

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- 53541; File No. SR-NASD-2006-033)

March 22, 2006

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendments No. 1 and 2 Thereto to Amend NASD Rule 11890

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 March 1, 2006, 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 and II below, which Items have been prepared by Nasdaq. On March 13, 2006 and March 22, 2006, Nasdaq submitted Amendments No. 1³ and 2,⁴ respectively, to the proposed rule change. Nasdaq has designated the proposed rule change as constituting a non-controversial rule change under Rule 19b-4(f)(6) under the Act,⁵ which renders the proposal effective upon filing with the Commission. 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 See Form 19b-4 dated March 13, 2006 (“Amendment No. 1”). In Amendment No. 1, Nasdaq amended its filing to indicate that Nasdaq proposes to implement the proposed rule change on March 13, 2006, rather than immediately, in the event the Commission waives the 30-day operative waiting period.

⁴ See Form 19b-4 dated March 21, 2006 (“Amendment No. 2”). In Amendment No. 2, Nasdaq amended its proposed definition of “Nasdaq security” and “non-Nasdaq security.”

⁵ 17 CFR 240.19b-4(f)(6).

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

Nasdaq proposes to clarify the scope of NASD Rule 11890. Nasdaq proposes to implement the proposed rule change on March 13, 2006.⁶ The text of the proposed rule change is below.⁷ Proposed new language is underlined; proposed deletions are in brackets.

11890. Clearly Erroneous Transactions

(a) Authority to Review Transactions Pursuant to Complaint of Market Participant

(1) No change.

(2) Procedures for Reviewing Transactions

(A) – (B) No change.

(C) Following the expiration of the period for submission of supporting material, a Nasdaq officer shall determine whether the complaint is eligible for review. A complaint shall not be eligible for review under paragraph (a) unless:

(i) the complainant has provided all of the supporting information required under paragraph (a)(2)(B), and

(ii) For trades in Nasdaq securities executed between 9:30 a.m. and 4:00 p.m. Eastern Time, or trades in non-Nasdaq

⁶ See Amendment No. 1, supra note 3.

⁷ 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. Prior to the date when The NASDAQ Stock Market LLC (“NASDAQ LLC”) commences operations, NASDAQ LLC will file a conforming change to the rules of NASDAQ LLC approved in Securities Exchange Act Release No. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006).

securities executed between the time when the primary market for the security first posts an executable two-sided quote for its regular market trading session and 4:00 p.m. Eastern Time, the price of transaction to buy (sell) that is the subject of the complaint is greater than (less than) the best offer (best bid) by an amount that equals or exceeds the minimum threshold set forth below:

Inside Price Minimum Threshold

\$0 – \$0.99	$\$0.02 + (0.10 \times \text{Inside Price})$
\$1.00 – \$4.99	$\$0.12 + (0.07 \times (\text{Inside Price} - \$1.00))$
\$5.00 – \$14.99	$\$0.40 + (0.06 \times (\text{Inside Price} - \$5.00))$
\$15 or more	\$1.00

For a transaction to buy (sell) a Nasdaq [listed] security, the inside price shall be the best offer (best bid) in Nasdaq at the time that the first share of the order that resulted in the disputed transaction was executed, and for a transaction to buy (sell) a[n exchange-listed] non-Nasdaq security, the inside price shall be the national best offer (best bid) at the time that the first share of the order that resulted in the disputed transaction was executed. A “Nasdaq security” means a security for which transaction reports are disseminated under the Nasdaq UTP Plan, and a “non-Nasdaq

security” means a security for which transaction reports are disseminated under the Consolidated Tape Association Plan. The “primary market” for a non-Nasdaq Security is the market designated as the primary market under the Consolidated Tape Association Plan.

(D) – (G) No change.

(b) – (d) No change.

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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

NASD Rule 11890(a) allows designated officers of Nasdaq to declare transactions that arise out of the use or operation of Nasdaq execution or communications systems to be clearly erroneous and to nullify or modify the terms of such transactions. In SR-NASD-2004-009,⁸ Nasdaq established a minimum price deviation threshold to provide a “bright line” rule standard for determining when transactions are considered

⁸ See Securities Exchange Act Release No. 52141 (July 27, 2005), 70 FR 44709 (August 3, 2005) (SR-NASD-2004-009).

eligible for review. A transaction price that meets these thresholds does not automatically trigger a clearly erroneous determination, but if the transaction price does not meet these thresholds the transaction will not be considered for clearly erroneous review. Thus, there is now a conclusive presumption that a transaction to buy (sell) is not clearly erroneous unless its price is greater than (less than) the best offer (best bid) by an amount that equals or exceeds the minimum threshold set forth below:

<u>Inside Price</u>	<u>Minimum Threshold</u>
\$0 - \$0.99	$\$0.02 + (0.10 \times \text{Inside Price})$
\$1.00 - \$4.99	$\$0.12 + (0.07 \times (\text{Inside Price} - \$1.00))$
\$5.00 - \$14.99	$\$0.40 + (0.06 \times (\text{Inside Price} - \$5.00))$
\$15 or more	\$1.00

