

Special Notice to Members

JULY 2003

SUGGESTED ROUTING

Senior Management
Legal and Compliance
Operations Managers

KEY TOPICS

NASD By-Laws
Trading Activity Fee

INFORMATIONAL

SEC Approves Increase to the Trading Activity Fee

Executive Summary

On July 28, 2003, the Securities and Exchange Commission (SEC or Commission) approved an NASD rule filing amending the Trading Activity Fee (TAF) to establish a new rate for covered equity securities.¹ NASD had been collecting the TAF and determined that the equity rate needed to be increased to ensure adequate funding levels for its member regulatory program. The new TAF rates for covered equity securities will go into effect on September 1, 2003. A revised Trading Activity Fee Self-Reporting Form is available on the NASD Web Site at http://www.nasdr.com/pdf-text/0275ntm_a.pdf.

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

Discussion

On May 30, 2003, the Commission approved the last component of a series of changes to NASD's member regulatory fee structure. Under the new fee structure, there are now three types of fees and assessments used to fund NASD's member regulatory activities: (1) the TAF;² (2) Personnel Assessment; and (3) Gross Income Assessment.³ These fees, assessed upon and paid by member firms, are used by NASD to fund NASD's member regulatory activities, including the regulation of members through examinations, processing of membership applications, financial monitoring, policy, rulemaking, interpretive, and enforcement activities. The new member regulatory fee structure was designed to be revenue neutral to NASD and to better align NASD's regulatory fees with its functions, efforts, and costs.

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On June 11, 2003, NASD filed with the Commission a proposed rule change to adjust the TAF rate, and related maximum charge and minimum price exceptions, for equity securities. The proposed rule change was published for notice and comment in the Federal Register on June 25, 2003⁴ and was subsequently approved by the Commission on July 28, 2003.⁵

NASD had been collecting the TAF for transactions effected after October 1, 2002 on a pilot basis, and determined that the equity rate needed to be increased to ensure adequate funding levels for its member regulatory program. The TAF will be increased from \$0.00005 per share to \$0.0001 per share for covered equity securities. The maximum charge for equity securities also was changed from \$5.00 per trade to \$10.00 per trade. Last, the exclusion for transactions in covered equity securities if the execution price is less than the TAF rate was modified from \$0.00005 to \$0.0001. The new TAF rates for covered equity securities will go into effect on September 1, 2003. Members should make the necessary changes to their internal systems to ensure compliance with the new TAF rates for covered equity securities by September 1, 2003. Additionally, a revised Trading Activity Fee Self-Reporting Form is available on the NASD Web Site at http://www.nasdr.com/pdf-text/0275ntm_a.pdf.

The proposed rate change is driven by lower than expected TAF revenues, not increased or unexpected member regulatory costs. NASD originally had proposed a rate of \$0.0001 per share for equity securities (announced on September 27, 2002 and published on NASD's Web Site), but after informal feedback from the membership about the level of volume meeting the definition of "covered equity security," NASD decided to reduce the rate to \$0.00005. Six months experience with the TAF has demonstrated that the initially proposed rate is more accurate to ensure revenue neutrality and adequate funding.

NASD periodically will analyze rates, volumes, and regulatory responsibilities to ensure adequate funding levels for its member regulatory programs.⁶ NASD also will perform an analysis for the annual Personnel Assessment and Gross Income Assessment, to ensure adequate contributions from each component fee, as well as adequate levels of funding overall. In addition, NASD previously stated its intent to reduce the percentage that the TAF contributes to the overall funding structure in 2004 and again in 2005 (increasing the percentage funded by the PA and holding the GIA percentage static). NASD remains committed to that program, and should regulatory costs and market volumes remain constant, fee levels for the TAF for 2004 could be expected to drop by approximately 20%. Of course, NASD will analyze all relevant factors prior to making any determination to modify the TAF.

Endnotes

- 1 Securities Exchange Act Rel. No. 48234 (July 28, 2003) (File No. SR-NASD-2003-93).
- 2 Securities Exchange Act Rel. No. 47946 (May 30, 2003), 68 FR 34021 (June 6, 2003) (File No. SR-NASD-2002-148).
- 3 Securities Exchange Act Rel. No. 47106 (Dec. 30, 2002), 68 FR 819 (January 7, 2003) (File No. SR-NASD-2002-99).
- 4 Securities Exchange Act Rel. No. 48061 (June 19, 2003), 68 FR 37877 (June 25, 2003) (File No. SR-NASD-2003-93).
- 5 Securities Exchange Act Rel. No. 48234 (July 28, 2003) (File No. SR-NASD-2003-93).
- 6 Specifically, NASD stated in the text of the TAF rule language that it will “periodically review these revenues in conjunction with these costs to determine the applicable rate.” NASD By-Laws, Schedule A, Section 1(a).

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