

Notice to Members

AUGUST 2006

SUGGESTED ROUTING

Finance
Legal & Compliance
Operations
Senior Management

KEY TOPICS

Away from the Market Sales
Odd-Lot Transactions
OTC Options
Regulatory Transaction Fee
Section 3 of Schedule A to
NASD By-Laws
Transaction Reporting

GUIDANCE

Automated Transaction Reporting

SEC Approves Amendments Relating to Automated Reporting of Transactions Subject to Regulatory Transaction Fee; **Effective Date: December 1, 2006**

Executive Summary

On June 12, 2006, the Securities and Exchange Commission (SEC) approved SR-NASD-2006-055 relating to automated reporting of transactions subject to the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws (NASD Section 3).¹ Specifically, effective December 1, 2006, members will be required to report to NASD in an automated manner all transactions that must be reported to NASD and that are subject to a regulatory transaction fee pursuant to NASD Section 3. Members can use NASD systems, including the Trade Reporting Facility (TRF), OTC Reporting Facility (OTCRF) and/or the Alternative Display Facility Trade Reporting and Comparison Service (TRACS) to report such transactions to NASD in an automated manner.

NASD also has amended certain rules governing trade reporting that currently prohibit member firms from reporting odd-lot transactions, sales where the buyer and seller have agreed to a price substantially unrelated to the current market for the security (also referred to as "away from the market sales"), and purchases or sales of securities effected upon the exercise of an over-the-counter (OTC) option, as well as other transactions, to clarify that the prohibition found in the transaction reporting rules is limited to the submission of a transaction for publication purposes. Lastly, NASD has amended Rules 6130 and 6130A to require members to report odd-lot transactions, away from the markets sales, and OTC option exercises with a special indicator denoting that such transactions are reported in accordance with NASD Section 3. The amended rule text is set forth in Attachment A. As noted above, the effective date is December 1, 2006.

Questions/Further Information

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

Background and Discussion

Section 31 of the Securities Exchange Act of 1934 (Exchange Act) requires NASD and national securities exchanges to pay transaction fees and assessments to the SEC that are designed to recover the costs related to the government's supervision and regulation of the securities markets and securities professionals. NASD obtains its Section 31 fees and assessments from its membership in accordance with NASD Section 3. NASD Section 3 assessments apply only to transactions effected otherwise than on a national securities exchange.² Many of the transactions that are assessable under NASD Section 3 are reported to NASD through automated facilities. NASD is able to use the transaction data reported to these automated facilities for NASD Section 3 billing purposes.

Currently, member firms are required to self-report manually covered sales of odd-lots, away from the market sales and the exercise of OTC options because these transactions are not otherwise required to be reported to NASD through an automated facility. To improve NASD's programs related to compliance with Section 31 of the Exchange Act and Rule 31 thereunder, NASD is requiring members to report in an automated manner all covered securities transactions that must be reported to NASD and that are assessed under NASD Section 3. While the previous manual self-reporting process has allowed NASD to meet its obligations under Section 31 of the Exchange Act, automated reporting of such covered transactions will facilitate more efficient, accurate and timely reporting to the SEC. Automated reporting also will reduce the burden on members that results from manually reporting certain transactions to NASD.

Under the new provisions, odd-lot transactions, away from the market sales and OTC option exercises must be submitted to the TRF, OTCRF or TRACS, as applicable, by 6:30 p.m. Eastern Time on the day of execution (or the end of the reporting session that is in effect at that time) with a special indicator denoting that such transactions are reported in accordance with NASD Section 3. Specifically, all odd-lot transactions effected by a member otherwise than on a national securities exchange that are subject to a regulatory transaction fee pursuant to NASD Section 3, must be submitted with a modifier of .RO; away from the market sales effected by a member otherwise than on a national securities exchange that are subject to a regulatory transaction fee pursuant to NASD Section 3 must be submitted with a modifier of .RA; and OTC option exercises that are subject to a regulatory transaction fee pursuant to NASD Section 3 must be reported with a modifier of .RX. The transactions may be entered as clearing or non-clearing, as appropriate. These entries will not be assessed any system usage fees by TRF, OTCRF or TRACS, unless the entry is submitted for clearing, in which case the normal clearing related fee schedule will apply.

As of December 1, 2006, NASD will require the automated reporting of all transactions effected otherwise than on a national securities exchange that must be reported to NASD and that are subject to a regulatory transaction fee pursuant to NASD Section 3. As a result, members will no longer be required to file a Self-Reporting Form with NASD's Finance Department. This rule change only applies to NASD Section 3 assessable transactions executed on or after December 1, 2006. Any NASD Section 3 assessable transaction that is subject to the self-reporting requirement executed prior to that date should not be reported to TRF, OTCRF or TRACS for this purpose, but should be submitted on the Self-Reporting Form for the applicable month.

