

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-58569; File No. SR-NASDAQ-2008-033)

September 17, 2008

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving Proposed Rule Change as Modified by Amendment Nos. 1 and 2 Related to Submission of Non-Tape Reports

I. Introduction

On April 18, 2008, The NASDAQ Stock Market LLC (“Nasdaq”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act” or “Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change related to submission of non-tape reports. On July 3, 2008, Nasdaq filed Amendment No. 1 to the proposed rule change. The proposed rule change was published for comment in the Federal Register on July 11, 2008.³ Two comments were received in support of the proposed rule change.⁴ On August 11, 2008, Nasdaq filed Amendment No. 2 to the proposed rule change to make certain technical, non-substantive modifications to the original rule filing. This order approves the proposed rule change, as amended.

II. Description of the Proposal

The proposed rule change would: expand the scope of step-outs⁵ to include all securities transfers from one Nasdaq member to another provided the transfer does not constitute a

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 58101 (July 3, 2008), 73 FR 40002.

⁴ See e-mail from Kirk Allen, Managing Director, Trading, NWQ Investment Management, dated August 1, 2008 (“NWQ Investment Letter”) and letter from William D. Edick, Pickard and Djinis LLP, to Florence E. Harmon, Acting Secretary, Commission, dated September 11, 2008 (“Pickard Letter”).

⁵ Nasdaq states that a step-out is a clearing entry used to transfer a broker’s position in a security to another broker, or within accounts at a firm.

reportable trade,⁶ eliminate the requirement for an authorizing agreement when Nasdaq members use the Automated Confirmation Transaction service (“ACT”) to effect a step-out along with the transfer of a sales fee or similar fee,⁷ describe riskless transactions,⁸ state that members may not use the step-out function in lieu of reporting a trade,⁹ and establish a fee for the use of the step-out function to transfer a transaction fee.¹⁰

Nasdaq will allow members to submit records for riskless transfers using the following capacities: “Riskless Principal” where the member acted as principal on the trade or trades related to the riskless submission; “Agent” where the member acted as agent on the trade or trades related to the riskless submission; and “Intra-Broker” where the transfer is occurring strictly within a member firm.

Transaction Fees

According to Nasdaq, trade reporting rules of other SROs allow transaction fees to be included in clearing reports. Nasdaq proposes to permit members to include transaction fees in clearing reports submitted under Rule 7038 or 7042, if the members agree in advance to transfer the transaction fee and if they are parties to a written agreement permitting the submission of fee-inclusive clearing reports. Nasdaq would allow members to transfer to another Nasdaq member transaction fees using the clearing reports that Nasdaq forwards to the National Securities

⁶ Rule 7038(b).

⁷ Rule 7038(c).

⁸ Rule 7042. Nasdaq states that this requirement follows the general standard for riskless principal transactions articulated in Financial Industry Regulatory Authority (“FINRA”) Rule 4632(d)(3)(B).

⁹ Rule 7038(d), 7042(b) and 7043(a).

¹⁰ Rule 7043.

Clearing Corporation (“NSCC”) to clear a trade. Nasdaq will impose a fee of \$0.03 per-side for each such clearing report.¹¹

Step-Outs

A step-out is a transfer of all or a portion of a broker-dealer’s securities position to another broker-dealer which transfer does not constitute a trade. According to Nasdaq, this proposal builds upon previous attempts to provide step-out parameters for its members. Nasdaq initially offered step-out capability in 2007 because FINRA rules restricted the use of step-outs to those portions of trades that were originally executed by, and reported to, FINRA facilities.¹² Certain broker-dealers wished to engage in step-outs but did not have systems in place to capture the venue of the original trade execution and/or they may have executed various portions of the underlying trade in non-FINRA facilities. FINRA rules do not permit the use of step-outs under these conditions. Accordingly, Nasdaq amended its rules to allow the use of step-outs in connection with any trade to which a Nasdaq member was a party regardless of the market on which the trade was executed.¹³

Nasdaq amended its step-out rules again in 2007 to require clearing member firms that wanted to transfer certain sales fees without transferring the underlying shares to have an authorizing agreement. No authorizing agreement is required when Nasdaq members conduct step-outs if the transfers are limited to transfer of the underlying shares.¹⁴

¹¹ Nasdaq states that under NASD Rule 7002B, FINRA/Nasdaq TRF participants are charged a fee of \$0.03 per side for submission of a clearing report to transfer a transaction fee charged by one FINRA member to another.

¹² See Securities Exchange Act Release No. 56345 (August 31, 2007), 72 FR 51880 (September 11, 2007).

¹³ Id.

¹⁴ See Securities Exchange Act Release No. 56929 (December 7, 2007), 72 FR 71176 (December 14, 2007).

