

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-56237; File No. SR-NASDAQ-2007-043)

August 9, 2007

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving a Proposed Rule Change, as Modified by Amendments No. 1 and 2, to Remove Provisions Governing the Operation of the ACES System

I. Introduction

On April 25, 2007, The NASDAQ Stock Market LLC (“Nasdaq” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”)¹ and Rule 19b-4 thereunder,² a proposal to remove its rule provisions governing the operation of the ACES system. The Exchange filed Amendments No. 1 and 2 to the proposed rule change on May 29, 2007, and June 5, 2007, respectively. The proposal was published for comment in the Federal Register on June 18, 2007.³ The Commission received no comments on the proposal. This order approves the proposed rule change, as modified by Amendments No. 1 and 2.

II. Description of the Proposal

The Exchange proposes to delete the Rule 6200 Series and Rule 7026, which govern the operations of the ACES system. The Exchange’s rule book contains rules pertaining to “facilities” of the exchange, and the Exchange believes that ACES is not a “facility” within the meaning of the Act.

The ACES system is a neutral communications service that allows Nasdaq members and non-members to route orders to one another. Market participants may execute orders received

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 55892 (June 11, 2007), 72 FR 33550 (“Notice”).

through ACES in any manner that they deem consistent with duties of best execution and other applicable industry obligations. ACES does not effect trade executions or report executed trades to the consolidated tape. Because ACES merely allows market participants to route orders to one another for execution and does not effect trade executions or report executed trades to the consolidated tape, the Exchange does not believe that ACES constitutes a facility of a national securities exchange within the meaning of the Act, nor does it believe it is required to file or maintain rules regarding the operation of ACES.

In the past, when Nasdaq's parent entity, The Nasdaq Stock Market, Inc., was a subsidiary of the National Association of Securities Dealers, Inc. ("NASD"), ACES rules were not included in the NASD Manual, based on Nasdaq's and NASD's understanding that ACES is not a facility of the NASD. These rules were, nevertheless, approved as Nasdaq rules in connection with Nasdaq's registration as a national securities exchange. Nasdaq now proposes the deletion of these rules based on its conclusion that ACES is not a Nasdaq facility and that therefore these rules are not required under the Act. However, Nasdaq represented that it would file a proposed rule change if ACES were modified in a manner that caused it to be deemed an exchange facility or if ACES fees were tied to fees for, or usage of, exchange services.

III. Discussion

After careful consideration, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.⁴ In particular, the Commission finds that the

⁴ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

proposal is consistent with Section 6(b) of the Act,⁵ because the ACES system is not a “facility” of the Exchange as that term is defined in Section 3 of the Act.⁶

Sections 6(b)⁷ and 19(b)(1)⁸ of the Act and Rule 19b-4 thereunder⁹ require a national securities exchange to file its rules with the Commission. Section 3(a)(27) of the Act¹⁰ and Rule 19b-4 define the “rules” of an exchange with reference to its “facilities.” In particular, a rule of an exchange includes “any material aspect of the operation of the facilities” of the exchange or any statement with respect to “the rights, obligations or privileges” of exchange members or persons having or seeking access to the facilities of the exchange.¹¹ Section 3(a)(2) of the Act defines “facility,” when used with respect to an exchange, to include:

its premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any services thereof for the purpose of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service.¹²

The Commission agrees with the Exchange’s conclusion that ACES, as currently operated, is not a facility of the Exchange. The Exchange has represented that ACES is a “pure router” that allows one subscriber (the “routing subscriber”) to send an order from a Nasdaq

⁵ 15 U.S.C. 78f(b).

⁶ See 15 U.S.C. 78c(a)(2).

⁷ 15 U.S.C. 78f(b).

⁸ 15 U.S.C. 78s(b)(1).

⁹ 17 CFR 240.19b-4.

¹⁰ 15 U.S.C. 78c(a)(27).

¹¹ 17 CFR 240.19b-4.

¹² 15 U.S.C. 78c(a)(2).

workstation directly to the order management system of another ACES subscriber (the “receiving subscriber”). Moreover, the Exchange has represented that the ACES system is not linked with the Exchange’s core systems, including the Nasdaq Market Center, the Exchange’s automated system for order execution and trade reporting. It is not possible for an order to be routed to the Nasdaq Market Center via the ACES system.

Once an order has been routed through ACES, the receiving subscriber may execute the order in any manner it determines to be consistent with its duty of best execution and other applicable regulatory obligations. The receiving subscriber is not required to route the order to, or execute the order on, the Nasdaq Market Center. Because the ACES system does not route orders to the Exchange, the Commission agrees with the Exchange’s conclusion that ACES does not have the “purpose of effecting . . . a transaction on an exchange.”¹³

The Exchange has also represented that ACES does not report executed trades. Rather, the receiving subscriber is responsible for ensuring that the execution of each order sent through ACES is reported in accordance with the applicable rules of the market center where the order was executed.¹⁴ Thus, the Commission similarly agrees with the Exchange’s conclusion that ACES does not have the “purpose of . . . reporting a transaction on an exchange.”¹⁵

A consequence of deleting the ACES rules from the Exchange’s rule book is that the Exchange will be able to change its ACES rules without providing public notice via filing of proposed changes with the Commission under Section 19(b) of the Act. However, the Commission notes that if the Exchange seeks to modify the operations of the ACES system in a

¹³ See 15 U.S.C. 78c(a)(2).

¹⁴ The ACES rules require the receiving subscriber to send an execution message to ACES so that ACES may notify the routing subscriber of the terms of the execution, see Nasdaq Rule 6250, but this does not constitute the “reporting” of the transaction.

¹⁵ See 15 U.S.C. 78c(a)(2).

manner that would cause the system to fit within the definition of an exchange facility, the Exchange would be required to file a proposed rule change with the Commission pursuant to Section 19(b) of the Act. For example, if the Exchange were to tie ACES fees in any way to fees for, or usage of, any Exchange services (for example, by offering a discount in ACES fees as an incentive for use of Exchange services, or vice versa), the Commission would consider such fees to be Exchange fees that must be filed with the Commission pursuant to Section 19(b) of the Act.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁶ that the proposed rule change (File No. SR-NASDAQ-2007-043), as modified by Amendments No. 1 and 2, be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁷

Florence E. Harmon
Deputy Secretary

¹⁶ Id.

¹⁷ 17 CFR 200.30-3(a)(12).