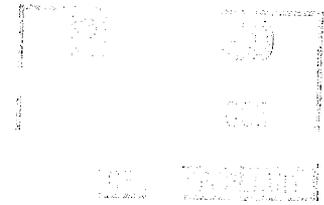




April 30, 2003

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street
Washington, D.C. 20549-0609



Re: Waiver of ACT Fees (SR-NASD-2003-56)

Dear Mr. Katz:

Once again, the Nasdaq Stock Market (“Nasdaq”) is attempting to create the equivalent of off-board trading restrictions that it opposed for listed stocks by proposing to waive for certain NASD members its fee for their reporting of trades to Nasdaq’s Automated Confirmation Transaction Service (“ACT”).¹ Nasdaq currently charges \$0.029 for members to report transactions executed through SuperMontage and other transaction execution systems that make use of SuperMontage’s reporting functionality. Nasdaq proposes to waive the fee for an ACT participant during any month in which the participant: (i) executes an average daily volume of 10,000 or more transactions through SuperMontage or other Nasdaq execution systems; (ii) reports to ACT at least 98% of its internalized transactions in Nasdaq National Market and SmallCap Market securities; and, (iii) posts in SuperMontage at least 70% of its bids, offers and non-marketable limit orders in Nasdaq National Market and SmallCap Market securities.

Not content with the usual volume discounts, which can recognize economies of scale and a member’s financial contribution through other fees, Nasdaq adds to the mix an “all-or-none” requirement with respect to reporting internalized trades to ACT and a near-exclusive requirement with respect to quote in SuperMontage. Nasdaq’s coercive pricing attempts to inflate its volume and secure tape revenue for internalized trades not taking place in any Nasdaq facility.²

Last year, Nasdaq made similar coercive attempts when it submitted a series of similar discriminatory proposed fee changes that would have discriminated in favor of “Full Contribution Members” (members **that** report at least 95 percent of their trading activity

¹ Release No. 34-47621 (SR-NASD-2003-56) (April 2, 2003).

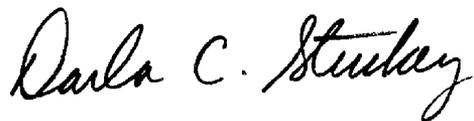
² If the Commission were to approve Nasdaq’s registration as a national securities exchange, the reporting of internalized trades to Nasdaq **would** violate federal securities law, Commission rules, national market system plans and certain national market system agreements. For an extensive discussion of this issue, see letter to Mr. **Katz** from James E. **Buck, Secretary**, NYSE, dated August 27, 2001, commenting on the Nasdaq Stock Market’s Application for Registration as a National Securities Exchange, Release No. 34-44396, File No. 10-131.

in Nasdaq-listed securities to Nasdaq) and against those that do not.³ As with its Full Contribution Member proposal, Nasdaq's latest proposal attempts to use its fees to unfairly discriminate between members; in this case, between ACT participants that send almost all of their business to Nasdaq and those that do not. Then, as now, the Exchange believes that fees and fee waivers based upon capturing a percentage of a member's business are unreasonably discriminatory and anti-competitive, and violate 1934 Act standards on equitable allocation of fees, promotion of just **and** equitable principles of trade, removal of impediments to a free and open market and national market system, and unreasonable discrimination among customers, brokers and dealers. Moreover, the Commission's continuing concerns about payment for order flow must naturally extend to this functionally equivalent scheme.

For these reasons, the Exchange urges the Commission to institute disapproval proceedings on this latest of Nasdaq's coercive and discriminatory proposals.

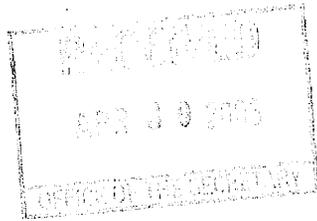
We thank you for this opportunity to comment and would be pleased to respond to any questions you may have.

