

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49738; File No. SR-NASD-2004-072)

May 19, 2004

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. to Establish Fees for the Use of the Nasdaq Workstation II Service by NASD Members Via Digital Subscriber Lines

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 April 26, 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 (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. The proposed rule change has been filed by Nasdaq as establishing or changing a due, fee or other charge under Section 19(b)(3)(A)(ii) of the Act³ and Rule 19b-4(f)(2) thereunder,⁴ which renders the proposal effective upon filing. On May 4, 2004, Nasdaq filed Amendment No. 1 to the proposed rule change.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 15 U.S.C. 78s(b)(3)(A)(ii).

⁴ 17 CFR 240.19b-4(f)(2).

⁵ See letter from John M. Yetter, Associate General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, SEC, dated May 3, 2004 (“Amendment No. 1”). Amendment No. 1 changes the implementation dates of the proposal (see discussion, *infra*, at I, II(A)).

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

Nasdaq proposes to establish fees for NASD members using the Nasdaq Workstation II (“NWII”) service via Digital Subscriber Line (“DSL”) connections. Nasdaq will implement the proposed rule change on June 1, 2004, when it will begin the process of connecting firms through DSL. Below is the text of the proposed rule change. Proposed new language is in italics.

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7000. CHARGES FOR SERVICES AND EQUIPMENT

7010. System Services

(a) – (e) No change

(f) Nasdaq Workstation™ Service

(1) (A) The following charges shall apply to the receipt of Level 2 or Level 3 Nasdaq Service via equipment and communications linkages prescribed for the Nasdaq Workstation II Service:

Service Charge	\$2,035/month per service delivery platform (“SDP”) <u>connected via T1 circuits</u>
	<u>\$1,000/month per SDP connected via Digital Subscriber Line (“DSL”), plus \$1,000 per DSL early termination fee if service is terminated within 60 days of installation</u>

Display Charge	\$525/month per logon for the first 150 logons
	\$200/month for each additional logon
Additional Circuit/SDP Charge	\$3,235/month
PD and SDP Maintenance	
Monthly maintenance agreement	\$55/presentation device (“PD”) logon or SDP/month
Hourly fee for maintenance provided without monthly maintenance agreement	\$195 per hour (two hour minimum), plus cost of parts

(B) A subscriber that accesses Nasdaq Workstation II Service via an application programming interface (“API”) shall be assessed the Service Charge for each of the subscriber’s SDPs and shall be assessed the Display Charge for each of the subscriber’s logons, including logons of an NWII substitute or quote-update facility. API subscribers also shall be subject to the Additional Circuit /SDP Charge.

(C) A subscriber shall be subject to the Additional Circuit/SDP Charge when the subscriber has not maximized capacity on its SDP(s) by placing eight logons on an SDP and obtains an additional SDP(s); in such case, the subscriber shall be charged the Additional Circuit/SDP Charge (in lieu of the service charge) for each “underutilized” SDP(s) (i.e., the

difference between the number of SDPs a subscriber has and the number of SDPs the subscriber would need to support its logons, assuming an eight-to-one ratio). A subscriber also shall be subject to the Additional Circuit/SDP Charge when the subscriber has not maximized capacity on its T1 circuits by placing eighteen SDPs on a T1 circuit; in such case, the subscriber shall be charged the Additional Circuit/SDP Charge (in lieu of the service charge) for each “underutilized” SDP slot on the existing T1 circuit(s). Regardless of the SDP allocation across T1 circuits, a subscriber will not be subject to the Additional Circuit/SDP Charge if the subscriber does not exceed the minimum number of T1 circuits needed to support its SDP, assuming an eighteen-to-one ratio.

(D) DSL service (i) shall be provided solely to NASD members without API logons, (ii) shall be provided to only one SDP per location, and (iii) may not be used in connection with SDP T1 circuit connections at the same location. A subscriber with an SDP connected to Nasdaq via T1 circuits that orders DSL on or before June 1, 2004 shall not be required to pay charges under Rule 7040 for initial disconnection of T1 circuits and installation of DSL. In addition, if such a subscriber cancels DSL service within 10 business days of its first date of DSL service, the subscriber shall not be required to pay the early termination fee or charges under Rule 7040 for disconnection of DSL and reinstallation of T1 circuits.

(2) No change.

(g) – (u) 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 states that the NWII service allows market participants to access The Nasdaq Stock Market and other Nasdaq facilities, using either an “NWII presentation device” (a workstation and associated software provided by Nasdaq) or the subscriber’s own workstation and software (often referred to as an “application programming interface” or “API” device). Each subscriber location has at least one service delivery platform (“SDP”) to which it connects the workstations used by its employees.

