Memo

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To: ☒ Senior Management
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From: Paul J. McKenney
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Date: April 10, 2006

Re: *Addendum to OATS Reporting Technical Specifications, November 11, 2005*

On November 11th, 2005, NASD published the OATS Reporting Technical Specifications containing the OATS reporting requirements for OATS Phase III, effective May 8, 2006. This addendum includes the following:

1) New value for Routing Method Code;
2) Clarification of Order Routing Scenario 4.4.20(a);
3) New Order Routing Scenario 4.4.20(b);
4) Additional Firm Order Report Status Message;
5) Four new Desk Type Code values; and
6) Correction to Appendix C – Order Report Formats.

All changes described in this addendum will be available in the OATS Production environment on May 8, 2006 and in the Certification Test environment on April 24, 2006. Please note that the new Smart Router Routing Method Code will be available as of May 8, 2006 but, to allow firms additional programming time, is not required until September 11, 2006.

Additional Routing Method Code

A new value has been added for the Routing Method Code. To identify when an order has been directed to another market center via a Smart Router, the OATS application will include a new Routing Method Code of ('S') for orders routed via a Smart Router. Although this new value will be available beginning May 8, 2006, it will not be required until September 11, 2006. A separate

OATS Report will be published concerning the appropriate use of this new Routing Method Code value.

All Route and Combined Order/Route reports with a Routing Method Code of ('S') and a Destination Code of Member Firm ('M'), ECN ('E') or NASDAQ Market Center ('U') require the Routed Order ID or Sent to Routed Order ID field to be populated. Beginning on May 8, 2006, Route and Combined Order/Route reports with a Routing Method Code of 'S', a Destination Code of 'M', 'E' or 'U', and a blank Routed Order ID or Sent to Routed Order ID will be rejected.

In addition, all Route and Combined Order/Route reports with a Routing Method Code of Smart Router ('S') and a Destination Code of Member Firm ('M') or ECN ('E') will be considered in the OATS Interfirm Route Matching process. Likewise, all Route and Combined Order Route reports with a Routing Method Code of Smart Router ('S') and a Destination Code of NASDAQ Market Center ('U') will be considered in the NASDAQ Market Center Route matching process.

Order Routing Scenarios

Order Routing Scenario 4.4.20(a) has been updated. This scenario describes the OATS reporting requirements for clearing firms that provide automated routing services to its correspondents.

Order Routing Scenario 4.4.20b has been added to clarify the specific circumstances under which a member providing a Smart Router to other members would not be required to report to OATS orders directed through its Smart Router.

Additional Firm Order Report Status Message

NASD has added a new Firm Order Report Status Message to indicate the receipt of a FORE file with an invalid format.

The Exception Code is 1036 – Invalid Forefile Format, which is defined as a file that is missing an end of file or end of line marker, or contains invalid special or hidden characters which prevents OATS from processing the file.

Additional Desk Type Code Values

The following Desk Type Codes are being added:

'O' – Other

'B' – Block Trading

'C' – Convertibles Desk

'TR' - Treasury

Correction to Appendix C – Order Report Formats

On both the New Order Report Format and the Desk Report Format, the Desk Type Code of 'PR' was listed twice and the 'PT' code was omitted. Both report formats should reflect a Desk Type Code of 'PR' Proprietary Trading as well as a Desk Type Code 'PT' Program Trading.

The OATS Reporting Technical Specifications may be viewed at the following link: http://www.nasd.com/oatsspecifications. For more information on OATS Phase III, please visit http://www.nasd.com/oats/PhaseIII. Should you have any questions regarding OATS, please contact the OATS Helpdesk at 1-800-321-NASD.

4.4.20 (a) Order Routing via an Algorithm Provided by the Clearing Firm

This scenario illustrates the reporting requirements to OATS when an introducing firm, that meets the definition of Reporting Member under NASD Rule 6951(n), receives a customer order and enters it into its clearing firm's system. The clearing firm's system then directs the order to a destination market center for execution. The introducing firm does not make a determination as to where the order is routed. Rather, the clearing firm's system automatically determines the routing destination based on pre-established criteria developed by the clearing firm. Further, the clearing firm identifies itself as the routing firm for purposes of SEC Rule 606 (formerly SEC Rule 11Ac1-6)

The introducing firm would report the following:

1. The receipt of the order from the customer.

2. The route of the order to the clearing firm.

The clearing firm would report the following:

1. The receipt of the order from the introducing firm.

2. The route of the order to the destination market center.

The destination market center would report the following (assuming it is a Reporting Member):

1. The receipt of the order from the clearing firm.

2. The execution of the order.

The introducing firm's order receipt time is the time the order is received from the customer. The clearing firm's order receipt time is the time the order is entered into its system.

