

Proposed Rule Change by National Association of Securities Dealers
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial <input checked="" type="checkbox"/>	Amendment <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) <input type="checkbox"/>	Section 19(b)(3)(A) <input checked="" type="checkbox"/>	Section 19(b)(3)(B) <input type="checkbox"/>
Pilot <input type="checkbox"/>			Rule		
Extension of Time Period for Commission Action <input type="checkbox"/>		Date Expires <input type="text"/>	<input checked="" type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
			<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(6)	

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>
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Description
Provide a brief description of the proposed rule change (limit 250 characters).

NASD is filing Notice to Members 05-11, providing further guidance regarding members' obligations under Section 3 of Schedule A to the NASD By-Laws (Regulatory Transaction Fees).

Contact Information
Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name Last Name
 Title
 E-mail
 Telephone Fax

Signature
Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date
 By Senior Vice President and Deputy General Counsel
 (Name) (Title)

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(3) of the Securities Exchange Act of 1934 (“Act”),¹ the National Association of Securities Dealers, Inc. (“NASD”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) Notice to Members (“NtM”) 05-11, providing further guidance regarding members’ obligations under Section 3 of Schedule A to the NASD By-Laws (Regulatory Transaction Fees) and a self-reporting form that is used by members to report trade data that is not captured by NASD’s trade reporting system.

No changes to the text of NASD rules are required by this proposed rule change.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The proposed rule change was approved by the Board of Governors of NASD (“Board”) at its meeting on January 23, 2003, which authorized the filing of the rule change with the SEC pursuant to a delegation of authority granted by the Board to the General Counsel of NASD Regulatory Policy and Oversight (or his officer designee) to file, without further specific Board authorization, proposed administrative, technical, conforming, and non-substantive rule changes to amend NASD rules (the “Delegation of Authority”). Counsel for The Nasdaq Stock Market and NASD Dispute Resolution were provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by NASD to its Subsidiaries. The staff will advise the Board of any action taken pursuant to the Delegation of Authority.

Section 1(a)(ii) of Article VII of NASD's By-Laws permits the Board of Governors of NASD to adopt amendments to or interpretations of NASD Rules without recourse to the membership for approval. No other action by NASD is necessary for the filing of the proposed rule change.

As further discussed below, NASD is filing the proposed rule change for immediate effectiveness. The proposed rule change also will be implemented on the date of filing. NASD will announce the implementation date of the proposed rule change in NtM 05-11, which NASD expects to issue on the same date as the filing of the proposed rule change with the Commission.

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

(a) Purpose

In August 2004, NASD issued NtM 04-63 (Transaction Fees: New SEC Procedures Relating to Section 31 of the Securities Exchange Act of 1934) informing member firms of the new SEC procedures governing the calculation, payment, and collection of fees and assessments on securities transactions owed by national securities exchanges and associations to the SEC pursuant to Section 31 of the Act. NtM 04-63 also discussed the obligations of member firms under Section 3 of Schedule A to the NASD By-Laws in light of the new SEC procedures.

Following the publication of NtM 04-63, NASD staff has received a significant number of questions from member firms regarding these obligations. Accordingly, NASD staff is providing further guidance regarding these obligations in NtM 05-11. In

¹ 15 U.S.C. 78s(b)(3).

NtM 05-11, NASD staff is, among other things, providing guidance on what constitutes an away from the market sale and additional information regarding member firms' self-reporting obligations. NASD also is reminding members about the restrictions on the use of the Step-Out function in ACT for transferring NASD's regulatory transaction fee to correspondents or broker-dealer customers. In addition, NtM 05-11 is revoking prior guidance concerning the appropriate rounding methodology used by member firms when they choose to pass regulatory transaction fees to their customers. Specifically, the guidance in NtM 05-11 regarding rounding supercedes the rounding guidance provided in NtM 04-63 or any prior NtMs and Member Alerts.

