

entered; and (2) to amend Article VI, Section 3 of the NASD By-Laws to clarify that NASD may suspend the association, and not just the registration, of any person who fails to pay an arbitration award. Notice of the proposed rule change was published for comment in the **Federal Register** on May 7, 2004.<sup>3</sup> The Commission received one comment on the proposed rule change.<sup>4</sup> This order approves the proposed rule change.

## II. Description of Proposed Rule Change

The proposed rule change amends Article V, Section 4 of the NASD By-Laws to provide that, for the limited purpose of instituting proceedings for failure to pay arbitration awards or settlements, NASD retains, for a period of two years after the entry of the award or settlement, jurisdiction to impose suspensions against former associated persons if the award or settlement resulted from a claim submitted for arbitration or mediation pursuant to the NASD Rules. The proposal addresses NASD's concern that a person associated with a member will terminate his or her association with the member once aware that an arbitration award may be entered against him or her in order to avoid sanction by NASD for failure to pay any award or settlement agreement resulting from the proceeding. In addition, the proposed rule change amends Article VI, Section 3 of the NASD By-Laws to clarify that NASD may suspend any person from associating with a member in any capacity for failure of such person to comply with an arbitration award or settlement.

## III. Discussion

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.<sup>5</sup> Specifically, the Commission finds that the proposal is consistent with Section 15A(b)(6) of the Act,<sup>6</sup> which requires, among other things, that NASD's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the

<sup>3</sup> See Securities Exchange Act Release No. 49636 (April 30, 2004), 69 FR 25652 ("Notice").

<sup>4</sup> See e-mail dated May 28, 2004 from Douglas K. Traynor. The e-mail did not raise any issues with respect to the substance of the proposed rule change.

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

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

public interest. The Commission believes that the amendments should improve NASD's ability to ensure that its membership is not likely to engage in conduct that may be harmful to public investors. The Commission notes that the proposed rule change strengthens NASD's ability to prevent persons who fail to honor securities-related arbitration awards from seeking to re-enter the securities business, and clarifies that persons who fail to honor such awards may be suspended from associating with NASD members in any capacity.

## IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>7</sup> that the proposed rule change (File No. SR-NASD-2003-69) be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49833; File No. SR-NASD-2004-056]

### 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

June 8, 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 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.<sup>3</sup> Nasdaq has

<sup>1</sup> 15 U.S.C. 78s(b)(2).

<sup>2</sup> 17 CFR 200.30-3(a)(12).

<sup>3</sup> 15 U.S.C. 78s(b)(1).

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

<sup>5</sup> 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").

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,<sup>4</sup> and Rule 19b-4(f)(1)<sup>5</sup> 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.

## 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.

\* \* \* \* \*

### 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).*

\* \* \* \* \*

## 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

<sup>4</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>5</sup> 17 CFR 240.19b-4(f)(1).

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.<sup>6</sup> On June 29, 1994, the Commission approved the NASD's short sale rule applicable to short sales<sup>7</sup> in NNM securities on an eighteen-month pilot basis through March 5, 1996 (the "Short Sale Rule").<sup>8</sup> 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 securities,<sup>9</sup> 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)<sup>10</sup> 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 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)<sup>11</sup> of the Act, and subparagraph (f)(1) of Rule 19b-4

thereunder,<sup>12</sup> 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.<sup>13</sup>

**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-2004-056 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.,

<sup>12</sup> 17 CFR 240.19b-4(f)(1).

<sup>13</sup> 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.

<sup>6</sup> 17 CFR 240.10a-1.

<sup>7</sup> 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).

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

<sup>9</sup> See ACT Notice 94-1 (August 22, 1994).

<sup>10</sup> 15 U.S.C. 78o-3(b)(6).

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A)(i).

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 July 8, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>14</sup>

**Margaret H. McFarland,**  
Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49842; File No. SR-NASD-2004-071]

### Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. Regarding Improved Nasdaq Opening Process

June 9, 2004.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on April 23, 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 27, 2004, Nasdaq amended the proposed rule change.<sup>3</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 is filing the proposed rule change to improve the opening process

for Nasdaq securities. There are four components of the proposal: (1) Modification of the pre-market hours trading environment for all Nasdaq securities, including the elimination of the Trade-or-Move process contained in Rule 4613(e) and the opening of quotations at 9:25 a.m. rather than 9:29:30 a.m.; (2) the creation of voluntary On Open, Imbalance Only, and Extended Hours order types ("Nasdaq Opening Orders") and the application of new time-in-force rules for existing orders; (3) the creation of the Nasdaq Opening Cross; and (4) the creation of a Modified Opening Process for Nasdaq-listed securities that do not participate in the Nasdaq Opening Cross. The text of the proposed rule change is set forth below.<sup>4</sup> Proposed new language is in *italics*; deletions are in [brackets].<sup>5</sup>

\* \* \* \* \*

#### 4613. Character of Quotations

- (a)-(d) No Change.  
(e) Locked and Crossed Markets.