Figure 1. Order Routing via an Algorithm Provided by the Clearing Firm
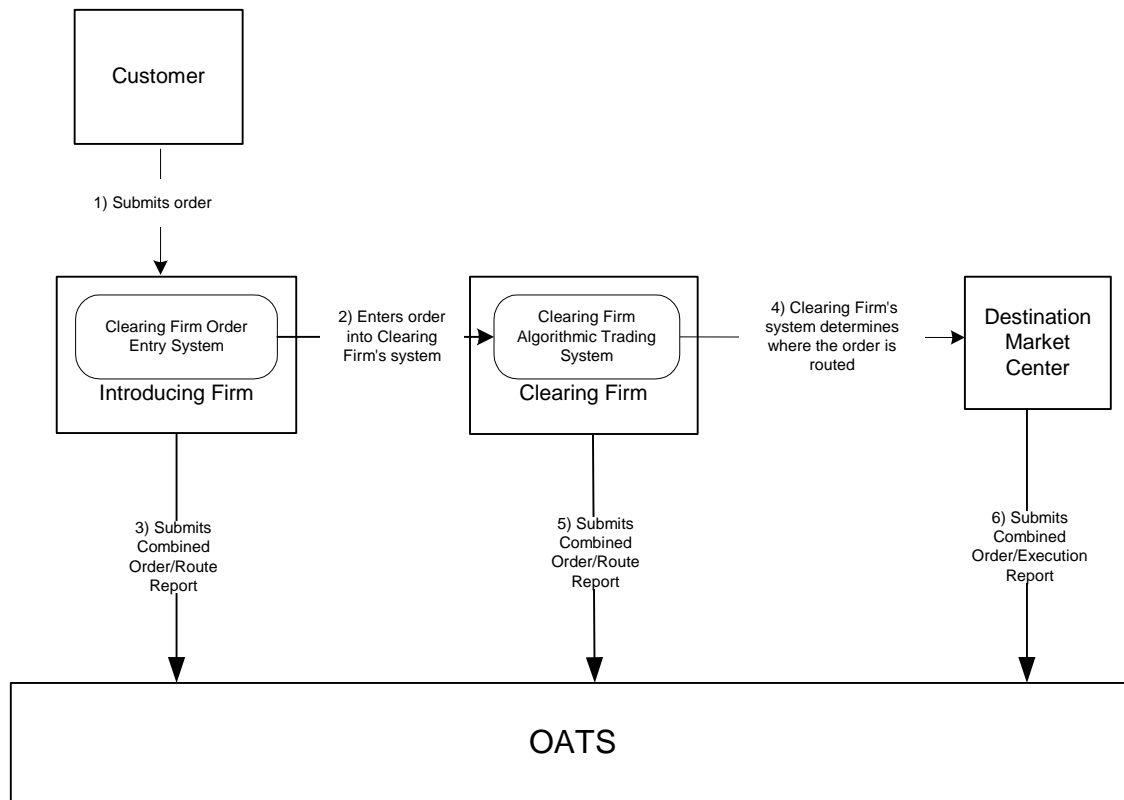
This scenario includes the following assumptions:

1. The Introducing Firm is responsible for OATS reporting, even if some other entity such as a clearing firm acts as its reporting agent.

2. Order receipt time and the time the order is received at a desk or department is simultaneous or within the same second.

3. The customer order is routed on an agency basis.

Table -1. Order Routing via an Algorithm Provided by the Clearing Firm

Ref	Event	Event Details
1	Customer submits order to Introducing Firm.	Market sell order for 2,000 shares of ORCL.
2	Introducing Firm enters order into Clearing Firm's system.	Market sell order for 2,000 shares of ORCL.
3	Introducing Firm submits Combined Order/Route report to OATS.	Combined Order/Route Report sample data includes: Order Receiving Firm MPID: FIRM Order Received Date: 20030102000000 Order Receiving Firm Order ID: ABCD1234 Order Received Timestamp: 20030102105755 Issue Symbol ID: ORCL Buy/Sell Code: SL Shares Quantity: 2000 Account Type Code: R Received Method Code: E Member Type Code: N ECN Flag: Desk Timestamp: Received by Desk ID: Desk Type Code: Sent to Firm MPID: MM01 Sent to Routed Order ID: ABCD1234 Order Sent Timestamp: 20030102105755 Routed Shares Quantity: 2000 Routing Method Code: E Bunched Order Indicator: Destination Code: M
4	Clearing Firm's system determines where the order is routed.	Clearing Firm routes 2,000 shares of ORCL to Market Maker.
5	Clearing Firm submits Combined Order/Route report to OATS.	Combined Order/Route Report sample data includes: Order Receiving Firm MPID: MM01 Order Received Date: 20030102000000 Order Receiving Firm Order ID: DEF456 Order Received Timestamp: 20030102105755 Issue Symbol ID: ORCL Buy/Sell Code: SL Shares Quantity: 2000 Account Type Code: W Received Method Code: E Member Type Code: M Routed Order ID: ABCD1234 Routing Firm MPID: FIRM ECN Flag: Desk Timestamp: Received by Desk ID: Desk Type Code: Sent to Firm MPID: ECN1 Sent to Routed Order ID: DEF456 Order Sent Timestamp: 20030102105756 Routed Shares Quantity: 2000 Routing Method Code: E Bunched Order Indicator: Destination Code: M