The staff believes that the guidance provided in NtM 05-11 constitutes an interpretation of Section 3 of Schedule A to the NASD By-Laws that, due to its nature, should be filed as a proposed rule change. In addition, NASD also is filing its Permanent Self-Reporting Form with the SEC.² A copy of the Permanent Self-Reporting Form will be attached to NtM-05-11. NASD has revised its Permanent Self-Reporting Form to: (1) incorporate the new rate structure that became effective on January 7, 2005 (in conformity with the change to the SEC's Section 31 fee rate); (2) incorporate minor changes to the instructions section; and (3) create an obligation on certain member firms

² As noted in NtM 05-11, clearing and self-clearing member firms will now be required to file with NASD the Permanent Self-Reporting Form each month, regardless of whether they have qualifying transactions for that month. NASD is requiring a monthly filing by all clearing and self-clearing member firms to ensure that they conduct the necessary review to determine that all qualifying transactions have been properly reported. Member firms that do not have any reportable transactions for a given month will be required to submit the blank form signed by an authorized representative, along with a statement that the firm had no reportable transactions for the month. While NASD is filing its Permanent Self-Reporting Form with the SEC in this instance, NASD does not intend to file its Permanent Self-Reporting Form with the SEC each time it makes a non-substantive change to the text of the form or changes that reflect adjustments in the amount or scope of the fee, where such adjustments are determined solely by reference to Section 31 of the Act.

to file the Permanent Self-Reporting Form each month (regardless of whether they have any reportable transactions).

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,³ which requires, among other things, that NASD's rules must 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 public interest. In addition, NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(5) of the Act,⁴ 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 that NASD operates or controls, insofar as it is intended to assist members in complying with Section 3 of Schedule A to the NASD By-Laws.

4. 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.

5. 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.

³ 15 U.S.C. 78o-3(b)(6).

⁴ 15 U.S.C. 78o-3(b)(5).

6. **Extension of Time Period for Commission Action**

Not applicable.

7. **Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)**

The proposed rule change is effective upon filing pursuant to Section 19(b)(3)(A)(i) of the Act⁵ and Rule 19b-4(f)(1) thereunder,⁶ in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of NASD. As noted above, the proposed rule change also will be implemented on the date of filing. NASD will announce the implementation date of the proposed rule change in NtM 05-11, which NASD expects to issue on the same date as the filing of the proposed rule change with the Commission.

8. **Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission**

Not applicable.

9. **Exhibits**

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 3a. NASD Notice to Members 05-11 (February 2005).

Exhibit 3b. Permanent Self-Reporting Form.

⁵ 15 U.S.C. 78s(b)(3)(A)(i).

⁶ 17 CFR 240.19b-4(f)(1).

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34- ; File No. SR-NASD-2005-021)

SELF-REGULATORY ORGANIZATIONS

Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Additional Guidance Regarding Members' Obligations Under Section 3 of Schedule A to the NASD By-Laws

Pursuant to Section 19(b)(3) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on , the National Association of Securities Dealers, Inc. ("NASD") 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 NASD. NASD has designated the proposed rule change as constituting a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of the self-regulatory organization pursuant to Section 19(b)(3)(A)(i) of the Act³ and Rule 19b-4(f)(1) thereunder,⁴ which renders the proposal effective upon receipt of this filing by the Commission. 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

¹ 15 U.S.C. 78s(b)(3).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(i).

⁴ 17 CFR 240.19b-4(f)(1).

NASD is filing Notice to Members (“NtM”) 05-11, providing further guidance regarding members’ obligations under Section 3 of Schedule A to the NASD By-Laws (Regulatory Transaction Fees) and a self-reporting form that is used by members to report trade data that is not captured.

No changes to the text of NASD rules are required by this proposed rule change.