Sincerely yours,



cc: Chairman William H. Donaldson
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
Commissioner Harvey 3. Goldschmid
Annette L. Nazareth, Director, Division of Market Regulation
Robert L.D. Colby, Deputy Director, Division of Market Regulation
Elizabeth King, Associate Director, Division of Market Regulation
Rebekah Liu, Special Counsel, Division of Market Regulation

³ Release No. 34-44918 (SR-NASD-2001-71) (October 17, 2001); Release No. **34-44391** (SR-NASD-2001-72) (October 12, 2001); Release No. **34-45342** (SR-NASD-2001-96) (January 28, 2002); Release No. 34-45444 (SR-NASD-2002-17) (February 14, 2002); Release No. 34-45506 (SR-NASD-2002-18) (March 5, 2002); Release No. 34-45916 (SR-NASD-2002-61) (May 10, 2002). The NYSE commented on these proposals and called for the Commission to institute disapproval proceedings on Nasdaq's Full Contribution Member proposal. See letter to Mr. Jonathan G. Katz, Secretary, Commission, from Darla C. Stuckey, Secretary, NYSE, dated August 6, 2002. We incorporate that letter, attached hereto, by reference. (The NASD subsequently withdrew SR-NASD-2001-11, 2001-72, 2002-17 and 2002-18. The Commission **approved** NASD-2001-96 and summarily abrogated NASD-2002-61.)



August 6, 2002

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Discriminatory, Coercive and Anti-Competitive

Dear Mr. Katz:

Full Contribution Members -- members that report at least 95 percent of their trading activity in Nasdaq-listed securities to Nasdaq -- and against those that do not.'

Nasdaq proposes new fees for the execution of SOES trades and for quotation updates in Nasdaq-listed securities. Under the proposal, those fees would be substantially higher for members that fail to report at least 95 percent of their trading to Nasdaq than for members that are Full Contribution Members. Furthermore, Nasdaq proposes to establish a program that rebates to Full Contribution Members certain Nasdaq market data revenues.

A. Summary

For the following reasons, the Exchange believes that the 95-percent requirement is unfair, unreasonably discriminatory, coercive and anti-competitive, and that the Commission should institute disapproval proceedings on the Nasdaq proposal:

- If a member does not meet the 95-percent requirement, Nasdaq would require it to pay 25 percent more to execute trades through Nasdaq systems and 100 percent more to advertise its liquidity on Nasdaq.

Exhibit A presents a fuller explanation of the relevant Nasdaq proposals.

- The degree of **Nasdaq's** proposed discrimination **and** its “all-or-none” nature **coerce** market participants to **report** substantially all **trades** in Nasdaq-listed securities through Nasdaq, either by executing trades through Nasdaq facilities or by reporting their internalized trades to **Nasdaq**.
- Nasdaq is **trying** to leverage **its** legacy market share arising **from** its position **as** the sole market regulator, sole **market** data processor, **sole** market linkage and sole systems provider for Nasdaq-listed stocks **as** it prepares **to** enter a marketplace in which it must compete with other exchanges.

The Commission conditioned its approval of SuperMontage on Nasdaq making participation in SuperMontage “entirely voluntary.” The coercive nature of the 95-percent requirement violates that condition.

- The Exchange’s former Rule 390 **and** the 95-percent requirement have the same objective -- encouraging members to execute trades on specific market venues. Rule 390, however, had a public policy **purpose** of maximizing **the** efficiency of price discovery through order interaction and of eliminating the conflicts in internalization. But, because the Commission found that Rule 390 impaired other markets **from** competing for orders, it required the **Exchange** to repeal it. The 95-percent requirement, which is far more restrictive **than** Rule 390 and is devoid of Rule 390’s public policy benefits, is anti-competitive, violates sections **15A(b)(9) and 6(b)(8) of the Securities Exchange Act of 1934** (the “Exchange Act”) and Commission Rules **19c-1 and 19c-3**.
- It is inherently wrong **when** a broker-dealer’s principal motivation in directing its customers’ order **flow** is based upon monetary rewards to the broker-dealer, rather than what is in the best interests of the customers. The **95-percent** requirement **would** motivate Nasdaq members to send trade reports to Nasdaq simply to allow them **to** qualify **as Full Contribution Members**. **This** creates **a** conflict with the fiduciary obligation of Nasdaq members to **act in a manner that** is best suited to their customers’ needs.
- **Nasdaq** is proposing **to** break the nexus between the location of a trade **and** transaction **reporting**. **The proposal** violates the **Exchange Act**, **Commission** rules, the CTA Plan, the agreements that **NASD has** entered into with the CTA Plan’s processor **and** conflicts of law principles. Nasdaq’s coercive fees exacerbate the fraudulent reporting of off-exchange liquidity by compelling members to report off-exchange trading activity through Nasdaq.
- Whether acting under section 6 or section 15A of the Exchange Act, the Commission **must** find **that Nasdaq** rules equitably allocate charges, promote just **and** equitable principles **of trade**, remove impediments to a free **and** open market **and** a national market system, and prohibit unfair discrimination. The 95-percent requirement fails on each count.