Ref	Event	Event Details	
6	Destination Market Center executes order and submits Combined Order/Execution report to OATS.	Combined Order/Execution sample data includes:	
		Order Receiving Firm MPID:	ECN1
		Order Received Date:	20030102000000
		Order Receiving Firm Order ID:	GHI789
		Order Received Timestamp:	20030102105756
		Received Method Code:	E
		Issue Symbol ID:	ORCL
		Buy/Sell Code:	SL
		Shares Quantity:	2000
		Account Type Code:	W
		Member Type Code:	M
		ECN Flag:	
		Routed Order ID:	DEF456
		Routing Firm MPID:	MM01
		Desk Timestamp:	
		Received by Desk ID:	
		Desk Type Code:	
		Execution Timestamp:	20030102105757
		Branch Sequence Num:	GHI789
		Execution Quantity:	2000
		Trader Terminal ID:	TERM00392
		Market Center ID:	Q
		Execution Price:	11.04
		Capacity Code:	P

4.4.20(b) Smart-Order Routers and Other Order Routing Services Provided by Members

Members that provide other NASD members smart order routers and other order routing services generally are required to report OATS information for orders routed through these systems, except under the following circumstances:

(1) The member providing the order routing system has no discretion over the order once it is entered into the member's order-routing system. The order routing destination ("Destination Market Center") must either be directed by the originating member or be subject to the pre-determined algorithm of the routing system agreed to by the originating member. The member providing the order routing system would have no involvement relating to the routing of the order, other than providing the routing mechanism.

(2) The originating member must have established a relationship with the Destination Market Center, including meeting any and all applicable requirements to route orders to that destination. The originating member understands that the member providing the order routing system has no involvement with respect to the order in any way, except for providing a routing mechanism. No pre-established relationship between the member providing the order routing system and the Destination Market Center would be necessary for the originating member to access the routing destination.

(3) The Destination Market Center views the order as coming directly from the originating member, not the member providing the order routing system, for all purposes, including, but not limited to, OATS reporting, trade reporting, applicable fees, etc.

(4) The originating member, rather than the member providing the order routing system, identifies itself as the routing firm for purposes of SEC Rule 606 (formerly SEC Rule 11Ac1-6).

This scenario illustrates the reporting requirements to OATS when an introducing firm that meets the definition of Reporting Member under NASD Rule 6951 (n) enters an order into a Smart Router provided by another member firm that meets the conditions noted above. In this scenario, therefore, the introducing firm would report the following:

1. The receipt or origination of the order.
2. The route to the Destination Market Center determined by the Smart Router.

The Destination Market Center, assuming it is a Reporting Member, would report the following:

