

Market, Inc. permitted ECN/ATs to remain on SelectNet (an order delivery system) for inbound executions against the ECN/ATs' displayed quotations rather than requiring them to migrate to the automatic execution methodology of the Nasdaq National Market Execution System ("NNMS").⁹ Nasdaq even amended its Intermarket Trading System ("ITS") / Computer Assisted Execution System ("CAES") (together, "ITS/CAES") definitions and functionality to permit ECN/ATs to operate in an order delivery format when interacting with inbound commitments from ITS. Similarly, CSE now proposes to permit members to select order delivery and automated response for order interaction with displayed quotations within the CSE System or to continue interacting through CSE's automatic execution facility.

In an order delivery and automated response system, a member's quotation or displayed order will be held in the CSE System, and when a contra-side order is received in the CSE System, CSE will immediately forward the order message to the quoting member, who will be obligated by rule to respond instantaneously to the order message. Moreover, the quoting member must have a demonstrated capability to respond instantaneously to the order message. On receipt of the order message delivered by CSE, the quoting member will automatically determine whether its quote is still active. If so, the member will automatically deliver to the CSE System matched orders representing its quote and the contra-side for execution. If the member's quote is in the process of changing due to a prior internal match at the displayed price, consistent with the Firm Quote Rule,¹⁰ the member will reject the inbound order and send it back to the CSE System. The CSE System will then automatically send a cancellation message to the member submitting the order. The entire duration of the order delivery and automated response process likely will be less than one second.

CSE will require that members demonstrate the capacity to accept inbound orders and to automatically respond to the CSE System before they will be permitted use of this functionality. Moreover, CSE Rule

11.9(i)(2) provides that the CSE System will offer order delivery and automated response subject to the requirement that members demonstrate the capability to respond in an automated manner.

Therefore, by rule and through demonstrated capacity verified by CSE examiners before operation, the CSE will reduce the risk of multiple execution liability, while ensuring that members comply with their obligations under the Firm Quote Rule.

III. Discussion

The Commission finds that the proposed rule change, as amended, is consistent with the provisions of section 6(b) of the Act,¹¹ in general, and section 6(b)(5) of the Act,¹² in particular, which requires, among other things, that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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.

The Commission believes that the proposal furthers the purpose of this section by reducing the risk of dual liability to CSE members. By reducing the risk of dual liability, the proposal may encourage CSE members, such as ECNs, to display larger sized quotations thereby adding liquidity and transparency to the market. Moreover, the Commission approved a similar approach to reducing the risk of dual liability in the Nasdaq market and believes that CSE's proposal should similarly benefit all market participants in the Nasdaq and listed markets. The Commission believes that the proposal's requirement that CSE members demonstrate the ability to process inbound orders and respond appropriately within one second should facilitate the efficient functioning of the order delivery and automated response execution option. The Commission believes that encouraging greater participation in the national market system by market participants, including ECNs, furthers the Congressional goal of developing a comprehensive national market system.

It is important to note that, upon approval of the instant proposal, a CSE member (or other market participant routing an order to the CSE via ITS) may attempt to execute a trade at a price quoted on the CSE by an ECN. In such

a case, a CSE member (or ITS user) submitting an order to the CSE's NSTS may not receive an execution at the price originally quoted by the ECN on the CSE, because the ECN may have adjusted its quoted price while the order was in transit from the CSE to the ECN. CSE represents that this transit time is less than one second, and, for firm quote rule¹³ compliance purposes, the Commission believes this time to be *de minimis*. Moreover, the Commission believes it is significant that this one-second transit time is generally less than the internal transmission time of order routing systems in place in other markets.

CSE has committed to examine regularly for patterns of adjustments in ECNs' quoted prices that lead to the rejection of orders. Specifically, the CSE will analyze those rejections that occur after an order arrives at the CSE and before the order arrives at the ECN. Should any such patterns be detected, CSE will scrutinize them for violations of the Firm Quote Rule and take appropriate action. The CSE has also committed to reporting the results of its examination of ECN order rejection patterns to the Commission.