B. Unreasonable Discrimination

1. Coercion Nasdaq's proposed discrimination in favor of Full Contribution Members is coercive. While the maze of Nasdaq filings and the conflicts among them make it difficult to fully understand Nasdaq's proposals, Nasdaq appears to seek to significantly penalize members that do not report at least 95 percent of their trading activity in Nasdaq-listed securities to ACT. If a member does not meet the 95-percent requirement, it must pay 25 percent more to execute trades through Nasdaq systems and it must pay 100 percent more to advertise its liquidity on Nasdaq.

A market's fee structure may differentiate between members and non-members, and may properly set fees that establish appropriate and reasonable "volume discounts" and other fee differentiations, without being unreasonably discriminatory. However, the coercive nature of Nasdaq's 95-percent requirement is distinguishable from devices designed to fairly allocate costs, such as volume fee discounts. Volume discounts are not geared to a percentage of a member firm's total order flow, but rather recognize economies of scale and the cumulative financial contributions of member organizations. However, the degree of Nasdaq's proposed discrimination, and its "all-or-none" nature, coerce market participants to execute trades in Nasdaq-listed securities almost exclusively through Nasdaq facilities or internally, and not through other venues.

The Exchange has previously commented upon the illegal trade-reporting rules that Nasdaq has proposed in its application to register as a national securities exchange. Nasdaq proposes to permit -- and in many cases require -- Nasdaq members to report through ACT trades that do not take place through Nasdaq facilities. Nasdaq is proposing to break the nexus between the location of a trade and transaction reporting. That proposal violates the Exchange Act, SEC rules, the CTA Plan, the agreements that NASD has entered into with the CTA Plan's processor and conflicts of law principles. Nasdaq's coercive fees exacerbate the fraudulent reporting of off-exchange liquidity by compelling members to report off-exchange through Nasdaq.

Equally troubling, Nasdaq has designed the "Full Contribution Member" filings to preserve Nasdaq's legacy position as the primary repository for transaction reports for Nasdaq-listed securities, impeding the ability of other marketplaces to compete. Instead of determining to send trades to a marketplace based on the liquidity of that market, its quality, the reliability of its technology and the speed of its execution (i.e., pursuant to fiduciary obligations), Nasdaq members are coerced into sending trade reports to Nasdaq simply to qualify as Full Contribution Members. This in and of itself creates a conflict for Nasdaq members. Also, opting to send more than five percent of their orders to other markets, which they may need to do in order to meet their customers' needs and their fiduciary and statutory obligations, would make it costlier for them -- and ultimately their customers -- to use Nasdaq.

In addition, the "Full Contribution Member" filings violate the order in which the Commission approved Nasdaq's proposed SuperMontage system (the "SuperMontage

See August 27, 2001, letter from James Buck, Secretary, Exchange, to Jonathan G. Katz, Secretary, Commission.

Approval Order”).³ In that order, the Commission recognized that Nasdaq’s status as an exclusive securities information processor would compel SuperMontage participation. It feared that Nasdaq’s legacy advantage as the mandatory collector of quotes and trade data for over-the-counter market participants would effectively make participation in SuperMontage involuntary. The Commission therefore conditioned its approval of SuperMontage on NASD’s developing an alternative quote and trade-reporting system and on Nasdaq making participation in SuperMontage “entirely voluntary.”

The “Full Contribution Member” filings would make participation in SuperMontage **involuntary** for many of its members. The 95-percent requirement and Nasdaq’s fee discount and rebate incentives would coerce the member into using SuperMontage to the near exclusion of other markets. This coercion would contravene the SuperMontage Approval Order’s condition that Nasdaq makes participation in SuperMontage “entirely voluntary.”⁴

The effect of the 95-percent requirement is similar to that of the off-board trading restrictions that the Exchange’s former Rule 390 imposed. Rule 390 had the strong public policy basis of maximizing the efficiency of price discovery through order interaction and of eliminating the conflict of interests inherent in internalization. In contrast, the purpose of the 95-percent requirement is to enhance Nasdaq’s revenues and give a false picture of Nasdaq liquidity. Notwithstanding the public policy benefits of Rule 390, the Commission found the rule to be anti-competitive and required the Exchange to repeal it because it impaired other markets from competing for orders.