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

In August 2004, NASD issued NtM 04-63 (Transaction Fees: New SEC Procedures Relating to Section 31 of the Securities Exchange Act of 1934) informing member firms of the new SEC procedures governing the calculation, payment, and collection of fees and assessments on securities transactions owed by national securities exchanges and associations to the SEC pursuant to Section 31 of the Act. NtM 04-63 also discussed the obligations of member firms under Section 3 of Schedule A to the NASD By-Laws in light of the new SEC procedures.

Following the publication of NtM 04-63, NASD staff has received a significant number of questions from member firms regarding these obligations. Accordingly,

NASD staff is providing further guidance regarding these obligations in NtM 05-11. In NtM 05-11, NASD staff is, among other things, providing guidance on what constitutes an away from the market sale and additional information regarding member firms' self-reporting obligations. NASD also is reminding members about the restrictions on the use of the Step-Out function in ACT for transferring NASD's regulatory transaction fee to correspondents or broker-dealer customers. In addition, NtM 05-11 is revoking prior guidance concerning the appropriate rounding methodology used by member firms when they choose to pass regulatory transaction fees to their customers. Specifically, the guidance in NtM 05-11 regarding rounding supercedes the rounding guidance provided in NtM 04-63 or any prior NtMs and Member Alerts.

The staff believes that the guidance provided in NtM 05-11 constitutes an interpretation of Section 3 of Schedule A to the NASD By-Laws that, due to its nature, should be filed as a proposed rule change. In addition, NASD also is filing its Permanent Self-Reporting Form with the SEC.⁵ A copy of the Permanent Self-Reporting Form will be attached to NtM-05-11. NASD has revised its Permanent Self-Reporting Form to: (1) incorporate the new rate structure that became effective on January 7, 2005 (in conformity with the change to the SEC's Section 31 fee rate); (2) incorporate minor changes to the instructions section; and (3) create an obligation on certain member firms

⁵ As noted in NtM 05-11, clearing and self-clearing member firms will now be required to file with NASD the Permanent Self-Reporting Form each month, regardless of whether they have qualifying transactions for that month. NASD is requiring a monthly filing by all clearing and self-clearing member firms to ensure that they conduct the necessary review to determine that all qualifying transactions have been properly reported. Member firms that do not have any reportable transactions for a given month will be required to submit the blank form signed by an authorized representative, along with a statement that the firm had no reportable transactions for the month. While NASD is filing its Permanent Self-Reporting Form with the SEC in this instance, NASD does not intend to file its Permanent Self-Reporting Form with the SEC each time it makes a non-substantive change to the text of the form or changes that reflect adjustments in the

to file the Permanent Self-Reporting Form each month (regardless of whether they have any reportable transactions).

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁶ which requires, among other things, that NASD's rules must 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 public interest. In addition, NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(5) of the Act,⁷ 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 that NASD operates or controls, insofar as it is intended to assist members in complying with Section 3 of Schedule A to the NASD By-Laws.

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.

amount or scope of the fee, where such adjustments are determined solely by reference to Section 31 of the Act.

⁶ 15 U.S.C. 78o-3(b)(6).

⁷ 15 U.S.C. 78o-3(b)(5).

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The proposed rule change has become effective pursuant to Section 19(b)(3)(A)(i) of the Act⁸ and Rule 19b-4(f)(1) thereunder,⁹ in that the proposed rule change constitutes a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule of NASD. NASD will announce the implementation date of the proposed rule change in NtM 05-11, which NASD expects to issue on the same date as the filing of the proposed rule change with the Commission.

At any time within 60 days of the filing of the 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.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change 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. Please include File Number SR-NASD-2005-021 on the subject line.

⁸ 15 U.S.C. 78s(b)(3)(A)(i).

⁹ 17 CFR 240.19b-4(f)(1).

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-2005-021. 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, 450 Fifth Street, NW, Washington, DC 20549. Copies of such filing also will be available for inspection and copying at the principal office of 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 the File Number SR-NASD-2005-021 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

authority.¹⁰

Margaret H. McFarland
Deputy Secretary

¹⁰ 17 CFR 200.30-3(a)(12).