In SR-NASD-2005-115,⁹ Nasdaq amended this rule to clarify that the minimum price deviation thresholds are applicable only to transactions executed during regular market hours, i.e., between 9:30 a.m. and 4:00 p.m. This amendment reflected the fact that the analysis conducted by Nasdaq to determine the appropriate levels for the thresholds was based on pricing during normal market hours, and that therefore application of the thresholds during other trading sessions was not consistent with the intent underlying the rule. During pre-market and post-market trading sessions, the inside price of many stocks may not fully reflect trading interest in the stock, since the range of market participants in these trading sessions is far more limited than during regular market hours. As a result, a trade that occurs at a price that deviates significantly from a stock's trading range during the most recent regular market session may

⁹ See Securities Exchange Act Release No. 52549 (October 3, 2005), 70 FR 58762 (October 7, 2005) (SR-NASD-2005-115).

nevertheless be sufficiently close to the pre-market or post-market inside price that it would not meet the minimum deviation threshold for the stock. Because the thresholds established by Nasdaq were based on analysis of trading patterns during regular market hours, Nasdaq concluded that the rule should be clarified by limiting the thresholds' application to such hours. The change has resulted in a larger number of transactions being eligible for review under NASD Rule 11890, since transactions occurring during pre-market and post-market sessions are always be eligible for adjudication under the rule unless the market participant seeking an adjudication failed to provide the information required under NASD Rule 11890(a)(2)(B) (i.e., the approximate time of transaction(s), security symbol, number of shares, price(s), contra broker(s) if the transactions are not anonymous, Nasdaq system used to execute the transactions, and the reason the review is being sought).

Nasdaq has now concluded that further clarification of the rule, in accordance with the foregoing discussion, is needed with respect to non-Nasdaq stocks (i.e., stocks for which transaction reports are disseminated through the Consolidated Tape Association Plan).¹⁰ Because the primary market¹¹ for such stocks may not post an executable two-sided quotation precisely at 9:30 a.m., the pre-market trading session for such stocks may, in effect, run beyond that time. As a result, Nasdaq has found that

¹⁰ See Amendment No. 2, supra note 4.

¹¹ The rule defines "primary market" with reference to the Consolidated Tape Association Plan ("CTA Plan"), which references the market in which the greatest number of transactions in the security reported on the consolidated tape during the preceding six month period (or such shorter period as the security has been reported on the consolidated tape if it has not been so reported for a full six month period) has taken place. See CTA Plan (second restatement), Section XI, Operational Matters.

trades in these stocks occurring after 9:30 but before the time when the primary market quote is available are frequently not subject to adjudication even though the price of the trades may deviate significantly from a stock's trading range during the most recent regular market session. The proposed rule change will address this concern by clarifying that for non-Nasdaq securities, the thresholds do not apply before the time when the primary market for the security first posts an executable two-sided quote for its regular market trading session.

2. Statutory Basis

Nasdaq believes that the proposed rule change, as amended, is consistent with the provisions of Section 15A of the Act,¹² in general and with Section 15A(b)(6) of the Act,¹³ in particular, in that the proposal is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The proposed rule change will ensure that NASD Rule 11890's minimum price deviation thresholds do not bar adjudication of clearly erroneous petitions in circumstances where the wider spreads prevailing before the primary market for a non-Nasdaq stock posts a quotation may make the application of such thresholds excessively restrictive.

¹² 15 U.S.C. 78o-3.

¹³ 15 U.S.C. 78o-3(b)(6).

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

Nasdaq neither solicited nor received any written comments.

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

Because the foregoing proposed rule change, as amended, 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 after the date of the filing or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁴ and Rule 19b-4(f)(6) thereunder.¹⁵

Nasdaq has requested that the Commission waive the 30-day operative delay to permit Nasdaq to implement the rule proposal on March 13, 2006. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because such waiver will ensure that NASD Rule 11890's minimum price deviation thresholds do not bar adjudication of clearly erroneous petitions for transactions occurring prior to the time that the primary market for a non-Nasdaq security disseminates a two-sided quote for the security, which is a period when

¹⁴ 15 U.S.C. 78s(b)(3)(A).

¹⁵ 17 C.F.R. 240.19b-4(f)(6).

wider spreads can prevail. Accordingly, the Commission has determined to waive the operative delay, and the proposed rule change has become effective upon filing with the Commission and operative as of March 13, 2006.¹⁶ 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.¹⁷

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-2006-033 on the subject line.

¹⁶ For purposes only of waiving 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).

¹⁷ For purposes of calculating the 60-day period within which the Commission may summarily abrogate the proposed rule change, as amended, under Section 19(b)(3)(C) of the Act, the Commission considers the period to commence on March 22, 2006, the date on which Nasdaq submitted Amendment No. 2. See 15 U.S.C. 78s(b)(3)(C).

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASD-2006-033. 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, as amended, that are filed with the Commission, and all written communications relating to the proposed rule change, as amended, 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. 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-2006-033 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.¹⁸

Nancy M. Morris
Secretary

¹⁸ 17 CFR 200.30-3(a)(12).