The 95-percent requirement is both far more restrictive than Rule 390 and devoid of Rule 390’s public policy benefits. Rule 390 permitted order execution on any of the eight registered national securities exchanges. In contrast, the 95-percent requirement would require Nasdaq members to report at least 95 percent of their trading activity through a single source -- ACT -- in order to gain the benefits associated with revenue sharing, reduced execution and quote-update fees, and execution fee rebates. Especially given the legacy advantages of Nasdaq’s many decades as the only over-the-counter venue for reporting trades in Nasdaq-listed securities, the 95-percent requirement amounts to an unfair and unreasonable form of competition. Furthermore, the public policy supporting Rule 390 is not present here, as the vast majority of these trade reports result from internalized dealer transactions rather than order interaction.

Nasdaq cannot point to any objective of the Exchange Act to justify its proposed off-board trading restriction and cannot reconcile its proposal with its members’ obligations to execute investors’ trades on the best market. The 95-percent requirement constitutes an unnecessary burden on competition in contravention of Nasdaq’s obligation under section 15A(b)(9) of the

³ See File No. SR-NASD-99-53; Release No. 34-43863 (January 19, 2001).

⁴ The SuperMontage Approval Order also required the NASD to offer the Alternative Display Facility (“ADF”). It is no secret that the NASD had no desire to provide such a facility or even to operate a market. The coercive nature of the 95-percent rule may have the effect of forcing into ACT all those transaction reports where there is a choice of reporting venue between ACT and ADF’s TRACS (ADF’s trade-reporting mechanism). This could have the intended effect of undermining the financial viability of the ADF, leading the NASD to petition the Commission to allow the NASD to abandon it.

Exchange Act as a registered securities association and its **corresponding** future obligation under section 6(b)(8) should it become registered **as a national securities exchange**.

As an exchange, Nasdaq would also be in violation of the Commission's prohibitions against off-board trading restrictions under Commission Rules 19c-1 and 19c-3, which both provide **in part** that:

no rule, stated policy or practice of this exchange shall prohibit or condition, or be construed to prohibit or condition or otherwise limit, directly or indirectly, the ability of any member ... to effect any transaction otherwise than on this exchange. [Emphasis added.]

The 95-percent requirement *limits* Nasdaq's members in **executing** or reporting more **than** five percent of their trading activity to **any market** other than **Nasdaq**.

2. Nasdaq Justification In the **February Filing**, **Nasdaq** attempts to justify the inequities of the 95-percent requirement with a **number of different arguments**.

- It claims that its proposal **is** a competitive **response** to the announcement by several regional exchanges that they intend to **trade** Nasdaq-listed securities in a meaningful **way** for the first time and to **compete aggressively** for trade-reporting revenue. But we have heard of **no other market establishing** a counterpart to the 95-percent requirement. Moreover, a "**competitive**" **response cannot** be anti-competitive, **as** the Nasdaq response is.
- Nasdaq also notes that exchanges routinely distinguish **among** members based on the level of system usage, citing Nasdaq's **array** of per-order charges for liability orders **as an** example. However, **as noted above**, the 95-percent requirement is qualitatively different than **a volume discount**. **It is** tantamount to an all-or-none dictate that a member either gives almost all of **its** business **to** Nasdaq or it suffers financial penalties.
- **Nasdaq asserts that** "most members are well **integrated** into **Nasdaq's** market structure **and therefore would be considered Full Contribution Members.**" **The fact that other markets** have only traded Nasdaq-listed stocks on a "very limited" basis until now makes **this claim specious**. **Nasdaq is trying to leverage** its legacy market share arising **from its position as the sole market regulator, sole market data processor, sole market linkage and sole systems provider for Nasdaq-listed stocks** as it prepares to **enter a marketplace** in which it must compete with other exchanges. **Moreover, Nasdaq's premise depends on its illegal pretension of offering a print facility for off-exchange trades if the Commission registers it as a national securities exchange. Assume that NASD members' trades in current Nasdaq facilities -- SOES, SelectNet and Primex -- are a proxy for future activity in SuperMontage. Once Nasdaq is registered as a national securities exchange, it**

will only report trades **that** occur in its facilities. Thus, most members can be expected to fail the 95-percent requirement.⁵

