

October 14, 2003

Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: File No. SR-NASD-2003-157 – Permanent Approval of Fees for the Trade Reporting and Compliance Engine (TRACE)

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed please find the above-numbered rule filing. Also enclosed is a 3-1/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Kosha K. Dalal, Office of General Counsel, Regulatory Policy and Oversight, NASD, at (202) 728-6903; e-mail kosha.dalal@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Barbara Z. Sweeney
Senior Vice President
and Corporate Secretary

Enclosures

cc: Stephen L. Williams, Division of Market Regulation
Gordon K. Fuller, Division of Market Regulation
Mary N. Simpkins, Division of Market Regulation

File No. SR-NASD-2003-157
Consists of 59 Pages
October 14, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”), the National Association of Securities Dealers, Inc. (“NASD”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend NASD Rule 7010(k) relating to fees for the Trade Reporting and Compliance Engine (“TRACE”), and seeking permanent approval of the TRACE fee structure prior to the expiration of the pilot program for fees on January 31, 2004. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

7010. System Services

(a) through (j) No Change.

(k) Trade Reporting and Compliance Engine (TRACE)

[(Rule 7010(k) shall expire on January 31, 2004, 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
[From 07/01/02 to 12/31/02: Web Browser Access: \$85/month for 1 user ID; \$75/month for 2-9 user IDs; \$70/month for 2-10+ user IDs, except] [If less than 25 trades per month, in October,	[From 07/01/02 to 12/31/02: 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	BTDS Professional <u>Real-Time Data</u> Display - \$60/month per terminal, except [For a period of one calendar month to be announced: Waiver of fee (\$0)]

November, or December 2002 - \$25/month per user ID] [From 01/01/03 to 01/31/04: Level I Trade Report Only Web Browser Access - \$25/month per user ID] [Level II Full Service Web Browser Access - \$85/month per user ID, except] <u>Level I Trade Report Only Web Browser Access - \$20/month per user ID</u> <u>Level II Full Service Web Browser Access - \$80/month per user ID</u> [For a period of one calendar month to be announced: Level II Full Service Web Browser Access – will be \$25/month per user ID]	value or more - \$2.50/trade] [From 01/01/03 to 01/31/04:] Trades up to and including \$200,000 par value - \$0.475/trade; Trades between \$201,000 and \$999,999 par value - \$0.002375 times the number of bonds traded/trade; Trades of \$1,000,000 par value or more - \$2.375/trade	
CTCI/<u>Third Party</u> - \$25/month/per firm	[From 07/01/02 to 12/31/02: Cancel/Correct - \$3/trade, except For October 2002 - \$1.50/trade For November 2002 - \$2.25/trade] [From 01/01/03 to 01/31/04:]Cancel/Correct - \$1.50/trade	<u>BTDS Professional Delayed-Time Data Display - \$15/month per terminal</u>
[Third Party - \$25/month]	[From 07/01/02 to 12/31/02: “As of” Trade Late - \$3/trade, except For October 2002 - \$1.50/trade	BTDS Internal Usage Authorization - \$500/month per application/service <u>for Real-Time and Delayed-Time Data</u>

	For November 2002 - \$2.25/trade] [From 01/01/03 to 01/31/04:] “As of” Trade Late - \$3/trade	
	[Browse & Query - \$0.05 after first page]	BTDS External Usage Authorization - \$1,000/month per application/service <u>for Real-Time and Delayed-Time Data</u>
`		BTDS Non-Professional <u>Real-Time Data Display</u> - \$1/month per terminal

(1) System Related Fees. There are three methods by which a member may report corporate bond transactions that are reportable to NASD pursuant to the Rule 6200 Series. A member may choose among the following methods to report data to NASD: (a) a TRACE web browser; (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

[(i) For the period commencing July 1, 2002 and ending December 31, 2002, the charge to be paid by a member that elects to report TRACE data to NASD 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.]