IV. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,¹⁴ that the proposed rule change (SR-CSE-2002-04), as amended, is hereby approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46893; File No. SR-NASD-2002-167]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Amendments to NASD Rule 7010(k)—Fees for the Trade Reporting and Compliance Engine (TRACE)

November 22, 2002.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934

⁹ See Securities Exchange Act Release No. 42344 (January 14, 2000), 65 FR 3987 (January 25, 2000) in which Nasdaq designated SelectNet as the link to ECNs pursuant to the SEC's Order Handling Rules. See Securities Exchange Act Release No. 38156 (January 10, 1997), 62 FR 2415 (January 16, 1997).

¹⁰ 17 CFR 240.11Ac1-1.

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

¹² 15 U.S.C. 78f(b)(5).

¹³ SEC Rule 11Ac1-1, 17 CFR 240.11Ac1-1 ("Firm Quote Rule").

¹⁴ 15 U.S.C. 78s(b)(2).

¹⁵ 17 CFR 200.30-3(a)(12).

(“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on November 15, 2002, the National Association of Securities Dealers, Inc. (“NASD”), filed with the Securities and Exchange Commission (“Commission” or “SEC”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. NASD has designated the proposed rule change as “establishing or changing a due, fee, or other charge” under Section 19(b)(3)(A)(ii) of the Act³ and Rule 19b-4(f)(2) thereunder,⁴ which renders the proposal effective upon filing with the Commission. In addition, the NASD is changing references in the text of the

rule from “the Association” to “NASD.” This change is effective immediately pursuant to Section 19(b)(3)(A)(iii) of the Act,⁵ as it is concerned solely with the administration of the self-regulatory organization. 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

NASD is proposing to amend NASD Rule 7010(k) to reduce certain fees that are currently in effect for the Trade Reporting and Compliance Engine

(TRACE). Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

Rule 7010(k) Trade Reporting and Compliance Engine (TRACE)

(Rule 7010(k) shall expire on December 28, 2002, unless amended, extended, or permanently adopted by NASD pursuant to SEC approval at or before such date).

The following charges shall be paid by participants for the use of the Trade Reporting and Compliance Engine (“TRACE”):

System fees	Transaction reporting fees	Market data fees
Web Browser Access: \$85/month for 1 user ID; \$75/month for 2–9 user IDs; \$70/month for 2–10+ user IDs. <i>If less than 25 trades per month, in October, November, or December 2002—\$25/month per user ID.</i> CTCI—\$25/month/line Third Party—\$25/month	Trades up to and including \$200,000 par value—\$0.50/trade; Trades between \$201,000 and \$999,999 par value—\$0.0025 times the number of bonds traded/trade; Trades of \$1,000,000 par value or more—\$2.50/trade. Cancel/Correct—\$3/trade: <i>For October 2002—\$1.50/trade. For November 2002—\$2.25/trade.</i> “As of” Trade Late—\$3/trade: <i>For October 2002—\$1.50/trade. For November 2002—\$2.25/trade.</i>	BTDS Professional Display—\$60/month per terminal. BTDS Internal Usage Authorization—\$500/month per organization. BTDS External Usage Authorization— \$1,000/month per organization. Daily List Fax—\$15/month per fax number/addressee.

(1) System Related Fees. There are three methods by which a member may report corporate bond transactions that are reportable to NASD [the Association] pursuant to the Rule 6200 Series. A member may choose among the following methods to report data to NASD [the Association]: (a) a TRACE web browser (either over the Internet or a secure private data network (“PDN”)); (b) a Computer-to-Computer Interface (“CTCI”) (either one dedicated solely to TRACE or a multi-purpose line); or (c) a third-party reporting intermediary. Fees will be charged based on the reporting methodology selected by the member.