- Nasdaq notes that a member may elect to **report trades** on another market if it so chooses. **This is wrong. As noted above, as a matter of law, trade reporting is determined by the location of the trade, not rebates and coercive pricing.**
- Nasdaq fears that members may **use Nasdaq systems to** advertise their quotes, but may then report their trades to another market. First, **if the Commission does register Nasdaq as a national securities exchange, the issue becomes moot. As a matter of law, if a Nasdaq member executes a trade within a Nasdaq facility (e.g., SuperMontage), only Nasdaq can report it. If the member executes a trade outside of Nasdaq's, or any other exchange's, facilities (e.g., internalizes the trade), only the NASD ADF can report it.**

But, taking Nasdaq's construct *arguendo*, Nasdaq is making a case for the anti-competitive bundling of its quote dissemination and trade reporting services. **Nasdaq protests that it would receive disproportionately less revenue from a member that uses Nasdaq systems to advertise its quotes but not to report its trades than from a Full Contribution Member. Nasdaq fails to mention that if a member advertises its quotes on another market and reports its internalized trades to Nasdaq, it would pay proportionately more to Nasdaq. It also fails to mention that quote update fees compensate Nasdaq for the use of Nasdaq facilities to advertise liquidity, just as execution fees compensate for the execution of trades through Nasdaq facilities. If either the quote-update fee or the execution fee is not contributing its fair share to the recovery of Nasdaq's regulatory and other operating costs, then Nasdaq can adjust the fees accordingly. Otherwise, Nasdaq is not acting in accordance with sections 6(b)(4) and 15A(b)(5) of the Exchange Act.**

3. Statutory Standards Nasdaq's proposed 95-percent requirement must meet the applicable standards under the Exchange Act.⁶ Whether acting under section 6 or section 15A of the Exchange Act, the Commission must find **that Nasdaq** rules (among other things):

- equitably allocate reasonable dues, **fees and other charges** among **members** and other persons using its facilities **or** systems;
- promote **just and equitable principles of trade**;

As reported by the Commission in the SuperMontage Approval Order at fn. 222, 26% of the share volume and 36% of trades on the NASD are executed through SOES or SelectNet, Nasdaq's two primary execution facilities.

In this unusual instance where Nasdaq is seeking to change from a national securities association into a national securities exchange, the Commission must look to both section 6 and section 15A of the Exchange Act. In both cases, the standards are the same.

- remove impediments to, and perfect the mechanism of, a free and open market and a national market system; and
- not permit unfair discrimination between customers, brokers and dealers.⁷

As explained above, the 95-percent requirement fails on each count.

Nasdaq asserts that the statutory standards require Nasdaq "to establish prices that provide similar treatment to similarly situated members; they do not require Nasdaq to provide similar treatment to all market participants without regard to their level of participation in the market." Nasdaq cites a Commission assertion in its approval of a fee of another market that the Act "prohibits 'unfair discrimination,' not 'discrimination' *simpliciter* . . ."⁸ The Exchange agrees with those statements. The statutory standards do not require a market to charge the same fees to every participant in every instance.

What those standards do require is that Nasdaq's classification be equitable, reasonable, just and fair. Marginalizing Nasdaq's competitors at a collective market share under five percent does not make that cut.

* * *

The Commission's abrogation of Nasdaq's market data revenue sharing programs for Nasdaq-listed stocks helps to mitigate the unfair impact on Nasdaq's 95-percent requirement. However, the fact remains that Commission approval of the 95-percent requirement would require a member to pay Nasdaq 100 percent more in quote-update fees, and 25 percent more in execution fees, unless it almost completely diverts its activities from other markets and executes and reports 95 percent of its trading in Nasdaq-listed securities to Nasdaq. This discriminates unfairly against members and competes unfairly against other markets.

We thank you for this opportunity to comment and would be pleased to respond to any questions you may have.