[(ii) For the period commencing January 1, 2003 and ending January 31, 2004, the charge to be paid by a member that elects to report TRACE data to NASD via a TRACE web browser shall be as follows: \$25 per month, per user ID for Level I Web Trade Report Only Browser Access and \$85 per month, per user ID for Level II Full Service Web Browser Access.] The charge to be paid by a member that elects to report TRACE data to NASD via a TRACE web browser shall be as follows: \$20 per month, per user ID for Level I Web Trade Report Only Browser Access and \$80 per month, per user ID for Level II Full Service Web Browser Access. [Notwithstanding the above sentence, following the effective date of increased bond data dissemination as approved by the SEC on January 31, 2003, NASD shall announce a period of one calendar month during which the charge for Level II Full Service Web Browser Access shall be \$25 per month, per user ID.]

(B) Computer-to-Computer Interface Access

The charge to be paid by a member that elects to report TRACE data to NASD via a CTCI line shall be \$25 per month, per firm[line], regardless of whether the line is or is not dedicated exclusively for TRACE.^[6]¹

(C) Third Party Access – Indirect Reporting

A member may elect to report TRACE data indirectly to NASD via third-party reporting intermediaries, such as vendors, service bureaus, or the National Securities Clearing Corporation (“NSCC”). The charge to be paid by a member shall be \$25 per month, per firm. Nothing in this Rule shall prevent such third-party intermediaries from charging additional fees for their services.

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

(A) Trade Reporting Fee

[(i) For the period commencing July 1, 2002 and ending December 31, 2002, a member shall be charged a Trade Reporting Fee based upon a sliding scale ranging from \$0.50 to \$2.50 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.50 fee per

trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.0025 multiplied by the number of bonds traded per trade; and trades of \$1,000,000 par value or more will be charged a fee of \$2.50 per trade.]

[(ii) For the period commencing January 1, 2003 and ending January 31, 2004, a] A member shall be charged a Trade Reporting Fee based upon a sliding scale ranging from \$0.475 to \$2.375 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.475 fee per trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.002375 multiplied by the number of bonds traded per trade; and trades of \$1,000,000 par value or more will be charged a fee of \$2.375 per trade.

(B) Cancel or Correct Trade Fee

[For the period commencing July 1, 2002 and ending December 31, 2002, 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. For the period commencing January 1, 2003 and ending January 31, 2004, a]A member shall be charged a Cancel or Correct Trade Fee of \$1.50 per canceled or corrected transaction.

(C) “As of” Trade Late Fee

[For the period commencing July 1, 2002 and ending December 31, 2002, a]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. For the period commencing January 1, 2003 and ending January 31, 2004, a member shall be charged an “As of” Trade Late Fee of \$3.00 per canceled or corrected transaction.]

[(D) Browse and Query Fee

Members may review their own previously reported transaction data through a Browse and Query function. A member shall be charged \$0.05 for each returned page of the query beyond the first page.]

(3) Market Data Fees

Professionals and non-professionals may subscribe to receive R[real-T[time and Delayed-Time TRACE data disseminated by NASD in one or more of the following ways for the charges specified. Members, vendors and other redistributors shall be required to execute appropriate agreements with NASD.

(A) Professional Fees. Professionals may subscribe for the following:

(i) Bond Trade Dissemination Service (“BTDS”) Professional Real-Time Data Display Fee of \$60 per month, per terminal charge for each interrogation or display device receiving R[real-T[time TRACE transaction data. [Notwithstanding the above sentence, following the effective date of increased bond data dissemination as approved by the SEC on January 31, 2003^[7], NASD shall announce a period of one calendar month during which NASD shall waive the \$60 per terminal, per month charge.]

(ii) BTDS Professional Delayed-Time Data Display Fee of \$15 per month, per terminal charge for each interrogation or display device receiving Delayed-Time TRACE transaction data; provided, that subscribers to the BTDS Professional Real-Time Data Display Fee described above shall not be charged this additional fee. Subject to the execution of appropriate agreements with NASD, certain summary market information of Delayed-Time TRACE transaction data may be published or

distributed by newspapers, press associations, newsletters, or similar media sources without charge.