Notice to Members

FEBRUARY 2005

SUGGESTED ROUTING

Finance
 Legal & Compliance
 Operations
 Senior Management

KEY TOPICS

Regulatory Transaction Fees
 Section 31 of the Exchange Act
 Section 3 of Schedule A to the NASD
 By-Laws

GUIDANCE AND REQUEST FOR COMMENT

Regulatory Transaction Fees

NASD Issues Further Guidance Regarding Members' Obligations under Section 3 of Schedule A to the NASD By-Laws; NASD Also Seeks Member Comment on Related Automation Issues; **Comment Period Expires March 30, 2005**

Executive Summary

In August 2004, NASD issued *Notice to Members (NtM) 04-63* (Transaction Fees: New SEC Procedures Relating to Section 31 of the Securities Exchange Act of 1934) informing member firms of the new Securities and Exchange Commission (SEC) procedures governing the calculation, payment, and collection of fees and assessments on securities transactions owed by national securities exchanges and associations to the SEC pursuant to Section 31 of the Securities Exchange Act of 1934 (Exchange Act). *NtM 04-63* also discussed the obligations of member firms under Section 3 of Schedule A to the NASD By-Laws in light of the new SEC procedures.

More specifically, *NtM 04-63* stated that members are required to self-report the following covered securities transactions that are not reported to NASD's trade reporting systems: (1) odd-lot transactions; (2) exercises of over-the-counter (OTC) options that settle by physical delivery; and (3) away from the market sales. In addition, NASD notified members that beginning in September 2004, members must self-report the relevant trade data and submit their payments by the seventh calendar day of each month. Further, NASD informed members that if they pass this regulatory transaction fee onto their customers, they should no longer consistently round up if there is a remainder. Instead, members should alternate between rounding up and rounding down to the next cent when calculating the transaction fees on individual trades. Last, based on statements made by the SEC in its order approving the new SEC procedures, NASD cautioned member firms that they must refrain from labeling the fees assessed by NASD as "Section 31 Fees" or "SEC Fees."

05-11

Today, NASD staff is announcing that, beginning in February 2005, all NASD member clearing and self-clearing firms will be required to submit a monthly Self-Reporting Form to NASD regardless of whether they have qualifying transactions for a specific month. The form must be signed by a registered principal indicating the firm has done the necessary review to ensure all qualifying transactions have been properly reported. In addition, **NASD staff is advising NASD members that they should disregard the advice on rounding provided in any previous *NtMs* (including *NtM 04-63*) and *Member Alerts* (including the December 28, 2001, *Member Alert*).** Attachment A to this *NtM* is an updated Self-Reporting Form.

NASD staff is also providing further guidance in this *NtM* in response to a significant number of questions from member firms regarding these obligations.¹ These questions have prompted NASD to seek input from the membership on automating the reporting process for odd-lot transactions, OTC exercised options and away from the market sales. Specifically, NASD is seeking member comment on requiring that all transactions subject to the Regulatory Transaction Fee be reported to an NASD trade reporting system. This proposal would include amending NASD transaction reporting rules to allow for odd-lot transactions, OTC exercised options and away from the market sales to be submitted to an NASD trade reporting system for regulatory reporting purposes. Transactions submitted in this manner would be flagged by NASD's billing system and included in the Regulatory Transaction Fee billing process, but would not be disseminated to the media. NASD foresees that these regulatory reports would follow the same Automated Confirmation Transaction Service (ACT) or Trade Reporting and Confirmation Service (TRACS) fee structure for non-tape, non-clearing entries as exists today (*i.e.*, no ACT or TRACS fee would be charged for the submission of these entries.)

Questions/Further Information

Questions concerning this *NtM* may be directed to NASD Finance, at (240) 386-5397; and the Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8071.