(A) Web Browser Access. The charge to be paid by a member that elects to report TRACE data to NASD [the Association] via a TRACE web browser shall be as follows: for the first user ID registered, a charge of \$85 per month; for the next two through nine user IDs registered, a charge of \$75 per month, per such additional user ID; and for ten or more user IDs registered, a charge of \$70 per month, per user ID from two to ten or more. *If a member reports less*

than 25 trades per month to the TRACE system in October, November, or December 2002, the charge to be paid by a member for the TRACE web browser shall be \$25, per such month, per user ID. In addition, a member that elects to report TRACE data to the Association via a web browser over a secure PDN rather than over the Internet shall pay an additional administrative charge of \$100 per month, per line.⁶

(B) Computer-to-Computer Interface Access. No change.

(C) Third Party Access “ Indirect Reporting. No change.

(2) Transaction Reporting Fees. For each transaction in corporate bonds that is reportable to NASD [the Association] pursuant to the Rule 6200 Series, the following charges shall be assessed against the member responsible for reporting the transaction:

(A) Trade Reporting Fee. No change.

(B) Cancel or Correct Trade Fee. A member shall be charged a Cancel or Correct Trade Fee of \$3.00 per canceled or corrected transaction. To provide firms with time to adjust to the new reporting system, the Cancel or Correct

Trade Fee will not be charged until the later of October 1, 2002 or 90 days after the effective date of TRACE. *For the month of October 2002, the Cancel or Correct Trade Fee shall be \$1.50 per canceled or corrected transaction. For the month of November 2002, the Cancel or Correct Trade Fee shall be \$2.25 per canceled or corrected transaction.*

(C) “As of” Trade Late Fee. A member shall be charged an “As of” Trade Late Fee of \$3.00 per transaction for those transactions that are not timely reported “As of” as required by these rules. To provide firms with time to adjust to the new reporting system, the “As of” Trade Late Fee will not be charged until the later of October 1, 2002 or 90 days after the effective date of TRACE. *For the month of October 2002, the “As of” Trade Late Fee shall be \$1.50 per such transaction. For the month of November 2002, the “As of” Trade Late Fee shall be \$2.25 per such transaction.*

(D) Browse and Query Fee. No change.

(3) Market Data Fees. No change.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(ii).

⁴ 17 CFR § 240.19b-4(f)(2).

⁵ 15 U.S.C. 78s(b)(3)(A)(iii).

⁶ Charges that may be imposed by third parties, such as network providers, are not included in these fees.

(4) Daily List Fax Service. No change.

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II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, NASD 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. NASD 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

On July 1, 2002, TRACE became effective. On June 28, 2002, the Commission approved proposed NASD fees relating to the operation of the TRACE system (Rule 7010(k)) on a pilot basis for a six-month period expiring on December 28, 2002.⁷ As part of that rule filing (Amendment No. 3 to SR-NASD-2002-63), NASD committed to review and reassess the proposed TRACE fees as soon as practicable and within six months after the effective date of TRACE, based on such factors as actual volume, usage, costs, and revenues.

Based on an initial review of the TRACE fees, and concerns raised by member firms, NASD is proposing to reduce the Web Browser Access Fee for low volume participants, and phase in the implementation of the Cancel or Correct Fee and the "As of" Trade Late Fee during the fourth quarter of 2002. NASD is proposing to make the proposed rule change effective as of October 1, 2002.

Following the effective date of TRACE, a large number of small member firms have reported to NASD staff that the Web Browser Access Fee is too burdensome for firms that handle a small volume of corporate bond transactions per month. In addition, the current fees (approved by the SEC on a pilot basis for a six-month period) included a fee holiday for the first 90 days after the effective date of TRACE for Cancel or Correct Fees and "As of" Trade Late Fees to permit firms to adjust

to the new TRACE rules.⁸ Following operation of the TRACE system, NASD staff reviewed the financial impact of these three fees on members. This review indicates that full implementation of these fees on October 1, 2002, at the currently approved rate, will result in a significant increase in the fees paid by many firms.