Endnotes

- 1 See Exchange Act Release No. 53977 (June 12, 2006), 71 FR 34976 (June 16, 2006) (Approval Order of File No. SR-NASD-2006-055).
- 2 On August 1, 2006, The Nasdaq Stock Market LLC began operation as a national securities exchange for purposes of NASDAQ-listed securities. Additionally, NASDAQ has announced it will become operational as an exchange for Consolidated Quotation System (CQS) securities on approximately October 1, 2006. Accordingly, NASD is reminding members that transactions executed on the NASDAQ exchange are not subject to NASD Section 3 and should not be reported to NASD pursuant to this rule change.

©2006. NASD. All rights reserved. *Notices to Members* attempt to present information to readers in a format that is easily understandable. However, please be aware that, in case of any misunderstanding, the rule language prevails.

ATTACHMENT A

Changes are shown against the current rule text. New language is underlined; deletions are in brackets.¹

* * * * *

SCHEDULE A TO NASD BY-LAWS

* * * * *

Section 3 — Regulatory Transaction Fee

Each member shall be assessed a regulatory transaction fee. The amount shall be determined periodically in accordance with Section 31 of the Act. Transactions assessable under this Section 3 that must be reported to NASD shall be reported in an automated manner.

* * * * *

4000. THE TRADE REPORTING FACILITY

* * * * *

4630. Reporting Transactions in Designated Securities

* * * * *

4632. Transaction Reporting

(a) through (d) No Change.

(e) Transactions Not [Required] To Be Reported For Publication Purposes

The following types of transactions shall not be reported to the Trade Reporting Facility for publication purposes:

(1) through (6) No Change.

(f) through (g) No Change.

* * * * *

4000A. NASD ALTERNATIVE DISPLAY FACILITY

* * * * *

4600A. TRADING IN NASDAQ SECURITIES

* * * * *

4632A. Transactions Reported by Members

(a) through (j) No Change.

(k) Transactions Not To Be Reported To NASD For Publication Purposes

The following types of transactions effected by NASD members shall not be reported to TRACS for publication purposes:

(1) through (6) No Change.

(l) No Change.

* * * * *

6000. NASD SYSTEMS AND PROGRAMS

* * * * *

6100. CLEARING AND COMPARISON RULES

* * * * *

6130. Trade Report Input

(a) through (f) No Change.

(g) Reporting Certain Transactions for Purposes of Regulatory Transaction Fee Assessment

The following types of transactions that are assessed a regulatory transaction fee in accordance with Section 3 of Schedule A to the NASD By-Laws must be reported to the System as prescribed below. Transactions must be submitted to the System by 6:30 p.m. Eastern Time (or the end of the System reporting session that is in effect at that time).

(1) Odd-Lot Transactions

Transactions for less than a normal unit of trading shall be reported to the System with a modifier of .RO to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

(2) Away From the Market Sales

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 given, shall be reported to the System with a modifier of .RA to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

(3) Exercises of OTC Options

Transactions effected pursuant to the exercise of an OTC option shall be reported to the System with a modifier of .RX to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

* * * * *

6400. REPORTING TRANSACTIONS IN LISTED SECURITIES

* * * * *

6420. Transaction Reporting

(a) through (d) No Change.

(e) Transactions Not [Required] To Be Reported For Publication Purposes

The following types of transactions shall not be reported for inclusion on the Consolidated Tape:

(1) through (8) No Change.

(f) No Change.

* * * * *

6600. Over-The-Counter Equity Securities

* * * * *

6620. Transaction Reporting

(a) through (d) No Change.

(e) Transactions Not [Required] To Be Reported For Publication Purposes

The following types of transactions shall not be reported for publication purposes:

(1) through (4) No Change.

(f) No Change.

* * * * *

6000A. NASD ADF SYSTEMS AND PROGRAMS

6100A. TRACS TRADE COMPARISON SERVICE

* * * * *

6130A. Trade Report Input

(a) through (b) No Change.

(c) Reporting Certain Transactions for Purposes of Regulatory Transaction Fee Assessment

The following types of transactions that are assessed a regulatory transaction fee in accordance with Section 3 of Schedule A to the NASD By-Laws must be reported to TRACS as prescribed below. Transactions must be submitted to TRACS by 6:30 p.m. Eastern Time (or the end of the TRACS reporting session that is in effect at that time).

(1) Odd-Lot Transactions

Transactions for less than a normal unit of trading shall be reported to TRACS with a modifier of .RO to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

(2) Away From the Market Sales

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 given, shall be reported to TRACS with a modifier of .RA to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

(3) Exercises of OTC Options

Transactions effected pursuant to the exercise of an OTC option shall be reported to TRACS with a modifier of .RX to designate the transaction as submitted for purposes of the regulatory transaction fee under Section 3 of Schedule A to the NASD By-Laws. Transactions may be entered as clearing or non-clearing.

* * * * *

Endnote

- 1 The rule text set forth in this attachment incorporates the amendments approved in SR-NASD-2006-055, as well as technical amendments that became effective pursuant to SR-NASD-2006-098.