Action Requested

NASD encourages all interested parties to comment on the proposed changes to the reporting process for the Regulatory Transaction Fee. Comments must be received by **March 30, 2005**. Members and other interested parties can submit their comments using the following methods:

- ◆ Mailing comments in hard copy to the address below
- ◆ E-mailing comments to pubcom@nasd.com

To help NASD process and review comments more efficiently, persons commenting on this proposal should use only one method; however, if a person wishes to submit comments using both of the methods listed above, he or she should indicate that in the submissions.

Comments sent by hard copy should be mailed to:

Barbara Z. Sweeney
Office of the Corporate Secretary
NASD
1735 K Street, NW
Washington, DC 20006-1500

Important Notes: The only comments that will be considered are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the NASD Web site. Generally, comments will be posted on the NASD Web site one week after the end of the comment period.²

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the NASD Board, and then must be approved by the SEC, following publication for public comment in the *Federal Register*.³

Question and Answers

The following Questions and Answers address a variety of issues that have arisen since the publication of *NtM 04-63*.

Q1. What are away from the market sales?

A1. Pursuant to NASD's transaction reporting rules, members are required to report transactions in designated securities, with few exceptions. One such exception is transactions where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security, and consideration is provided. Such sales are called away from the market sales. Away from the market sales historically have been excluded from the reporting requirements under NASD's transaction reporting rules, including the rules applicable to ACT.⁴

However, given the underlying goals of transaction reporting, NASD interprets the exception from the transaction reporting rules for away from the market sales very narrowly. Specifically, as noted in *NtM 02-76*, an away from the market sale is an execution that occurs without reference to current market pricing and investment, commercial, or trading considerations.⁵ Consequently, NASD staff anticipates that the number of away from the market sales subject to self-reporting pursuant to Section 3 of Schedule A to the NASD By-Laws should be *de minimis*. Members also should note that any sales that are reported to ACT or TRACS are not subject to self-reporting. Moreover, members are not required to self-report transactions involving a gift of a security *without* consideration because such a transaction is not considered a "sale" for reporting purposes.

- Q2.** In *NtM 04-63*, NASD stated that members should calculate the regulatory transaction fees by: (1) multiplying the aggregate dollar amount of covered sales by the fee rate; (2) truncating the resulting amount at the fifth place after the decimal point; and (3) alternating between rounding up and rounding down to the next cent, if there is any remainder. How should members apply the alternating round up/down methodology? Do members still have the option of solely rounding up to the next cent if there is any remainder following the calculation?
- A2. The guidance provided in *NtM 04-63* regarding the rounding methodology was intended to prevent the accumulation of any overages that may result from routinely rounding up to the next cent when calculating the transaction fees that firms pass on to their customers by suggesting that firms adopt a standard mid-point rounding convention. Section 3 of Schedule A to the NASD's By-Laws does not dictate whether or how members should charge customers to recover amounts paid to NASD; accordingly, members should disregard the advice on rounding provided in the *NtM 04-63* or any other previous *NtMs* and *Member Alerts* (including the December 28, 2001, *Member Alert*).
- Q3.** Are all member firms required to self-report the applicable trade data and submit payments to NASD?
- A3. No. Although reporting obligations are ultimately the responsibility of each member firm, only member firms that are clearing firms (including self-clearing firms) should be submitting the self-reported trade data and applicable payments to NASD. Clearing firms are expected to collect any applicable trading information from their respective correspondent firms to be included in the aggregate totals.
- Q4.** Can odd-lot transactions be reported to ACT or TRACS in order to fulfill a member's self-reporting obligation for covered odd-lot sales?
- A4. Yes. Odd-lot transactions submitted to ACT or TRACS for clearing purposes pursuant to NASD Rule 6130(a) will satisfy a member's self-reporting obligation.⁶ Therefore, any odd-lot sale submitted to ACT (in the manner as prescribed in endnote six) or TRACS for clearing should not be included on the member's Self-Reporting Form. Members should be aware, however, that NASD rules prohibit odd-lot transactions from being reported to NASD trade reporting systems for media dissemination only.⁷ Members, therefore, must use the Self-Reporting Form to satisfy their reporting obligation with respect to odd-lot transactions that are not cleared through ACT or TRACS.