Sincerely yours,



cc: Chairman Harvey L. Pitt
 Commissioner Paul S. Atkinson
 Commissioner Roel Campos
 Commissioner Cynthia A. Glassman

⁷ See sections 6(b)(4) and (5) and sections 15A(b)(5) and (6) of the Exchange Act. See File No. SR-NASD-2002-18 (Release No. 34-45506; March 5, 2002). Nasdaq cites Release No. 37250 (May 29, 1996).

Commissioner Harvey J. Goldschmid
Annette L. Nazareth, Director, Division of Market Regulation
Robert L.D. Colby, Deputy Director, Division of Market Regulation
Elizabeth King, Associate Director, Division of Market Regulation
Rebekah Liu, Special Counsel, Division of Market Regulation

Exhibit A

NEW YORK STOCK EXCHANGE ANALYSIS

The Nasdaq Stock Market Inc. ("Nasdaq")

Fee Changes and Revenue Sharing Program for Trading in Nasdaq Securities
Release No. 34-44918; File No. SR-NASD-2001-71
Release No. 34-44391; File No. SR-NASD-2001-72
Release No. 34-45342; File No. SR-NASD-2001-96
Release No. 34-45444; File No. SR-NASD-2002-17
Release No. 34-45506; File No. SR-NASD-2002-18
Release No. 34-45916; File No. SR-NASD-2002-61

The Filings

The labyrinth of Nasdaq's filings makes assessing Nasdaq's fees and revenue sharing program daunting.⁷ To facilitate review, we provide a summary of the relevant Nasdaq filings:

1. October Member-Fee Filing In October 2001, Nasdaq submitted a proposed rule change² (the "October Member-Fee Filing") that established discriminatory pricing and rebate programs that favored members that report substantially all of their trades in Nasdaq-listed securities to Nasdaq ("Full Contribution Members") over other members. To qualify as a "Full Contribution Member" under that filing, a member must report "substantially all" of its trades through Nasdaq's Automated Confirmation Transaction Service ("ACT"). Nasdaq submitted the October Member-Fee Filing as a pilot program and for immediate effectiveness.

The October Member-Fee Filing discriminated in favor of Full Contribution Members and against other members in the following ways:

- (a) Revenue Sharing Nasdaq agreed to rebate to Full Contribution Members - but not to other members -- revenues that Nasdaq's Level 1 market data service generates.

The Exchange has previously commented upon the opaque and confusing application filed by Nasdaq to register as a national securities exchange. (See August 27, 2001, letter from James Buck, Secretary, Exchange, to Jonathan G. Katz, Secretary, Commission (the "August Comment Letter")). Nasdaq's maze of filings regarding its execution-related fees and market data revenue sharing program exemplifies the flaws.

See File No. SR-NASD-2001-71 (Release No. 34-44918; October 17, 2001).

- (b) **Execution Fee** Nasdaq set the per-share execution fee payable by “UTP exchanges”³ and members other than Full Contribution Members for trades that they execute through SOES at a level that was *50 percent higher* than the fee payable by Full Contribution Members. Full Contribution Members would pay \$0.002 per share and all others would pay \$0.003 per share.
- (c) **Execution Fee Rebate** If a Full Contribution Member did not charge a quotation access fee to market participants, Nasdaq provided that Full Contribution Member with a rebate of Nasdaq’s per-share execution charge that was *100 percent as large* as the rebate that Nasdaq provided to other members. Full Contribution Members would receive \$0.001 per share and other members would receive \$0.0005 per share. (UTP exchanges received no rebate.)
- (d) **Quote Update Fee** Nasdaq set the quotation update fee payable by members other than Full Contribution Members at a level that was *200 percent higher* than the fee payable by Full Contribution Members. Full Contribution Members pay \$0.01 per quotation update and other members pay \$0.03 per quotation update.

Although Nasdaq submitted the **October Member-Fee Filing** for immediate effectiveness, Nasdaq never implemented it and, after discussions with Commission staff, withdrew the filing on November 29.