Nasdaq represents that, in the past, the only option available for connecting a subscriber’s SDP to Nasdaq has been the use of a dedicated T1 circuit pair, provided by Nasdaq’s telecommunications service provider pursuant to a contract with Nasdaq. Nasdaq has concluded that this “one-size-fits-all” approach is unduly expensive for small firms that never use most of the bandwidth⁶ associated with T1 circuits. Accordingly,

⁶ The term “bandwidth” refers to the amount of data that can be transmitted in one second. Specifically, 1.2 megabits per second of data can be transmitted over

Nasdaq plans to offer subscribers the option of connecting through lower-bandwidth, lower-cost DSL service. Other market centers, including the New York Stock Exchange and the Archipelago Exchange facility of the Pacific Exchange, allow firms to connect to their trading systems through DSL.⁷

Nasdaq states that it will use a certificate-based “Virtual Private Network” (“VPN”) architecture to provide the highest level of security currently available for internet traffic. Data transmitted through the VPN will be encrypted using Triple Data Encryption Internet Protocol Security (“3DES IPsec”) encryption, which is more robust than the encryption used by on-line banking and brokerage services.

Nasdaq represents that it will also take steps designed to ensure that DSL connections generally support the same level of performance as small firm NWII customers currently receive through their T1 circuits. Specifically, because API devices are frequently used to support high volume computer-generated transactions whereas NWII presentation devices must be operated by an individual and therefore transmit lower volumes of data, DSL connections will only be available to subscribers without API logons. In addition, Nasdaq will provide only one DSL connection per site and will not allow simultaneous use of DSL and T1 connections at the same site, because a firm with sufficient bandwidth needs to require more than one connection at a particular site

each of the T1 circuits used to support an SDP. A subscriber that regularly transmitted a much smaller quantity of data would not be utilizing the bandwidth inherent in its T1 circuits. Conversely, a subscriber that utilized most of its bandwidth would eventually be required to obtain an additional SDP to ensure that sufficient bandwidth was always available to it.

⁷ See www.nyse.com/pdfs/anondotintroguide.pdf (describing internet access to NYSE’s Anonymous SuperDOT system); www.tradearca.com/exchange/realtick.asp (describing DSL access to Archipelago via RealTick[®] product of Townsend Analytics, Ltd.).

would be better served by having one or more T1 connections. Finally, firms whose needs for simultaneous access to data about a significant number of securities is such that they would be in danger of exhausting the bandwidth available through a DSL connection will be advised to use a T1 connection.

Nasdaq states that, prior to submitting this rule filing, it contacted 10 of the approximately 150 firms that Nasdaq believes may be interested in using DSL. Nasdaq represents that all of the firms that were contacted stated that they would be interested in trying DSL, and most expressed an interest in doing so as soon as possible. Accordingly, Nasdaq will begin taking orders for the new service during May 2004, and will begin the process of connecting firms that order the service in June 2004.

Nasdaq states that the monthly charge for an SDP attached to a DSL line will be \$1,000 per month, less than half the charge of \$2,035 per month for a T1 connection, reflecting the lower cost of the lower bandwidth service. Firms wishing to switch from T1 to DSL would be required to pay the cost of disconnecting one line and connecting the other.⁸ A subscriber that cancels its service within 60 days of installation would be charged an early termination fee of \$1,000 per terminated DSL. Nasdaq represents that, in order to encourage firms that may benefit from DSL usage to switch rapidly, however, it will waive the disconnection and connection charges for firms that order the new service by June 1, 2004. Moreover, firms ordering DSL by that date will be permitted to use it on a 10-day trial basis, and may return to T1 connections at the end of the 10-day period at no additional cost (i.e., Nasdaq will waive the associated disconnection, reconnection, and early termination fees).

⁸ See NASD Rule 7040 (authorizing charges for installation, removal, or relocation of NWII-related equipment).

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,⁹ in general, and Section 15A(b)(5) of the Act,¹⁰ in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members. Nasdaq believes the proposed rule change will allow Nasdaq to charge small firms that use the NWII service fees that are more commensurate with the lower levels of bandwidth that they use.

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.

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 Act¹¹ and subparagraph (f)(2) of Rule 19b-4 thereunder,¹² because it establishes or changes a due, fee, or other charge imposed by Nasdaq. At any time within 60 days of the filing of the proposed rule change, the Commission may summarily

⁹ 15 U.S.C. 78o-3.

¹⁰ 15 U.S.C. 78o-3(b)(5).

¹¹ 15 U.S.C. 78s(b)(3)(A)(ii).

¹² 17 CFR 240.19b-4(f)(2).

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.¹³

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-2004-072 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-2004-072. 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

¹³ For purposes of calculating the sixty-day abrogation period, the Commission considers the period to have begun on May 4, 2004, the date Nasdaq submitted Amendment No. 1. See 15 U.S.C. 78s(b)(3)(C).

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 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-2004-072 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.¹⁴

Margaret H. McFarland
Deputy Secretary

¹⁴ 17 CFR 200.30-3(a)(12).