

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54089; File No. SR-NASD-2006-077)

June 30, 2006

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Eliminate its Current General Revenue Sharing Program Under NASD Rule 7010(u) and to Adopt a Revenue Sharing Program Limited to Transactions in Nasdaq-Listed Securities Reported to the Trade Reporting Service of the Nasdaq Market Center

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on June 22, 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. Nasdaq has filed the proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A) of the Act,³ and Rule 19b-4(f)(6) thereunder,⁴ which renders the proposal effective upon filing with the Commission.⁵ 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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).

⁵ Nasdaq gave the Commission written notice of its intent to file the proposed rule change on May 31, 2006 and has asked the Commission to waive the 30-day operative delay. See Rule 19b-4(f)(6)(iii). 17 CFR 240.19b-4(f)(6)(iii).

Nasdaq proposes to eliminate its current general revenue sharing plan under NASD Rule 7010(u) and to adopt a revenue sharing program limited to transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center. Nasdaq will implement the proposed rule change on July 1, 2006.

The text of the proposed rule change is below. Proposed new language⁶ is underlined; proposed deletions are in [brackets].

7010. System Services

(a) – (f) No change.

(g) Nasdaq Market Center Trade Reporting

(1) No change to text.

(2) Nasdaq Market Center Trade Reporting Revenue Sharing Program

After Nasdaq earns total operating revenue sufficient to offset actual expenses and working capital needs, a percentage of Reporting Participant Operating Revenue ("RPOR") associated with transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center shall be eligible for sharing with Nasdaq Market Makers and Nasdaq ECNs (as defined in the Rule 4700 Series). RPOR is defined as operating revenue that is generated by Nasdaq Market Makers and Nasdaq ECNs and consists of transaction fees and market data revenue that is attributable to Nasdaq Market Makers' and Nasdaq ECNs' transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center. RPOR shall not include any investment income or regulatory monies. The sharing of RPOR shall be based on each Nasdaq

⁶ With Nasdaq's permission, the Commission modified the proposed rule text to add italics to item (g)(1). See email from John Yetter, Senior Associate General Counsel, Nasdaq, to Joseph Morra, Special Counsel, Division of Market Regulation, Commission, dated June 28, 2006.

Market Maker's and Nasdaq ECN's pro rata contribution to RPOR. In no event shall the amount of revenue shared with Nasdaq Market Makers and Nasdaq ECNs under Rule 7010(g)(2) exceed RPOR. To the extent market data revenue is subject to year-end adjustment, RPOR revenue may be adjusted accordingly. Credits will be provided on a quarterly basis.

(h) – (t) No change.

(u) [Nasdaq Revenue Sharing Program] Reserved

[After Nasdaq earns total operating revenue sufficient to offset actual expenses and working capital needs, a percentage of all Market Participant Operating Revenue ("MPOR") shall be eligible for sharing with Nasdaq Quoting Market Participants (as defined in Rule 4701). MPOR is defined as operating revenue that is generated by Nasdaq Quoting Market Participants. MPOR consists of transaction fees, technology fees, and market data revenue that is attributable to Nasdaq Quoting Market Participant activity in Nasdaq National Market and Capital Market securities. MPOR shall not include any investment income or regulatory monies. The sharing of MPOR shall be based on each Nasdaq Quoting Market Participant's pro rata contribution to MPOR. In no event shall the amount of revenue shared with Nasdaq Quoting Market Participants exceed MPOR. To the extent market data revenue is subject to year-end adjustment, MPOR revenue may be adjusted accordingly.]

(v) - (w) 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

Nasdaq is proposing to modify the scope of its current programs for revenue sharing by replacing its current general revenue sharing program under NASD Rule 7010(u) with a program limited to transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center. The program will be similar in structure to Nasdaq's current program, in that it will share a percentage of operating revenue with members based on their pro rata contribution to such revenues. Like the revenue sharing program recently instituted by NYSE Arca, Inc. ("NYSE Arca"),⁷ however, it will be narrower in its application because it will be limited to transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center. In SR-PCX-2005-121, the Pacific Exchange (now NYSE Arca) instituted a general revenue sharing program for Cross Orders in Nasdaq-listed securities. As provided in NYSE Arca Rule 7.31(s), a Cross Order allows an NYSE Arca member to internalize orders and report them through NYSE Arca after the matched order is processed through a limited algorithm designed to pursue price improvement opportunities on NYSE Arca and markets to which it routes.

