

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49733; File No. SR-NASD-2004-034]

### 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 Allow Members To Report Certain Trades Through SuperMontage

May 19, 2004.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 26, 2004, the National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), submitted to 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. Nasdaq filed the proposal pursuant to Section 19(b)(3)(A) of the Act,<sup>3</sup> and Rule 19b-4(f)(5) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission. Nasdaq filed Amendment No. 1 to the proposed rule change on April 27, 2004.<sup>5</sup> 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

Nasdaq proposes to allow members to report certain trades through the Nasdaq National Market Execution System ("SuperMontage"). New text is italicized. Deleted text is in brackets.

\* \* \* \* \*

#### 4630. Reporting Transactions in Nasdaq National Market Securities

This Rule 4630 Series applies to the reporting by members of transactions in Nasdaq National Market securities ("designated securities") through the Automated Confirmation Transaction Reporting Service (ACT) *or the Nasdaq*

*National Market Execution System ("NNMS")*, as permitted by Rule 4720.

#### 4632. Transaction Reporting

\* \* \* \* \*

##### (c) Information To Be Reported

Each last sale report shall contain the following information:

\* \* \* \* \*

(6) For any transaction in an order for which a member has recording and reporting obligations under Rules 6954 and 6955, the trade report must include:

(A) An order identifier, meeting such parameters as may be prescribed by the Association, assigned to the order that uniquely identifies the order for the date it was received (see Rule 6954(b)(1)).

(B) The time of the execution expressed in hours, minutes, and seconds. This information must be reported regardless of the period of time between execution of the trade and the ACT *or NNMS* trade report. All times reported to the ACT *or NNMS* systems shall be in Eastern Time.

##### (d) Procedures for Reporting Price and Volume

Members that are required, or have the option, to report transactions using ACT *or NNMS*, pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in designated securities in the following manner:

\* \* \* \* \*

(B) Exception: A "riskless" principal transaction in which a member, after having received an order to buy a security, purchases the security as principal at the same price to satisfy the order to buy or, after having received an order to sell, sells the security as principal at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee. Alternatively, a member may report a riskless principal transaction by submitting the following report(s) to ACT *or NNMS*:

\* \* \* \* \*

Example:

SELL as a principal 100 shares to another member at 40 to fill an existing order;

BUY as principal 100 shares from a customer at 40 minus a mark-down of \$12.50;

REPORT 100 shares at 40 by submitting to ACT *or NNMS* either a single trade report marked with a "riskless principal" capacity indicator or by submitting the following reports:

(1) Where required by this Rule, a tape report marked with a "principal" capacity indicator; and

(2) Either a non-tape, non-clearing report or a clearing-only report marked with a "riskless principal" capacity indicator.

##### (e) Transactions Not Required To Be Reported

The following types of transactions shall not be reported:

(1) Transactions executed through [the Nasdaq National Market Execution System ("NNMS")], the Primex Auction System, or the SelectNet service];

\* \* \* \* \*

#### 4640. Reporting Transactions in Nasdaq SmallCap<sup>SM</sup> Market Securities

This Rule 4640 Series sets forth the requirements for reporting transactions in Nasdaq SmallCap<sup>SM</sup> Market securities ("designated securities") utilizing the Automated Confirmation Transaction Service (ACT) *or the Nasdaq National Market Execution System ("NNMS")*, as permitted by Rule 4720.

#### 4642. Transaction Reporting

\* \* \* \* \*

##### (c) Information To Be Reported

Each last sale report shall contain the following information:

\* \* \* \* \*

(6) For any transaction in an order for which a member has recording and reporting obligations under Rules 6954 and 6955, the trade report must include:

(A) An order identifier, meeting such parameters as may be prescribed by the Association, assigned to the order that uniquely identifies the order for the date it was received (see Rule 6954(b)(1)).

(B) The time of execution expressed in hours, minutes, and seconds. This information must be reported regardless of the period of time between execution of the trade and the ACT *or NNMS* trade report. All times reported to the ACT *or NNMS* systems shall be in Eastern Time.

##### (d) Procedures for Reporting Price and Volume\*

Members that are required, or have the option, to report transactions using ACT *or NNMS*, pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in designated securities in the following manner:

\* \* \* \* \*

(B) Exception: A "riskless" principal transaction in which a member, after having received an order to buy a security, purchases the security as principal at the same price to satisfy the order to buy or, after having received an

\* For examples of reporting procedures, refer to Rule 4632, Transaction Reporting.