(1) A market maker shall not, except under extraordinary circumstances, enter or maintain quotations in Nasdaq during normal business hours if:

- (A) No Change.  
(B) No Change.

[(C) Obligations Regarding Locked/Crossed Market Conditions Prior to Market Opening.

(i) Locked/Crossed Market Prior to 9:20 a.m.—For locks/crosses that occur prior to 9:20 a.m. Eastern Time, a market maker that is a party to a lock/cross because the market maker either has entered a bid (ask) quotation that locks/crosses another market maker's quotation(s) or has had its quotation(s) locked/crossed by another market maker ("party to a lock/cross") may, beginning at 9:20 a.m. Eastern Time, send a Directed Order of any size that is at the receiving market maker's quoted price

<sup>4</sup> The Commission made the following corrections to the proposed rule text: (1) Internal cross references in proposed Rule 4704(a)(2)(a)(i) and (iii) were corrected; and (2) the title of Rule 4710 was corrected. Telephone conversation between Jeffrey S. Davis, Associate Vice President and Associate General Counsel, Nasdaq, and Ann E. Leddy, Special Counsel, Division, Commission (June 8, 2004).

<sup>5</sup> The proposed rule change is marked to show changes from the rule text appearing in the NASD Manual available at [www.nasd.com](http://www.nasd.com), as amended by the following: SR-NASD-2003-149 (Securities Exchange Act Release No. 49349 (March 2, 2004), 69 FR 10775 (March 8, 2004)); SR-NASD-2004-046 (Securities Exchange Act Release No. 49547 (April 9, 2004), 69 FR 20091 (April 15, 2004)); SR-NASD-2004-064 (Securities Exchange Act Release No. 49650 (May 4, 2004), 69 FR 25941 (May 10, 2004)); SR-NASD-2004-051 (Securities Exchange Act Release No. 49597 (April 21, 2004), 69 FR 23244 (April 28, 2004)); and SR-NASD-2004-076 (filed on an immediately effective basis on May 5, 2004).

("Trade-or-Move Directed Order"). Exception: A market maker that is a party to a lock/cross may not send such an order to the SIZE MMID.

(ii) Locked/Crossed Market Between 9:20 and 9:29:29 a.m.—

a. Before an ECN enters a quote that would lock or cross the market between 9:20 and 9:29:59 a.m. Eastern Time, the ECN must first send a Trade-or-Move Directed Order to the market maker or ECN whose quote it would lock or cross that is at or superior to the receiving market maker's or ECN's quoted price. An ECN that sends a Trade-or-Move Directed Order during these periods must then wait at least 10 seconds before entering a quote that would lock or cross the market. Exception: An ECN is not required to send such an order to the SIZE MMID.

b. If a market maker enters a quote that would lock or cross the market between 9:20 and 9:29:29 a.m. Eastern Time, the market maker must then immediately send a Trade-or-Move Directed Order to the market maker or ECN whose quote it would lock or cross that is at or superior to the receiving market maker's or ECN's quoted price. Exception: A market maker is not required to send such an order to the SIZE MMID.

c. If any market participant enters a quote that would lock or cross the market between 9:29:30 and 9:29:59, that quote will be processed as set forth in Rule 4710(b)(3)(B).

(iii)

a. In the case of securities included in the Nasdaq 100 Index or the S&P 400 Index, a Trade-or-Move Directed Order must be at least 10,000 shares (if multiple market makers would be locked/crossed, each one must receive a Trade-or-Move Directed Order and the aggregate size of all such messages must be at least 10,000 shares); provided, however, that if a market participant is representing an agency order (as defined in subparagraph (vi) of this rule), the market participant shall be required to send a Trade-or-Move Directed Order(s) in an amount equal to the agency order, even if that order is less than 10,000 shares.

b. In the case of all other securities, a Trade-or-Move Directed Order must be for at least 5,000 shares (if multiple market makers would be locked/crossed, each one must receive a Trade-or-Move Directed Order and the aggregate size of all such orders must be at least 5,000 shares); provided, however, that if a market participant is representing an agency order (as defined in subparagraph (vi) of this rule), the market participant shall be required to send a Trade-or-Move Directed Order(s)

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> See letter from Mary M. Dunbar, Vice President and Deputy General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation ("Division"), Commission, dated May 26, 2004 ("Amendment No. 1"). In Amendment No. 1, Nasdaq restated the proposed rule change in its entirety.