Under Nasdaq's proposal, Nasdaq Market Makers and Nasdaq ECNs (i.e., market makers and ECNs that post quotes in one or more Nasdaq-listed stocks in the Nasdaq Market Center)

⁷ Securities Exchange Act Release No. 52672 (October 25, 2005), 70 FR 66885 (November 3, 2005) (SR-PCX-2005-121).

would be eligible to share in Reporting Participant Operating Revenue (“RPOR”) associated with transactions in Nasdaq-listed securities reported to the Trade Reporting Service of the Nasdaq Market Center. RPOR is defined as operating revenue that is generated by Nasdaq Market Makers and ECNs from transaction fees and market data revenue attributable to trade reports. RPOR will not include any investment income or regulatory monies.

The proposed new rule provides that the amount of revenue shared with Nasdaq Market Makers and Nasdaq ECNs under NASD Rule 7010(g)(2) may not exceed RPOR. As with the current rule, Nasdaq’s Board of Directors (either acting through its Finance Committee or as a whole) will have the authority to determine on an ongoing basis the appropriate amount of RPOR to be shared with Nasdaq Market Makers and Nasdaq ECNs, on a pro rata basis. In making this determination, the Board will balance the objective of sharing a meaningful percentage of RPOR with the objective of maintaining Nasdaq’s financial integrity. In particular, Nasdaq will not compromise its regulatory responsibilities by sharing revenue that would more appropriately be used to fund regulatory responsibilities. Nasdaq will be mindful of its regulatory responsibilities when determining its working capital needs. This determination will be made, and the credits will be provided, on a quarterly basis.

These changes are designed to provide a competitive response to efforts by NYSE Arca and potentially other venues to attract order flow that is matched by a broker-dealer and then submitted to a self-regulatory organization for clearing and reporting to the tape. Nasdaq evaluated the economics of modifying its current approach to revenue sharing and determined that the approach reflected in the proposed rule was feasible and appropriate, given the costs involved and competitive concerns.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,⁸ in general, and with Sections 15A(b)(5)⁹ and (b)(6) of the Act,¹⁰ 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; and in that it is designed to facilitate transactions in securities, to promote just and equitable principles of trade, to enhance competition, and to protect investors and the public interest.

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

Because the foregoing proposed rule change 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 on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public

⁸ 15 U.S.C. 78o-3.

⁹ 15 U.S.C. 78o-3(b)(5)

¹⁰ 15 U.S.C. 78o-3(b)(6).

interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act¹¹ and Rule 10b-4(f)(6) thereunder.¹²

At any time within 60 days of the filing of such 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.

Nasdaq has requested that the Commission waive the 30-day operative delay contained in Rule 19b-4(f)(6)(iii) under the Act¹³ based upon a representation that the proposal will allow Nasdaq to implement more competitive pricing for transactions reported to the trade reporting service of the Nasdaq Market Center, and in that it is intended as a response to a similar program instituted by a competitor on an immediately effective basis. In light of the foregoing, the Commission believes such waiver is consistent with the protection of investors and the public interest. Accordingly, the Commission designates the proposal to be effective and operative upon filing with the Commission.¹⁴

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:

¹¹ 15 U.S.C. 78s(b)(3)(A).

¹² 17 CFR 240.19b-4(f)(6).

¹³ 17 CFR 240.19b-4(f)(6)(iii).

¹⁴ For purposes only of waiving the 30-day operative delay of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

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-2006-077 on the subject line.

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-2006-077. 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 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-2006-077 and should be submitted on or before [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Nancy M. Morris
Secretary

¹⁵ 17 CFR 200.30-3(a)(12).