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(5).

<sup>5</sup> See letter from Peter R. Geraghty, Associate Vice President and Associate General Counsel, Nasdaq, to Katherine England, Assistant Director, Division of Market Regulation, Commission, dated April 26, 2004 ("Amendment No. 1"). In amendment No. 1, Nasdaq provided additional description of the proposed rule change but did not amend the proposed rule text.

order to sell, sells the security as principal at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee. Alternatively, a member may report a riskless principal transaction by submitting the following report(s) to ACT or NNMS:

\* \* \* \* \*

Example:

SELL as a principal 100 shares to another member at 40 to fill an existing order;

BUY as principal 100 shares from a customer at 40 minus a mark-down of \$12.50;

REPORT 100 shares at 40 by submitting to ACT or NNMS either a single trade report marked with a "riskless principal" capacity indicator or by submitting the following reports:

(1) Where required by this Rule, a tape report marked with a "principal" capacity indicator; and

(2) Either a non-tape, non-clearing report or a clearing-only report marked with a "riskless principal" capacity indicator.

#### (e) Transactions Not Required To Be Reported

The following types of transactions shall not be reported:

(1) Transactions executed through NNMS [the SmallCap Small Order Execution System (SOES), the Primex Auction System, or the SelectNet service].

\* \* \* \* \*

#### 4650. Reporting Transactions in Nasdaq Convertible Debt Securities

This Rule 4650 Series sets forth the applicable reporting requirements for transactions in convertible bonds that are listed on Nasdaq (designated securities) and reported utilizing the Automated Confirmation Transaction Service (ACT) or the Nasdaq National Market Execution System ("NNMS"), as permitted by Rule 4720.

#### 4652. Transaction Reporting

\* \* \* \* \*

#### (c) Information To Be Reported

Each last sale report shall contain the following information:

\* \* \* \* \*

(6) For any transaction in an order for which a member has recording and reporting obligations under Rules 6954 and 6955, the trade report must include:

(A) An order identifier, meeting such parameters as may be prescribed by the Association, assigned to the order that

uniquely identifies the order for the date it was received (*see* Rule 6954 (b)(1)).

(B) The time of the execution expressed in hours, minutes, and seconds. This information must be reported regardless of the period of time between execution of the trade and the ACT or NNMS trade report. All times reported to the ACT or NNMS systems shall be in Eastern Time.

#### (d) Procedures for Reporting Price and Volume\*

Members that are required, or have the option, to report transactions using ACT or NNMS, pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in designated securities in the following manner:

\* \* \* \* \*

(B) Exception: A "riskless" principal transaction in which a member, after having received an order to buy a security, purchases the bond as principal at the same price to satisfy the order to buy or, after having received an order to sell, sells the bond as principal at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee. Alternatively, a member may report a riskless principal transaction by submitting the following report(s) to ACT or NNMS:

Example:

SELL as a principal 100 shares to another member at 40 to fill an existing order;

BUY as principal 100 shares from a customer at 40 minus a mark-down of \$12.50;

REPORT 100 shares at 40 by submitting to ACT or NNMS either a single trade report marked with a "riskless principal" capacity indicator or by submitting the following reports:

(1) where required by this Rule, a tape report marked with a "principal" capacity indicator; and

(2) either a non-tape, non-clearing report or a clearing-only report marked with a "riskless principal" capacity indicator.

\* \* \* \* \*

#### 4710. Participant Obligations in NNMS

(a) Registration—Upon the effectiveness of registration as a NNMS Market Maker, NNMS ECN, or NNMS Order Entry Firm, the NNMS Participant may commence activity within NNMS for exposure to orders, *[or] entry of orders, or to report trades*, as applicable. The operating hours of NNMS may be

\* For examples of reporting procedures, refer to Rule 4632, Transaction Reporting.

established as appropriate by the Association. The extent of participation in Nasdaq by an NNMS Order Entry Firm shall be determined solely by the firm in the exercise of its ability to enter orders into Nasdaq.

\* \* \* \* \*

#### 4711. Clearance and Settlement

All transactions executed in, or reported through, NNMS shall be cleared and settled through a registered clearing agency using a continuous net settlement system.

