

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53371; File No. SR-NASD-2005-144)

February 24, 2006

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Approval of a Proposed Rule Change Relating to Order Entry and Execution Practices

I. Introduction

On December 8, 2005, the National Association of Securities Dealers, Inc. (“NASD”) filed with the Securities and Exchange Commission (“Commission”) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934, as amended, (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change relating to order entry and execution practices. The proposed rule change was published in the Federal Register on January 23, 2006.³ The Commission has received one comment on the proposal.⁴ This order approves the proposed rule change.

II. Description of the Proposal

The NASD proposed to add Rule 3380 to prohibit members and associated persons from splitting any order into multiple smaller orders for execution or any execution into multiple smaller executions for transaction reporting for the primary purpose of maximizing a monetary or in-kind payment to the member or associated persons as a result of the execution of such orders or the transaction reporting of such executions.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240. 19b-4.

³ See Securities Exchange Act Release No. 53132 (January 17, 2006), 71 FR 3584.

⁴ See email comment from Jefferson Wigley, Managing Member, Sun Trading LLC, dated February 15, 2006 (“Sun Trading Letter”).

III. Discussion and Commission Findings

The Commission has reviewed carefully the proposed rule change and finds that it is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association,⁵ particularly Section 15A(b)(6) of the Act,⁶ which requires that an association's rules be designed to prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, remove impediments to, and perfect the mechanism of, a free and open market and, in general, protect investors and the public interest.

In its comment letter on behalf of Sun Trading LLC,⁷ the commenter argues, in essence, that the rule proposal should be limited to the splitting of customer orders, and that trade shredding should be permitted for member proprietary trades, since this could allow members to make tighter and more efficient markets. Accordingly, the commenter suggests that the Commission limit the application of the rule to exclude trading by market makers and proprietary trading firms where no customer orders are involved. The commenter believes that the Commission has adequately addressed the issue of trade shredding in the newly adopted Regulation NMS and that further steps would be counter productive.

While Regulation NMS will revise the current plan formulas, which allocate market data revenues based either solely on the number of trades, or on trade and share volume, to reduce the emphasis on trade volume, the Commission believes it is

⁵ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

⁶ 15 U.S.C. 78o-3(b)(6).

⁷ See supra note 4.

appropriate for self-regulatory organizations (“SROs”) to take additional steps to address trade shredding and its potentially distortive effects. The Commission notes that, to date, it has approved rule changes to address the practice of trade shredding from four SROs.⁸ The remaining SROs have filed proposed rule changes to address the issue of trade shredding.⁹

The Commission believes that the proposed rule change should further deter the distortive practice of trade shredding, and, therefore, promote just and equitable principles of trade.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁰ that the proposed rule change (File No. SR-NASD-2005-144), be and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹¹

Nancy M. Morris
Secretary

⁸ See Securities Exchange Act Release Nos. 52341 (August 26, 2005), 70 FR 52455 (September 2, 2005) (SR-BSE-2005-20); 52683 (October 26, 2005), 70 FR 66480 (November 2, 2005) (SR-NYSE-2005-62); 53070 (January 6, 2006), 71 FR 2286 (January 13, 2006) (SR-Phlx-2005-63); 53088 (January 10, 2006), 71 FR 2605 (January 17, 2006) (SR-CBOE-2005-92).

⁹ See SR-Amex-2005-112, SR-CHX-2006-03, SR-PCX-2006-10. National Stock Exchange expects to file a trade shredding rule change proposal in the near future.

¹⁰ 15 U.S.C. 78s(b)(2).

¹¹ 17 CFR 200.30-3(a)(12).