

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49833; File No. SR-NASD-2004-056)

June 8, 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. Relating to Short-Sale ACT Reporting Requirements

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 31, 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 May 21, 2004, Nasdaq filed Amendment No. 1 on behalf of the NASD.³ Nasdaq has designated this proposal as a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule pursuant to Section 19(b)(3)(A) of the Act,⁴ and Rule 19b-4(f)(1)⁵ thereunder, 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 Letter from Mary M. Dunbar, Vice-President and Deputy General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission, dated May 20, 2004 (“Amendment No. 1”).

⁴ 15 U.S.C 78s(b)(3)(A).

⁵ 17 CFR 240.19b-4(f)(1).

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

Nasdaq is filing with the Commission a proposed rule change to clarify that members are required to indicate on their Automated Confirmation Transaction ("ACT") Service reports whether a sale is a short sale or short sale exempt transaction for all securities, including exchange-listed, SmallCap, OTC Bulletin Board and OTC equity securities.

The text of the proposed rule change is below. Proposed new language is underlined.

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IM 6130. Trade Reporting of Short Sales

The NASD's short sale rule (Short Sale Rule or Rule 3350) generally prohibits members from effecting short sales in NNM securities at or below the inside bid when the current inside bid is below the previous inside bid. Rule 6130(d)(6) requires that members indicate on ACT reports whether a transaction is a short sale or a short sale exempt transaction ("ACT short sale reporting requirements"). Rule 6130 explicitly requires members to file ACT reports not just for NNM securities transactions, but for other securities transactions, including transactions in exchange-listed, SmallCap, convertible debt, OTC Bulletin Board, and OTC equity securities. Thus, all short sale transactions in these securities reported to ACT must carry a "short sale" indicator (or a "short sale exempt" indicator if it is a short sale transaction in an NNM or exchange-listed security that qualifies for an exemption from Rule 3350 or SEC Rule 10a-1).

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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 the Statutory Basis for, the Proposed Rule Change

1. Purpose

In 1992, the NASD, believing that short sale regulation is important to the orderly operation of securities markets, proposed a short sale rule for trading of Nasdaq National Market ("NNM") securities that incorporates the protections provided by Rule 10a-1 of the Act.⁶ On June 29, 1994, the Commission approved the NASD's short sale rule applicable to short sales⁷ in NNM securities on an eighteen-month pilot basis through March 5, 1996 (the "Short Sale Rule").⁸ The NASD and the Commission have extended NASD Rule 3350 numerous times, most recently, until June 15, 2004.

As part of the Short Sale Rule, the NASD also amended NASD Rule 6130(d)(6) (previously ACT Rule (d)(4)(F)) to require that members include in ACT information regarding whether a sale is a short sale or short sale exempt ("short sale ACT reporting requirements"). Nasdaq believes that, because the Short Sale Rule applies only to NNM securities, and earlier guidance was issued relating specifically to short sale ACT reporting requirements for NNM

⁶ 17 CFR 240.10a-1.

⁷ A short sale is a sale of a security that the seller does not own or any sale that is consummated by the delivery of a security borrowed by, or for the account of, the seller. To determine whether a sale is a short sale, members must adhere to the definition of a "short sale" contained in Rule 3b-3 of the Act, which is incorporated into NASD's short sale rule by NASD Rule 3350(k)(1).

⁸ See Securities Exchange Act Release No. 34277 (June 29, 1994), 59 FR 34885 (July 7, 1994) ("Short Sale Rule Approval Order").

securities,⁹ some members may have been confused as to the types of securities that are subject to the short sale ACT reporting requirements. Through this filing, Nasdaq is clarifying that, as required by the text of the rule, the short sale ACT reporting requirements apply to transactions in all securities reported to ACT, including exchange-listed, SmallCap, OTC Bulletin Board and OTC equity securities. Nasdaq is submitting this filing to eliminate any ambiguity and make clear that members are required to annotate whether a sale is a short sale or short sale exempt, as applicable, pursuant to NASD Rule 6130(d)(4) for all ACT reports.

The proposed interpretation will become effective immediately upon filing, but Nasdaq will allow firms a 60-day period to re-program their systems to comply with the interpretation. Nasdaq believes that a 60-day period is necessary and reasonable in light of any confusion that may have existed to date. Within 10 days after filing this proposal, Nasdaq will publish a Notice to Members describing firms' obligations under IM 6130. The publication of that Notice to Members will trigger the start of the 60-day period.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the Act, including Section 15A(b)(6)¹⁰ of the Act, which requires, among other things, that a registered national securities association's rules be designed 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 mechanisms of a free and open market and a national market system, and to protect investors and the public interest. Nasdaq believes the proposed rule change is consistent with the Act in that it clarifies short sale reporting requirements and

⁹ See ACT Notice 94-1 (August 22, 1994).

¹⁰ 15 U.S.C. 78q-3(b)(6).

promotes compliance with and regulation of short sale requirements.

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)(i)¹¹ of the Act, and subparagraph (f)(1) of Rule 19b-4 thereunder,¹² because it is concerned solely with the interpretation of the meaning, administration or enforcement of an existing NASD rule.

At any time within 60 days of the filing of a rule change pursuant to Section 19(b)(3)(A) of the Act, the Commission may summarily abrogate the 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, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

¹¹ 15 U.S.C 78s(b)(3)(A)(i).

¹² 17 CFR 240.19b-4(f)(1).

¹³ For purposes of determining the effective date of the filing and calculating the 60-day abrogation date, the Commission considers the period to commence on May 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 an e-mail to rule-comments@sec.gov. Please include File Number SR-NASD-2004-056 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-2004-056. 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-2004-056 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).