\* \* \* \* \*

#### 4720. Reporting Through NNMS

*Subject to the conditions set forth below, members may utilize NNMS to report trades in NNMS eligible securities required or eligible to be reported to Nasdaq pursuant to the Rule 4630, 4640, 4650 and 6100 Series.*

(1) *Members shall include the time of execution on reports submitted to NNMS; and*

(2) *For transactions between members, the members who are parties to the trade shall agree to all trade details prior to submitting the report to NNMS, and have in effect and on file with Nasdaq, an Automated Confirmation Transaction Service Service Bureau/Executing Broker Supplement to the Nasdaq Workstation II Agreement ("Attachment 2 Agreement"), and a Nasdaq National Market Execution System Give-Up Addendum to the Nasdaq Workstation II Subscriber Agreement ("SuperMontage Give-Up Agreement").*

#### 5400. NASDAQ STOCK MARKET AND ALTERNATIVE DISPLAY FACILITY TRADE REPORTING

##### 5410. Applicability

(a) For a period of time, NASD will operate two facilities for collecting trade reports for executions in Nasdaq National Market, Nasdaq SmallCap Market, and Nasdaq Convertible Debt securities ("designated securities"): The Nasdaq Stock Market and the Alternative Display Facility ("ADF"). Nasdaq will continue to operate the Automated Confirmation Transaction Service ("ACT") and the Nasdaq National Market Execution System ("NNMS"), and NASD, through the ADF, will operate Trade Reporting and Comparison Service ("TRACS"). This Rule 5400 Series establishes the rules for determining which member must report a trade and whether a trade must be reported to ACT or NNMS (*as permitted by Rule 4720*), pursuant to the Rule 4630, 4640, 4650 and 6100 Series

or TRACS, pursuant to the Rule 4630A and 6100A Series.

(b) The requirements of this Rule 5400 Series are in addition to the trade reporting requirements contained in Rule Series 4630, 4640, 4650, 6100, 4630A and 6100A Series, and Rule 4720.

### 5430. Transaction Reporting

(a) When and How Transactions Are Reported

\* \* \* \* \*

(2) Non-Registered Reporting Members shall, within 90 seconds after execution, transmit through ACT, NNMS or TRACS, as applicable, or if ACT, NNMS or TRACS is unavailable due to system or transmission failure, by telephone to Market Operations Department, last sale reports of transactions in designated securities executed during normal market hours. Transactions not reported within 90 seconds after execution shall be designated as late and such trade reports must include the time of execution.

\* \* \* \* \*

(5) All members shall report as soon as practicable to the Market Regulation Department on Form T, last sale reports of transactions in designated securities for which electronic submission into ACT, NNMS or TRACS is not possible (e.g., the ticker symbol for the security is no longer available or a market participant identifier is no longer active). Transactions that can be reported into ACT, NNMS or TRACS, whether on trade date or on a subsequent date on an "as of" basis (T + N), shall not be reported on Form T.

\* \* \* \* \*

(b) Which Party Reports Transaction and to Which Facility

(1) In transactions between two Registered Reporting Nasdaq Market Makers, the member representing the sell side shall report the trade using ACT or NNMS.

(2) In transactions between a Registered Reporting Nasdaq Market Maker and a Non-Registered Reporting Member, the Registered Reporting Nasdaq Market Maker shall report the trade using ACT or NNMS.

(3) In transactions between two Non-Registered Reporting Members, the member representing the sell side shall report the trade using ACT, NNMS, or TRACS.

(4) In transactions between a member and a customer, the member shall report as follows:

(A) A Registered Reporting Nasdaq Market Maker shall report the trade using ACT or NNMS;

(B) A Registered Reporting ADF Market Maker shall report the trade using TRACS; and

(C) A Non-Registered Reporting Member shall report the trade using ACT, NNMS, or TRACS.

(5) In transactions between two Registered Reporting ADF Market Makers, the member representing the sell side shall report the trade using TRACS.

(6) In transactions between a Registered Reporting ADF Market Maker and a Non-Registered Reporting Member, the Registered Reporting ADF Market Maker shall report the trade using TRACS.

(7) In transactions between a Registered Reporting Nasdaq Market Maker and a Registered Reporting ADF Market Maker, the member representing the sell side shall report as follows:

(A) A Registered Reporting Nasdaq Market Maker shall report the trade using ACT or NNMS; and

(B) A Registered Reporting ADF Market Maker shall report the trade using TRACS.