Nasdaq is again expanding its step-out parameters: first, it proposes to expand the scope of step-outs to include all securities transfers from one Nasdaq member to another provided that the transfer does not constitute a reportable trade; second, Nasdaq is eliminating the requirement for an authorizing agreement when Nasdaq members use ACT to effect a step-out along with the transfer of a sales or similar fee.¹⁵ Third, Nasdaq is reiterating in its rules that step-outs are not trade reports and cannot be used as such and reminding members of the need to comply with trade reporting rules of other SROs governing a particular transaction.¹⁶ Finally, Nasdaq is implementing a fee for step-outs that also transfer a transaction fee.

Nasdaq believes that the above changes will enhance the ability of Nasdaq members to transfer securities positions and their associated fees in an efficient and transparent manner.

III. Discussion and Commission Findings

After careful consideration, 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 exchange¹⁷ and, in particular, the requirements of Section 6 of the Act.¹⁸ Specifically, the Commission finds that the proposed rule change is consistent with Section

¹⁵ Nasdaq represents that step-outs are already completed pursuant to formal agreements among Nasdaq members or through ACT's comparison processes, which renders the current requirement for an authorizing agreement duplicative.

This proposed rule change would not change the requirement of a formal sales fee transfer agreement between firms that wish to use ACT to move sales fees without an accompanying transfer of securities. Nasdaq believes that it is important to retain the requirement that the parties to a fee transfer have a written agreement specifically permitting the fee transfers because a sales fee transfer that moves no shares is not a step-out and therefore there are no specific share movements for firms to readily identify as being associated with the fee transfer.

¹⁶ See Rules 7038(d), 7042(b) and 7043(a).

¹⁷ In approving this proposed rule change the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹⁸ 15 U.S.C. 78f.

6(b)(5) of the Act,¹⁹ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, 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 mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. Nasdaq's proposal to expand the use of step-outs, as described above should enhance the efficiency and transparency to members of their post-trade operations.

The Commission received two comment letters on the proposed rule change.²⁰ One commenter expressed support for Nasdaq's proposal and stated it believes Nasdaq's proposal will bring added transparency.²¹ The other commenter questioned the impact this proposed rule change may have on Exchange Act Rule 10b-10²² disclosure requirements.²³

Nasdaq's proposal to allow submission of non-tape, riskless principal reports through ACT should facilitate the transfer of information between parties to the transaction and make the trade record information electronically available. It can facilitate the ultimate transmission of the

¹⁹ 15 U.S.C. 78f(b)(5).

²⁰ See supra note 4.

²¹ See NWQ Letter, supra note 4.

²² 17 CFR 240.10b-10.

²³ See Pickard Letter, supra note 4. The Commission believes that this comment raises an interpretive question regarding the applicability of Exchange Act Rule 10b-10 and is outside of the scope of NASDAQ's proposed rule change. Procedures applicable to requests for no-action and interpretive letters from the Division of Trading and Markets are available in Securities Act Release No. 6269 (December 5, 1980) (available at: <http://www.sec.gov/rules/other/33-6269.pdf>).

transfer records to the appropriate clearing agency.²⁴ The Commission notes that Nasdaq members can not satisfy any trade reporting obligations by submitting non-tape, clearing, or non-tape, non-clearing records to ACT. Furthermore, the Commission expects Nasdaq to monitor the expanded use of the step-out functionality to ensure that its members use these position movements as specified in the rule, and not to effect trades.

Nasdaq's proposal to allow the transfer of fees in conjunction with the step-out is analogous to rules of other SROs which allow transaction fees to be included in clearing reports.²⁵ The Commission understands that although Nasdaq no longer requires members to have agreements in place for step-out transactions, the transaction comparison process itself requires the acquiescence of both parties for the ACT system to complete the transaction. A member retains the opportunity to manually reject or reverse the step-out and fee transfer arrangement if it disagrees with their terms when the terms are presented to the member even after the step-out and fee transfer had initially been affirmed.²⁶

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular Section 6 of the Act and the rules and regulations thereunder.

²⁴ The Commission notes that Nasdaq represents it will continue to honor Attachment 2's and Uniform Trade Reporting Agreements on file with it or the FINRA/Nasdaq TRF.

²⁵ When a firm uses this function the fee will be electronically billed and collected.

²⁶ Nasdaq represents that it determined through discussions with its member firms that many firms preferred to handle step-outs on a match/compare basis, i.e. manually, even when they had a fee agreement between them and that it was an unnecessary burden for firms to sign separate agreements to move fees associated with step-out submissions to ACT since this functionality already was in place on ACT.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (File No. SR-NASDAQ-2008-033), as modified by Amendments No. 1 and 2, be and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁷

Florence E. Harmon
Acting Secretary

²⁷ 17 CFR 200.30-3(a)(12).