As a result, NASD is proposing the rule change described herein. NASD believes that the proposed rule change will alleviate some of the immediate burden on small firms resulting from TRACE reporting requirements and grant all firms additional time to adjust to the Cancel or Correct Fee and the "As of" Trade Late Fee. In addition, NASD is in the process of reassessing the entire TRACE fee structure and expects to submit additional proposed amendments to TRACE fees to the SEC prior to the expiration of the pilot program.

Proposed Amendments to Reduce Web Browser Fee for Period of October 1, 2002 to December 31, 2002

Many small member firms have registered to report TRACE transactions through the web browser to satisfy their TRACE reporting obligations because the alternative reporting methods available under the TRACE rules (through a service bureau, clearing firm or a direct computer-to-computer interface) are not cost-effective for them. Following the effective date of TRACE, small member firms have raised concerns regarding the burden of paying the Web Browser Access Fee. Small member firms have reported to NASD staff that the small number of TRACE transactions that they handle and, therefore, are required to report on a monthly basis are not in line with the \$85 per month cost for one web browser.

The current Web Browser Access Fee for each registered member is: \$85 per month for the first user ID; \$75 per month for the second through ninth user ID; and \$70 per month for the second through ten or more user ID, if the member registers ten or more user IDs. The web browser permits the reporting of transactions into the TRACE system, and, through the use of a query feature, allows members access to TRACE transactions and real time TRACE market data. At this point in time, NASD does not have the capability to separate the real time market data access feature from the web browser, although NASD expects this capability will be

available in early 2003. When such capability does become available, NASD expects it will adjust the Web Browser Access Fee to allow members to choose whether or not they would like to receive the real time TRACE data access through the web browser.

After carefully reviewing the data collected from the first three months of operation of the TRACE system, in particular data on the monthly reporting volume of small firms, NASD is proposing that the Web Browser Access Fee be amended for the period commencing October 1, 2002 and ending December 31, 2002 as follows: all registered members that report less than 25 trades per month will be charged \$25 for such month, per user ID. All members registered to report TRACE transaction data through the web browser will continue to have access to the real time market data feature included in the web browser during this time period.

Proposed Amendments to Phase In Cancel, and/or Correct Fee and "As of" Late Fee for October and November 2002

To achieve the goal of market transparency mandated by the SEC, members must report TRACE transaction data accurately. NASD has included Cancel or Correct Fees and "As of" Trade Late Fees in the overall TRACE fee structure to provide incentives to members to enter trade data correctly, and on time, into the TRACE system. Cancel or Correct, and "As of" transactions (collectively, referred to as "corrective transactions") are used by participants to modify and correct original trade entries. While NASD believes that a certain level of corrective transactions will always be necessary, NASD believes it is very important that trades be entered into the system correctly the first time to ensure that data disseminated through the TRACE system is accurate and to allow investors to rely on the data stream they receive. In addition, a large volume of corrective transactions on a regular basis will increase NASD's technology costs over time.

In NASD's original rule filing for TRACE fees, NASD had delayed the effectiveness of the Cancel or Correct Fee and the "As of" Late Fee to October 1, 2002 (effectively granting a 90-day fee holiday) to allow firms time to adjust to the new TRACE system. The current charge for the Cancel or Correct Fee and the "As of" Late Fee is \$3.00 for each such reported trade. Based on NASD review of the data collected on such corrective transactions to date, NASD is proposing to reduce the Cancel or

⁷ The Commission approved Rule 7010(k) relating to TRACE fees on June 28, 2002 on a six-month pilot basis. See Securities Exchange Act Release No. 46145 (June 28, 2002), 67 FR 44911 (July 5, 2002) (File No. SR-NASD-2002-63).