(8) If a member simultaneously is a Registered Reporting Nasdaq Market Maker and a Registered Reporting ADF Market Maker, and has the trade reporting obligation pursuant to paragraphs (1), (2), (4), (5), (6), or (7), the member can report the trade using either ACT or NNMS, or TRACS, unless the trade is executed using ACES or [the Nasdaq National Market Execution System ("NNMS")]. A trade executed using ACES must be reported using ACT or NNMS, and trades executed using NNMS will be reported to ACT automatically.

(9) In transactions conducted through an ACT/NNMS ECN (as defined in Rule 6110) that are reported to ACT or NNMS, the ACT/NNMS ECN shall ensure that transactions are reported in accordance with Rule 6130(c). If an ACT/NNMS ECN is also a Registered Reporting ADF ECN (as defined in Rule 4200A), Rule 6130(c) shall apply only to transactions conducted through the ECN for which trade reports are submitted to ACT or NNMS.

(10) Nasdaq will append the .T modifier or the .SLD modifier, as appropriate, to those reports submitted to ACT or NNMS that contain the time of execution, but that do not contain the appropriate modifier.

### 6100. AUTOMATED CONFIRMATION TRANSACTION SERVICE (ACT)

#### 6110. Definitions

(q) The term "ACT/NNMS ECN" shall mean a member of the Association that is an electronic communications

network that is a [member] *participant* of a registered clearing agency for clearing or comparison purposes or has a clearing arrangement with such a [member] *participant*, to the extent that transactions executed through it are reported to ACT or NNMS.

### 6130. Trade Report Input

(a) Reportable ACT Transactions

*With the exception of those trades reported to Nasdaq through the Nasdaq National Market Execution System "NNMS" (as permitted by Rule 4720), [M]members shall utilize ACT to report transactions that are required to be reported to Nasdaq pursuant to the Rule Series 4630, 4640, 4650, 5430, 6400, 6500 and 6600 Series, including executions of less than one round lot if those executions are to be compared and locked-in. Members may utilize ACT to report transactions that are eligible to be reported to Nasdaq pursuant to Rule 5430, including executions of less than one round lot if those executions are to be compared and locked-in.*

*Members also may utilize NNMS to report transactions that are eligible to be reported to Nasdaq pursuant to Rule 5430, including executions of less than one round lot if those executions are locked-in. All trades that are reportable transactions will be processed through the National Trade Reporting System; however, only those trades that are subject to regular way settlement and are not already locked-in trades will be compared and locked-in through ACT. Trades that are reported as other than regular way settlement (i.e., Cash, Next-Day, Seller's Option) will not be compared in ACT or reported to NSCC. All transactions in Direct Participation Program securities shall be reported to ACT pursuant to the Rule 6900 Series as set forth therein.*

\* \* \* \* \*

(c) Which Party Inputs Trade Reports to ACT

ACT Participants shall, subject to the input requirements below, either input trade reports into the ACT system or utilize the Browse feature to accept or decline a trade within the applicable time-frames as specified in paragraph (b) of this Rule. Trade data input obligations are as follows:

\* \* \* \* \*

(5) in transactions conducted through an ACT/NNMS ECN that are reported to ACT or NNMS, the ACT/NNMS ECN shall ensure that transactions are reported in accordance with one of the following methods:

(A) The ACT/NNMS ECN shall submit the trade reports to ACT *or* NNMS and identify itself as the reporting party;

(B) The ACT/NNMS ECN shall submit the trade reports to ACT *or* NNMS on behalf of the reporting party and identify the reporting party in accordance with the rules for determining reporting parties reflected in paragraphs (1), (2), (3), and (4) above; or

(C) The ACT/NNMS ECN shall require one of the parties, determined in accordance with the rules for determining reporting parties reflected in paragraphs (1), (2), (3), and (4) above, to submit the trade reports to ACT *or* NNMS.

When an ACT/NNMS ECN reports transactions in accordance with subparagraph (A), the ACT/NNMS ECN shall be responsible for ensuring that the trade reports are accurate and contain all information required by subsection (d) of this rule for both the ACT/NNMS ECN and the identified non-reporting party. When an ACT/NNMS ECN reports transactions in accordance with subparagraph (B), both the ACT/NNMS ECN and the party identified as the reporting party shall be responsible for ensuring that the trade reports are accurate and contain all information required by subsection (d) of this rule for both the ACT/NNMS ECN and the identified reporting party. When an ACT/NNMS ECN requires reporting of transactions in accordance with subparagraph (C), the reporting party shall be responsible for ensuring the accuracy and completeness of the trade report.