2. **October Non-Member-Fee Filing** Contemporaneously with its October 2001 filing of the **October Member-Fee Filing**, Nasdaq submitted a companion proposed rule change⁴ (the “**October Non-Member-Fee Filing**”). That filing sought to impose on non-members the same proposed fee changes and rebate program as the **October Member-Fee Filing** imposed on members.⁵ Nasdaq did not file the **October Non-Member-Fee Filing** for immediate effectiveness, did not file it as a pilot program and did not withdraw it.⁶ As a result, the **October Non-Member-Fee Filing** is evidently still pending before the Commission and awaiting Commission action.

3. **February Filing** In February 2002, Nasdaq submitted a proposed rule change’ (the “**February Filing**”) that proposed SOES fees and a rebate program different

A “UTP exchange” is a national securities exchange that trades Nasdaq-listed securities through SOES based on unlisted trading privileges.

See File No. SR-NASD-2001-72 (Release No. 34-44391; October 12, 2001).

We understand that Nasdaq expects to apply the SOES fee structure to SuperMontage and to retain that fee structure if the Commission approves Nasdaq’s pending registration as a national securities exchange. Our comments reflect that understanding.

See Amendment No.1 to the **October Non-Member-Fee Filing**, which is contained in an October 11, 2001, letter from John M. Yetter, Assistant General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission.

See File No. SR-NASD-2002-18 (Release No. 34-45506; March 5, 2002).

from the withdrawn October **Member-Fee Filing**. Nasdaq submitted **the** February Filing “regular way” and for permanent approval.

The **February** Filing discriminates in favor of “Full Contribution Members” and **against** other members. **This** time, Nasdaq defined “**Full Contribution Member**” as a member **that** reports at least 95 **percent** of **its** trading activity **to** ACT, (The two October filings define “Full Contribution Member” as a member that **reports substantially all of its trades to ACT**.) Discriminatory practices that the February Filing proposes include the following:

- (a) Revenue Sharing After withdrawing the **October** Member-Fee **Filing** in November, **but before** submitting the **February** Filing, Nasdaq established **a** pilot market data rebate **program**. At the time of the submission of the February Filing, that pilot program rebated **to** all Nasdaq **members 80 percent of** Nasdaq Level 1 revenues less **certain** regulatory fees.’ The February Filing proposes to rebate market data fees **to Full** Contribution Members **only**.

Subsequent to the February Filing, Nasdaq amended its rebate program to provide that Nasdaq will rebate 90 percent of its Level 1 revenues to its members, without deducting regulatory **casts**.’ However, **Nasdaq** did not **amend** the February Filing to reflect those changes. Therefore, **Nasdaq** evidently **has** pending before the Commission **a** proposal (i.e., the February Filing) that would amend **a** rebate program that **Nasdaq** has superseded with a different program.

Complicating matters even further are the Commission’s recent abrogation of the underlying **Nasdaq** rebate program for Nasdaq-listed stocks **and** Nasdaq’s subsequently proposed amendment **to** reinstate the abrogated transaction credit **pilot** programs for NYSE-listed securities but not for **Nasdaq-listed securities.”** **As** a result, Nasdaq **has** pending before the Commission **proposed** amendments to **a** rebate program that the Commission **has** abrogated **and that Nasdaq may or** may not move to reinstate.

- (b) Execution Fee Nasdaq **set** the per-share execution fee payable by **UTP** exchanges and members other than Full **Contribution** Members at **a** level **that** is **25** percent higher than the fee payable by Full Contribution

See File Nos. SR-NASD-2001-96 (Release No. 34-45342; January 28, 2002) and SR-NASD-2002-17 (Release No. 34-45444; February 14, 2002).

⁹ *See* File No. SR-NASD-2002-61 (Release No. 45916; May 10, 2002).

¹⁰ *See* the Commission’s Order of Summary Abrogation (Release No. 34-46159; July 2, 2002) and File No. SR-NASD-2002-94 (Release No. 46232; July 19, 2002).

Members. Full Contribution Members would pay \$0.002 per share and other members would pay \$0.0025.”

- (c) **Quote Update Fee** The February Filing sets the quotation update fee payable by members other than Full Contribution Members at a level that is *100 percent higher* than the fee payable by Full Contribution Members. Full Contribution Members pay \$0.01 per quotation update and other members pay \$0.02 per quotation update.

This conflicts with the still pending October Non-Member Fee Filing, which seeks to have other members pay \$0.003 per share. In a similar conflict, the February Filing does not propose an execution-fee rebate whereas the October Non-Member Fee Filing does.