1. The receipt or the order from the introducing firm.
2. The execution (or any other action) of the order.

Figure- 2 Smart-Order Routers and Other Order Routing Services Provided by Members
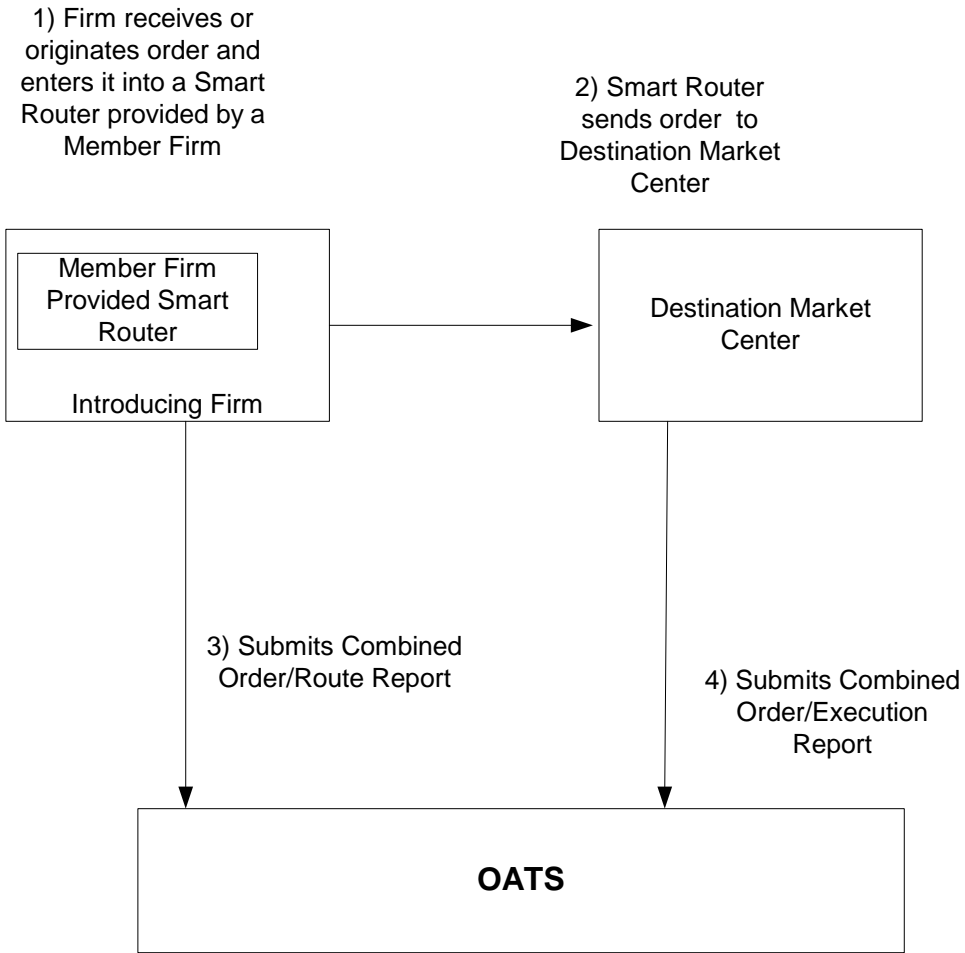
1) Firm receives or
originates order and
enters it into a Smart
Router provided by a
Member Firm

2) Smart Router
sends order to
Destination Market
Center

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│ ┌─────────────────────┐ │              │                         │
│ │   Member Firm       │ │              │   Destination Market    │
│ │   Provided Smart    │ │─────────────▶│        Center           │
│ │      Router         │ │              │                         │
│ └─────────────────────┘ │              │                         │
│                         │              │                         │
│   Introducing Firm      │              │                         │
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3) Submits Combined
Order/Route Report

4) Submits Combined
Order/Execution
Report

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│                              OATS                                  │
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Table-2 Smart-Order Routers and Other Order Routing Services Provided by Members

Ref	Event	Event Details
1	Firm receives or originates an order and enters it into a Smart Router provided by a Member Firm.	Market sell order for 2,000 shares of ORCL.
2	Smart Router sends order to destination market center.	Market sell order for 2,000 shares of ORCL.
3	Introducing Firm submits Combined Order/Route report to OATS.	Combined Order/Route Report sample data includes: Order Receiving Firm MPID: MM01 Order Received Date: 20030102000000 Order Receiving Firm Order ID: DEF456 Order Received Timestamp: 20030102105755 Issue Symbol ID: ORCL Buy/Sell Code: SL Shares Quantity: 2000 Account Type Code: W Received Method Code: E Member Type Code: R Routed Order ID: Routing Firm MPID: ECN Flag: Desk Timestamp: Received by Desk ID: Desk Type Code: Sent to Firm MPID: DM01 Sent to Routed Order ID: DEF456 Order Sent Timestamp: 20030102105756 Routed Shares Quantity: 2000 Routing Method Code: S Bunched Order Indicator: Destination Code: M
6	Destination Market Center executes order and submits Combined Order/Execution report to OATS.	Combined Order/Execution sample data includes: Order Receiving Firm MPID: DM01 Order Received Date: 20030102000000 Order Receiving Firm Order ID: GHI789 Order Received Timestamp: 20030102105756 Received Method Code: E Issue Symbol ID: ORCL Buy/Sell Code: SL Shares Quantity: 2000 Account Type Code: W Member Type Code: M ECN Flag: Routed Order ID: DEF456 Routing Firm MPID: MM01 Desk Timestamp: Received by Desk ID: Desk Type Code: Execution Timestamp: 20030102105757 Branch Sequence Num: GHI789 Execution Quantity: 2000 Trader Terminal ID: TERM00392 Market Center ID: Q Execution Price: 11.04 Capacity Code: P