An ACT/NNMS ECN shall provide written notice to the Association of the method of trade reporting used by the ACT/NNMS ECN for each of its subscribers, and may change the method of trade reporting used for a subscriber by providing advance written notice of the change to the Association;

(6) In transactions conducted through two ACT/NNMS ECNs or an ACT/NNMS ECN and an ECN that is not an ACT/NNMS ECN, an ACT/NNMS ECN shall be responsible for complying with the requirements of paragraph (5) above for reporting a transaction executed through its facilities, and an ECN that routed an order to it for execution shall be deemed to be an Order Entry Firm and a member for purposes of the rules for determining reporting parties reflected in paragraphs (1), (3), and (4) above; and

(7) In transactions conducted through an ACT/NNMS ECN in which neither of the parties is a member, the ACT/NNMS ECN shall report the transaction in

accordance with the requirements of subparagraph (5)(A) above.

\* \* \* \* \*

#### **6400. REPORTING TRANSACTIONS IN LISTED SECURITIES**

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##### **6420. Transaction Reporting**

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##### **(b) Which Party Reports Transaction**

(5) In transactions conducted through an ACT/NNMS ECN (as defined in Rule 6110), the ACT/NNMS ECN shall ensure that the transactions are reported in accordance with Rule 6130(c).

#### **6600. OVER-THE-COUNTER EQUITY SECURITIES**

\* \* \* \* \*

##### **6620. Transaction Reporting**

\* \* \* \* \*

##### **(b) Which Party Reports Transactions**

\* \* \* \* \*

(5) In transactions conducted through an ACT/NNMS ECN (as defined in Rule 6110), the ACT/NNMS ECN shall ensure that the transactions are reported in accordance with Rule 6130(c), and the term "Market Maker" as used in such rule shall be construed to refer to an OTC Market Maker.

#### **6900. REPORTING TRANSACTIONS IN DIRECT PARTICIPATION PROGRAMS**

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##### **6920. Transaction Reporting**

##### **(b) Which Party Reports Transactions**

\* \* \* \* \*

(3) In transactions conducted through an ACT/NNMS ECN (as defined in Rule 6110), the ACT/NNMS ECN shall ensure that the transactions are reported in accordance with Rule 6130(c); provided that for purposes of Rule 6130(c)(5) (B) and (C), the party with the reporting obligation shall be as set forth in Rule 6130(c)(3) and the term "Order Entry Firm" as used in such rule shall be construed to refer to any member.

\* \* \* \* \*

#### **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 proposes to provide members the ability to use SuperMontage to report trades in Nasdaq National Market and SmallCap Market securities ("Nasdaq securities") that they have matched outside of any system operated by a self-regulatory organization. Today when a member matches orders in its own system it can report the trade to Nasdaq's Automated Confirmation Transaction Service ("ACT"). Under this proposal, members now will be able to report matched trades in Nasdaq securities to SuperMontage. SuperMontage will transmit the information to ACT, where it will be processed as any other information submitted to that system. For example, the trade information will be disseminated on the consolidated tape and included in ACT risk management calculations and Nasdaq's audit trail. In addition, the trades will be submitted to the National Securities Clearing Corporation ("NSCC") for clearing, if necessary. Trades reported to SuperMontage will not be included in the SuperMontage execution algorithm, and thus will not interact with any quotes or orders in the system.

Members will not be permitted to report through SuperMontage trades for which the details have not already been compared and agreed to by the parties to the trade. This limitation is necessary because SuperMontage will not have the same functionality as ACT that allows one party to submit the trade details and the other party to review the information and affirmatively agree to the trade, or the functionality that allows ACT to compare the information submitted by each party to the trade. Members that desire to report trades using either of these methods must continue to submit reports directly to ACT.