⁸ See Securities Exchange Act Release No. 43873 (January 23, 2001), 66 FR 8131 (January 29, 2001) (File No. SR-NASD-1999-65).

Correct Fee and the "As of" Late Fee charge assessed to each member for the month of October 2002 from \$3.00 per trade to \$1.50 per trade (a 50% discount), and to reduce the Cancel or Correct Fee and the "As of" Late Fee for the month of November 2002 from \$3.00 per trade to \$2.25 per trade (a 25% discount).

The proposed rule change is based on an analysis by NASD of the economic impact of the current fees versus the proposed amended fees on TRACE participants. NASD had initially anticipated that the number of corrective transactions entered into the TRACE system over time would decline as participants grew more familiar with the new system and improved their reporting accuracy. However, a review by NASD of the unbilled July, August and September 2002 activity in these corrective transactions does not evidence the anticipated decline in these transactions. Moreover, certain firms have experienced a disproportionately high volume of corrective transactions largely because of reporting and system coding errors by participants. As a result, NASD believes that phasing-in the full fee structure for corrective transactions will allow firms greater time to learn to effectively use the new TRACE system and focus on methods to reduce corrective transactions, while still establishing an incentive for firms to report TRACE transactions correctly and on time.

NASD will continue to review and reassess the impact of the overall TRACE fee structure over time to ensure that the fees are reasonable and equitable for participants in the TRACE system.

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(5) of the Act,⁹ which requires, among other things, that NASD's rules provide for the equitable allocation of reasonable dues, fees, and other charges among members and issuers and other persons using any facility or system which NASD operates or controls. NASD proposes to reduce the Web Browser Access Fee, the Cancel or Correct Fee, and the "As of" Trade Late Fee during the periods described for the TRACE system to allow member firms more time to adjust to the new reporting system and focus on methods to decrease the likelihood of incurring such charges over time. NASD believes that such proposed rule change will more equitably allocate fees to NASD

members during the early stages of implementing TRACE.

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

NASD 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, as amended.

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 proposed rule change is effective pursuant to Section 19(b)(3)(A)(ii) of the Act¹⁰ and Rule 19b-4(f)(2) thereunder,¹¹ because the proposal is "establishing or changing a due, fee, or other charge." The rule change has become effective pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(2) thereunder, and is operational as of October 1, 2002.

At any time within 60 days of this filing, the Commission may summarily abrogate this proposal 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.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. 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 will also be available for inspection and copying at the principal office of the NASD. All

submissions should refer to file number SR-NASD-2002-167 and should be submitted by December 24, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹²

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46901; File No. SR-NASD-2002-85]

Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Issuer Disclosure of Material Information

November 25, 2002.

I. Introduction

On June 26, 2002, 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"), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² a proposed rule change to modify Nasdaq's rules pertaining to issuer disclosure of material information. The proposed rule change was published for notice and comment in the **Federal Register** on August 7, 2002.³

The Commission received one comment on the proposed rule change.⁴ On October 16, 2002, Nasdaq filed a letter in response to comments on the proposal.⁵ This order approves the proposed rule change.

II. Summary of Comments

The PR Newswire Letter

In its comment letter, PR Newswire ("Commenter") submits that the filing of a Form 8-K via EDGAR, without more, does not achieve the goal of providing

¹² 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 46288 (July 31, 2002), 67 FR 51306.

⁴ See August 26, 2002 letter from Charles H. Morin, Chief Executive Officer, PR Newswire, to Margaret H. McFarland, Deputy Secretary, Commission ("PR Newswire Letter").

⁵ See October 15, 2002 letter from John D. Nachmann, Senior Attorney, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission ("Nasdaq Response Letter").

¹⁰ 15 U.S.C. 78s(b)(3)(A)(ii).

¹¹ 17 CFR 240.19b-4(f)(2).

⁹ 15 U.S.C. 78o-3(b)(5).