(iii) BTDS Internal Usage Authorization Fee of \$500 per month, per application/service [charge] for internal dissemination of R[r]eal-T[t]ime and/or Delayed-Time TRACE transaction data used in one or more of the following ways in a single application/service: internal operational and processing systems, internal monitoring and surveillance systems, internal price validation, internal portfolio valuation services, internal analytical programs leading to purchase/sale or other trading decisions, and other related activities.^[8]2

(iv) BTDS External Usage Authorization Fee of \$1,000 per month, per application/service [charge] for dissemination of R[r]eal-T[t]ime and/or Delayed-Time TRACE transaction data used in one or more of the following ways in a single application/service: repackaging of market data for delivery and dissemination outside the organization, such as indices or other derivative products.^[9]3

(B) Non-Professional Fees

The charge to be paid by a non-professional for each terminal receiving all or any portion of R[r]eal-T[t]ime TRACE transaction data disseminated through TRACE shall be \$1.00 per month, per terminal.

(C) Definitions

(i) “Delayed-Time” as used in Rule 7010(k)(3) shall mean that period of time starting four hours after the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending at 11:59:59 p.m. Eastern Time that calendar day.

(ii) “Non-Professional”- A non-professional subscriber must provide certain information to NASD and shall receive TRACE market data primarily for his or her personal, non-commercial use. As used in Rule 7010(k)(3) [A]a “non-professional” is a natural person who is neither:

(a) registered nor qualified in any capacity with the Commission, the Commodity Futures Trading Commission, any state securities agency, any securities exchange or association, or any commodities or futures contract market or association, or an employee of the above who uses such information primarily for business-related activities;[or]

(b) engaged as an “investment adviser” as that term is defined in Section 202(a)(11) of the Investment Advisers Act of 1940 (whether or not registered or qualified under that Act), or an employee of the above who uses such information primarily for business-related activities;

(c) employed by a bank, insurance company or other organization exempt from registration under federal or state

securities laws to perform functions that would require registration or qualification if such functions were performed for an organization not so exempt; or

(d) engaged in, or has the intention to engage in, any redistribution of all or any portion of the information disseminated through TRACE.

(iii) “Real-Time” as used in Rule 7010(k)(3) shall mean that period of time starting from the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending no more than four hours thereafter.

(D) Other Requests for Data

NASD may impose and collect charges for data NASD supplied upon request, where there is no provision elsewhere in this Rule 7010(k) for charges for such service or sale.

[6]1 The charges that may be imposed by third parties, such as CTCI line providers, are not included in these fees.

[7] [On January 31, 2003, the SEC approved amendments to NASD Rule 6250 of the TRACE rules that will allow NASD to begin disseminating transaction information on more than 4,000 qualifying Investment Grade corporate debt securities. See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 FR 6233 (February 6, 2003) (File No. SR-NASD-2002-174).]

[8]2 Under this service, R[real-T]ime and/or Delayed-Time TRACE transaction data may not be used in any interrogation display devices, any systems that permit end users to determine individual transaction pricing[in real-time], or disseminated to any external source.

[9]3 Under this service, R[real-T]ime and/or Delayed-Time TRACE transaction data may not be used in any interrogation display devices or any systems that permit end users to determine individual transaction pricing[in real-time].

* * * * *

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) Certain fees that are part of the proposed rule change were approved by the Board of Governors of NASD ("Board") at its meeting on July 31, 2003, which authorized the filing of the rule change with the SEC. Certain other fees that are part of the proposed rule change were approved by the Board and authorized for filing with the SEC pursuant to a delegation of authority granted by the Board at its meeting on July 31, 2003, to the Chief Executive Officer of NASD and the Presidents of the Regulatory Policy and Oversight Division, the Regulatory Services and Operations Division, and the Dispute Resolution Division of NASD to file, without further specific Board authorization, de minimis changes to fees administered by NASD ("Delegation of Authority"). Counsel for The Nasdaq Stock Market and NASD Dispute Resolution have been provided an opportunity to consult with respect to the proposed rule change, including the Delegation of Authority, pursuant to the Plan of Allocation and Delegation of Functions by NASD to its Subsidiaries. NASD staff will advise the Board of any action taken pursuant to the Delegation of Authority. No other action by NASD is necessary for the filing of the proposed rule change. NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 30 days following

Commission approval. The effective date will be on the first day of the full calendar month following the month that the Commission approves the proposed rule change.¹

(b) Questions regarding this rule filing may be directed to Kosha K. Dalal, Assistant General Counsel, Office of General Counsel, Regulatory Policy and Oversight, NASD at (202) 728-6903.