As a result, SuperMontage will accept only: (1) Tape-only reports;<sup>6</sup> (2) locked-

<sup>6</sup> A "tape-only report" is a trade that is reported to Nasdaq for dissemination to the public, but the trade does not need to be transmitted to NSCC because one of the parties to the trade is a customer (*i.e.*, not a broker-dealer), or the buyer and seller both are broker-dealers and they have a common clearing arrangement that will enable them to settle the trade without using NSCC's facilities.

in clearing-only reports;<sup>7</sup> (3) tape reports of locked-in trades that are to be submitted to clearing;<sup>8</sup> and (4) non-clearing, non-tape reports.<sup>9</sup> A member that seeks to submit a locked-in report to SuperMontage must have agreements with its contra party that permit one or both of them to submit orders to SuperMontage on behalf of the other, and to report trades on behalf of both of the parties.<sup>10</sup>

Members will be able to report trades through SuperMontage during the hours that ACT is operational, which presently is 8:00 a.m. until 6:30 p.m. eastern time. The full reporting functionality will be implemented in phases and, when fully implemented, with the exception of those trades for which comparison through ACT is necessary, members will be able to report to SuperMontage the same types of trades they can report directly through ACT today.<sup>11</sup> In the first phase,

<sup>7</sup> A transaction is "locked-in" when the buying and selling broker-dealers have agreed to all the trade details prior to submitting the trade to Nasdaq and no further comparison is necessary. A "locked-in clearing-only report" is a report that is locked-in and Nasdaq must forward the trade to NSCC for settlement. The trade does not have to be disseminated to the public because an exception to the public reporting requirement is applicable (*e.g.*, the transaction is the offsetting leg of a riskless principal trade).

<sup>8</sup> A "tape report of a locked-in trade that is submitted for clearing" is a locked-in report of a trade that must be disseminated to the public and settled through NSCC.

<sup>9</sup> A "non-clearing, non-tape report" is a report of trade that is not required to be disseminated to the public and does not need to be transmitted to NSCC for settlement, but the broker-dealer is obligated or chooses to submit this "regulatory report" to Nasdaq. *See, e.g.*, NASD Rule 4632 (d)(3)(B) and NASD Notice to Members 00-79.

<sup>10</sup> Today a member can submit locked-in trades to ACT if it has executed an Automated Confirmation Transaction Services Service Bureau/Executing Broker Supplement to the Nasdaq Workstation II Agreement ("Attachment 2 Agreement") with its contra party and the agreement has been filed with Nasdaq. In addition, a member can submit orders to SuperMontage on behalf of another member if Nasdaq has on file a Nasdaq National Market Execution System Give-Up Addendum to the Nasdaq Workstation II® Subscriber Agreement (commonly referred to as the "SuperMontage Give-Up Agreement") that has been executed by both parties. Among other things, these agreements establish which member is responsible for settling trades. A member that wishes to report locked-in trades through SuperMontage must have on file with Nasdaq executed Attachment 2 and SuperMontage Give-Up agreements for each member for which it will report trades through SuperMontage.

<sup>11</sup> Initially, with the exception of .T and .SLD trades, SuperMontage will not accept reports of trades that must include trade report modifiers (*e.g.*, the .W modifier). During this initial phase SuperMontage also will not accept reports of trades that include special settlement conditions (*e.g.*, next-day settlement), special processing conditions (*e.g.*, reversals), or "as/of" reports, which are reports of a transaction executed on a previous day. Members will be able to submit these types of reports to SuperMontage once Nasdaq makes that

members will be able to report, among other things, the security identity, the number of shares, the price, whether the member is the buyer or seller, and whether its member is acting as agent or principal. In addition, to facilitate the reporting of pre-open, after-hours, and late reports in the first phase, members will be required to include the time of execution on all reports submitted to SuperMontage.<sup>12</sup>

The proposal is designed to provide members several benefits, including the possibility of consolidating the systems used for reporting and executing trades. In addition, members will be able to take advantage of the anonymity feature available in SuperMontage, which is not available for trades submitted directly to ACT, and combine it with the benefits of "give-up" relationships, which members utilize today in SuperMontage and ACT.<sup>13</sup> The result is that a member will be able to give up the true contra parties to a trade, but still preserve full anonymity between these parties.

For example, today ECNs match buyers and sellers in their own systems and provide anonymity by becoming the contra party to each party. With the proposed feature, the ECN could submit the same matched order to SuperMontage for anonymous processing and give up the parties that matched in its system. Now, instead of the ECN being the contra party, the parties that matched through the ECN will be direct contra parties. Full anonymity (*i.e.*, anonymity through settlement) will be preserved because the actual buyer and seller will be informed that SIZE is their contra party, just the same as today when they trade

necessary system changes. *See infra* note 12 for a discussion concerning reporting .T and .SLD trades to SuperMontage.

