

- 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-2005-011 on the subject line.

Paper comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NASD-2005-011. 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 Room. Copies of such filing also will be available for inspection and copying at the principal office of the Nasdaq. 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-2005-011 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.¹⁹

Margaret H. McFarland
Deputy Secretary

¹⁹ 17 CFR 200.30-3(a)(12).