Q5. Does my firm have to submit a Self-Reporting Form if we have no transactions that are subject to the self-reporting requirement?

A5. Yes. Previously, clearing and self-clearing firms were only required to submit an initial Self-Reporting Form indicating that they did not process any transactions falling within the self-reporting requirement. After the initial form, there was no requirement to submit blank forms on a monthly basis. However, to ensure firms' on-going compliance with self-reporting obligations, NASD is now requiring that each clearing and self-clearing firm submit a Self-Reporting Form each month regardless of whether they have qualifying transactions. Additionally, the form must be signed by a registered principal of the firm representing that a review has been performed to ensure all qualifying transactions have been properly reported. This new requirement will begin with January trade data that is due to NASD by February 7, 2005. An updated Self-Reporting Form is included in this *NtM* as Attachment A.

Q6. Does NASD pay the SEC a Section 31 fee on all sales transacted by or through an NASD member?

A6. NASD is responsible for paying fees for sales transacted by or through its members in securities subject to prompt last sale reporting pursuant to the rules of the SEC or NASD and securities that are off-exchange trades of exchange-registered securities. This means that, as a general matter, transactions in equity securities submitted to an NASD trade reporting system for last sale reporting are subject to the fee.⁸ However, certain sales are exempt from the fee. SEC Rule 31(a)(11) states that the following sales are exempt: (i) any sale of a security offered pursuant to an effective registration statement under the Securities Act of 1933 (except a sale of a put or call option issued by the Options Clearing Corporation) or offered in accordance with an exemption from registration afforded by section 3(a) or 3(b) of the Securities Act of 1933, or a rule thereunder; (ii) any sale of a security by an issuer not involving any public offering within the meaning of section 4(2) of the Securities Act of 1933; (iii) any sale of a security pursuant to and in consummation of a tender or exchange offer; (iv) any sale of a security upon the exercise of a warrant or right (except a put or call), or upon the conversion of a convertible security; (v) any sale of a security that is executed outside the United States and is not reported, or required to be reported, to a transaction reporting association as defined in §240.11Aa3-1 and any approved plan filed thereunder; (vi) any sale of an option on a security index (including both a narrow-based security index and a non-narrow-based security index); (vii) any sale of a bond, debenture, or other evidence of indebtedness; and (viii) any recognized riskless principal sale.

Q7. Our firm has decided to pass on the Regulatory Transaction Fees assessed by NASD to our broker-dealer customers. Is it acceptable to use the Step-Out function in ACT for the specific purpose of transferring the transaction fees to broker-dealer customers?

A7. No. As explained in *NtM 98-40* (Nasdaq To Incorporate Trade Acceptance And Reconciliation Service Into Automated Confirmation Transaction Service) (May 1998), ACT provides a Step-Out function to allow members to “step out,” or allocate, all or part of a previously executed trade to another broker-dealer. In other words, a Step-Out functions as a position transfer, rather than a trade. The Step-Out function was designed and implemented to facilitate the clearing process for members involved in these types of transactions. As part of the Step-Out function, ACT also provides the ability to move the transaction fee associated with the trade to the ultimate seller of the security when the trade is allocated. However, the Step-Out functionality was not intended to serve as a means to transfer transaction fees related to trades that do not fit ACT’s definition of a Step-Out. Using the Step-Out flag on transactions that do not meet ACT’s definition of a Step-Out results in such transactions being incorrectly characterized in NASD’s audit trail. Because NASD relies on the audit trail for regulatory and surveillance purposes, it is critical that all transactions submitted to ACT be reported in accordance with the ACT rules to ensure the integrity of the information contained in the audit trail.