<sup>12</sup> Today, ACT automatically appends the .SLD modifier or .T modifier, as appropriate, to reports it receives that contain the time of execution. ACT compares the time of execution to the time the report was received by ACT, and if more than 90 seconds has elapsed between these times and the report does not contain the .SLD modifier, ACT will append the .SLD modifier. Similarly, ACT will read the time of execution, and if this time is outside normal market hours and the .T modifier is not included on the report, ACT will append the .T modifier. Therefore, requiring members to include the time of execution on reports submitted to SuperMontage will enable them to submit late reports and reports of pre-open and after-hours trades, because ACT will validate the time of execution and automatically append the .SLD modifier or the .T modifier, as appropriate.

<sup>13</sup> When a "give-up" occurs, the member that submits the order to SuperMontage (or the trade report to ACT) discloses to the contra party that the order (or report) is being entered on behalf of another member and the trade is to be settled with this other member. The member submitting the order (or trade report) has "given up" the identity of the other member who is the true party to the trade.

fully anonymously, using SIZE in SuperMontage's Non-Directed Order processing.

The processing of fully anonymous trades is the same regardless of whether the trade is executed as a result of a match occurring in the Non-Directed Order processing or matched in a member's own system and submitted to SuperMontage for reporting purposes. For example, the identities of all the parties (buyer, seller, and reporting member) will be known to Nasdaq and NSCC at all times.<sup>14</sup> In addition, the anonymous trades reported through SuperMontage will be included in the risk management reports Nasdaq issues each day, and Nasdaq will reveal contra party identities to members on a trade-by-trade basis if NSCC ceases to act for the buyer or seller, or one of their clearing firms.<sup>15</sup>

## 2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,<sup>16</sup> in general and with Section 15A(b)(6) of the Act,<sup>17</sup> in particular, in that it is designed to foster coordination and cooperation with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities. Nasdaq asserts that the proposal is consistent with this obligation because it will provide members both the opportunity to consolidate the execution and reporting of trades and to combine the benefits give-up relationships and anonymous trading.

### B. Self-Regulatory Organization's Statement on Burden on Competition

Nasdaq does not believe that the proposed rule change would 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.

<sup>14</sup> A detailed description of the processing of anonymous orders in SuperMontage is contained in the Commission's order approving the anonymity feature. *See* Securities Exchange Act Release No. 48527 (September 23, 2003), 68 FR 56361 (September 30, 2003).

<sup>15</sup> NSCC's authority to cease to act for one of its participants is contained in NSCC Rule 46.

<sup>16</sup> 15 U.S.C. 78o-3.

<sup>17</sup> 15 U.S.C. 78o-3(b)(6).

### 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) of the Act<sup>18</sup> and subparagraph (f)(5) of Rule 19b-4<sup>19</sup> thereunder because it effects a change in an existing order entry or trading system that (i) does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) does not have the effect of limiting access to or availability of the system. 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.<sup>20</sup>

Nasdaq believes that the proposed rule change, as amended, is consistent with these requirements because it proposes to add a reporting feature to SuperMontage, an existing order-entry system that will not have any affect on the protection of investors. Members are being provided an alternative means to report the types of trading they already conduct today, and the anonymity feature is the same as currently exists in SuperMontage. In addition, the functionality added by the proposed rule change is optional, and thus does not limit access to SuperMontage. Nasdaq states that it will make the proposed rule change operative as the necessary system changes are completed. Nasdaq expects to implement the first phase of the proposal on or about July 15, 2004. Nasdaq has represented that it will issue a Head Trader Alert informing members of the implementation schedule once the exact dates are determined.

### 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:*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASD-2004-034 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-2004-034. 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 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-2004-034 and should be submitted on or before June 16, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>21</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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### SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49738; File No. SR-NASD-2004-072]

#### **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**

May 19, 2004.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> 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 Act<sup>3</sup> and Rule 19b-4(f)(2) thereunder,<sup>4</sup> which renders the proposal effective upon filing. On May 4, 2004, Nasdaq filed Amendment No. 1 to the proposed rule change.<sup>5</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

#### **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*.

\* \* \* \* \*

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>4</sup> 17 CFR 240.19b-4(f)(2).

<sup>5</sup> 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)).

<sup>18</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>19</sup> 17 CFR 240.19b-4(f)(5).

<sup>20</sup> For purposes of calculating the 60-day abrogation period, the Commission considers the period to commence on April 27, 2004, the date Nasdaq filed Amendment No. 1.

<sup>21</sup> 17 CFR 200.30-3(a)(12).