Q8. Where do member firms send the monthly self-reporting form?

A8. Member firms should submit the Permanent Self-Reporting Form and payment to NASD, P.O. Box 7777-W4230, Philadelphia, PA 19175-4230.

Endnotes

- 1 NASD filed this *NtM* on February 4, 2005, with the SEC for immediate effectiveness. See SR-NASD-2005-021 (Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Additional Guidance Regarding Members' Obligations under Section 3 of Schedule A to the NASD By-Laws).
- 2 See *NtM 03-73* (November 2003) (NASD Announces Online Availability of Comments). Personal identifying information, such as names or e-mail addresses, will not be edited from submissions. Persons commenting on this proposal should submit only information that they wish to make publicly available.
- 3 Section 19 of the Exchange Act permits certain limited types of proposed rule changes to take effect upon filing with the SEC. The SEC has the authority to summarily abrogate these types of rule changes within 60 days of filing. See Exchange Act Section 19 and rules thereunder.
- 4 See NASD Rules 4632(e)(5), 4642(e)(4), 4652(e)(3), 6230(e)(3), 6420(e)(5), and 6920(e)(2) (providing that away from the market sales—for example, to make a gift—need not be reported).
- 5 See *NtM 02-76* (November 2002) (Corporate Debt Securities Transactions Subject to Reporting and Dissemination; NASD Issues Interpretive Guidance to the Trade Reporting and Compliance Engine Rules (TRACE Rules)).
- 6 Firms should note that in order for odd-lot transactions submitted to ACT to be billed automatically by NASD, the trade must be submitted to ACT for both reporting and clearing. The reporting designation of the entry is used to identify the trade as eligible for the Regulatory Transaction Fee in NASD's billing system. Note that ACT automatically suppresses the trade from media dissemination.
- 7 See, e.g., Rule 4623(e)(2).
- 8 The fee, however, does not apply to non-Canadian foreign securities submitted to an NASD trade reporting system since these securities are generally not subject to prompt last sale reporting (reported on a T+1 basis).

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**NASD Permanent Self-Reporting Form for Odd-Lot Transactions,
OTC Exercised Options, and Away from the Market Sales**

*****Effective January 7, 2005*****

Important Note: Only NASD members that are clearing firms (including self-clearing firms) should be submitting this form on a monthly basis to NASD. All clearing firms are expected to collect any applicable trading information from their respective correspondent firms to be included in the aggregate totals. The trade date must be used when determining aggregate odd-lot and away from the market sales transactions for the preceding calendar month. The exercise date must be used when reporting aggregate OTC exercised option sales for the preceding calendar month.

General Instructions

The purpose of this form is to facilitate the collection of transaction fees under Section 3 of Schedule A to the NASD By-Laws with respect to transactions in odd-lots, transactions effected pursuant to the exercise of OTC options, and certain transactions that occur away from the market.

Transactions of the clearing firm and its correspondents should be consolidated for reporting purposes.

Please retain a copy of this blank form for your firm's monthly reporting. Additional copies of this form may be obtained by contacting the NASD Finance Department at (240) 386-5354.

Each clearing firm must submit this form each month regardless of whether it has reportable transactions. If your firm does not have any reportable transactions for the current month, your firm must submit the blank form signed by an authorized principal, along with a statement that your firm had no reportable transactions for the month.

Odd-Lot Transactions

NASD members that are clearing firms, including self-clearing firms, must report the aggregate dollar amount of covered odd-lot sales transacted by or through such member, including all such sales by the member's correspondent firm(s). Firms must report odd-lot sales under the same general rules and guidelines applicable to round lot transactions as detailed in *Special Notice to Members 96-81* dated December 3, 1996 and the SEC Billing Document from NASD in December 1996. Member firms should consider the following when accumulating odd-lot data for each reporting period:

- Odd-lot transactions are those sides for less than the normal trading unit, e.g., 100 shares. Do not include "mixed lots" as part of your odd-lot reporting.
- Include all transactions where you or your correspondent firms represent the sell side of the odd-lot transaction.
- Include all transactions where you or your correspondent firms represent the buy side of a transaction with or between public customers or non-NASD member firms.
- Include all odd-lot transactions in NASDAQ Equity Securities.
- Include all odd-lot transactions in non-NASDAQ OTC Equity Securities as defined in NASD Rule 6610.
- Include all odd-lot transactions in non-NASDAQ OTC Equity Securities that are ADRs or Canadian foreign securities but exclude all non-NASDAQ non-Canadian foreign securities.
- Include all odd-lot transactions in exchange-registered securities traded off the exchange ("third market trades").
- Do *not* include odd-lot transactions that were reported to TRACS or that were submitted to ACT for clearing and reporting (see endnote three in *NTM 05-11*). This form must only be used for odd lots that are not reported to TRACS or that were not submitted to ACT for *both* reporting and clearing (e.g., an entry marked as clearing only will not be automatically billed by NASD).

OTC Option Exercise

Use this section of the form to report all transactions in a covered security effected pursuant to the exercise of an OTC option by or through a member that is a clearing firm (including self-clearing firm) or its correspondent firm(s). Covered securities are those securities that are subject to prompt last-sale-reporting and exchange-registered securities. Member firms should determine the following when accumulating options exercise data for each calendar reporting period:

- This form is only used to report transactions in covered securities that arise pursuant to the exercise of an OTC option by or through an NASD member that settle by physical delivery. Do not include any exercise of an option not involving the purchase or sale of the underlying covered security, e.g., a cash settled exercise.
- Include all transactions where you or your correspondent firms represent the sell side of the transaction.
- Include all transactions where you or your correspondent firms represent the buy side of a transaction with or between public customers or non-NASD member firms.
- Do not include any transactions in a covered security effected pursuant to the exercise of an exchange-registered option. The Options Clearing Corporation will collect the fee for these types of transactions.
- Report the aggregate dollar amount of the transactions determined on the basis of the exercise price.

Sales Away from the Market

NASD members that are clearing firms (including self-clearing firms) must report the aggregate dollar amount of covered sales where the buyer and seller have agreed to trade at a price substantially unrelated to the current market for the security and where these sales are prohibited from being reported to an NASD trade reporting system pursuant to NASD Rules. Firms should not include transactions involving a gift of a security **without** consideration because such a transaction is not considered a "sale" for purposes of this form.

**NASD Permanent Self-Reporting Form for Odd-Lot Transactions,
OTC Exercised Options, and Away from the Market Sales**

***** Effective January 7, 2005 *****

Regulatory Transaction Fees under Section 3 of Schedule A to the NASD By-Laws for the Calendar Month of _____, 200() for odd-lot transactions, OTC exercised options, and away from the market sales.

Report of Sales by: Firm Name _____
 B/D# _____
 Clearing# _____

Transaction	Aggregate Sales/Exercise Price	Rate	Fee Due
Odd-Lot Transactions	\$	0.0000329	\$
OTC Exercised Options	\$	0.0000329	\$
Away from the Market Sales	\$	0.0000329	\$
Total Amount Due \$			_____

*****IMPORTANT*** PAYMENT FOR TOTAL AMOUNT DUE MUST BE SUBMITTED WITH THIS REPORT.**

NASD must receive this form and payment by the seventh calendar day¹ subsequent to the subject trade-reporting period. Please submit this form and payment to:

NASD • P.O. Box 7777-W4230 • Philadelphia, PA 19175-4230

Signature of Authorized Principal _____ Title _____

Print Name _____ Date/Telephone Number _____

Address (Street, City, State, Zip) _____

E-mail Address _____

¹ If the seventh calendar day falls on a weekend or a public holiday, the report must be received by NASD on the first business day following the weekend or public holiday.