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

(a) Purpose

NASD is proposing the rule change to establish a permanent fee structure for the TRACE system. TRACE became effective on July 1, 2002. At such time, the Commission approved the original fee structure for TRACE on a pilot basis. Since then, NASD staff has been committed to reassessing the TRACE fee structure based on actual information collected such as the number of participants, debt securities transaction volume, and subscribers for transaction data. During the last fourteen months, in response to industry concerns and emerging trends, NASD staff has revised the TRACE fee structure five times. Following more than a year of reassessment of the originally approved TRACE fees, NASD believes the fees are reasonable and necessary to ensure recovery of developmental costs of the TRACE system, fund ongoing operational costs, and fund the regulatory activities necessary for surveillance of the market. NASD believes the proposed rule change will equitably distribute the costs to participants of the TRACE system. While NASD is seeking permanent approval of the TRACE fees, NASD remains committed to periodically reassessing the appropriateness of TRACE fees.

¹ Subject to any notices that may be required to be given under applicable agreements.

Background

In 1998, former U. S. Securities and Exchange Commission (“SEC”) Chairman Arthur Levitt requested NASD to provide increased transparency in, and better surveillance of, the corporate debt market by (i) requiring that NASD members report corporate bond transactions to NASD; (ii) developing a system or systems to surveill the corporate debt market, including an audit trail of reported transactions; and (iii) delivering price and other information to large and small investors and other debt market participants. At that time, NASD began to develop TRACE and make it operational.

On June 28, 2002, the SEC 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, 2002.² 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.

On November 15, 2002 NASD filed, for immediate effectiveness, a rule filing to reduce certain TRACE fees for the 4th quarter of 2002.³ On December 16, 2002, NASD filed for immediate effectiveness, a rule filing to extend the pilot program for TRACE fees to February 28, 2003 and modify certain fees effective January 1, 2003.⁴ On February 27, 2003, NASD filed, for immediate effectiveness, a rule filing to extend the pilot program

² 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).

³ See Securities Exchange Act Release No. 46893 (November 22, 2002), 67 FR 72008 (December 3, 2002) (File No. SR-NASD-2002-167).

⁴ See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002) (File No. SR-NASD-2002-176).

for TRACE fees to June 30, 2003.⁵ On June 17, 2003 NASD filed, for immediate effectiveness, a rule filing to extend the pilot for TRACE fees to January 31, 2004.⁶

Operational Information

Since TRACE reporting began on July 1, 2002, approximately 1,800 NASD member firms have registered for TRACE reporting. Currently, approximately 28,000 corporate debt issues are subject to TRACE reporting requirements. Dissemination, however, currently occurs for approximately 4,700 of these corporate debt issues as TRACE transaction data is being disseminated in phases.⁷ In January 2001, the Commission initially approved “Phase I” dissemination of TRACE transaction data.⁸ On the first day of “Phase I” dissemination (July 1, 2002), approximately 550 corporate bonds became subject to dissemination.⁹ In January 2003, the Commission approved “Phase II”

⁵ See Securities Exchange Act Release No. 47444 (March 4, 2003), 68 FR 11602 (March 11, 2003) (File No. SR-NASD-2003-25).

⁶ See Securities Exchange Act Release No. 48110 (July 7, 2003), 68 FR 40315 (June 30, 2003) (File No. SR-NASD-2003-97).

⁷ NASD continues to review proposals to increase the number of TRACE-eligible securities that will be subject to dissemination.

⁸ Specifically, under Rule 6250, transactions in two types of securities were subject to the TRACE dissemination requirements that took effect on July 1, 2002: (1) those transactions in a TRACE-eligible security having an initial issuance size of \$1 billion or greater that is Investment Grade at the time of receipt of the transaction report as set forth in Rule 6250(a)(1); and (2) those transactions in 50 TRACE-eligible debt securities that are actively traded, rated Non-Investment Grade, and meet other criteria set forth in Rule 6250(a)(2). See Securities Exchange Act Release No. 46144 (June 28, 2002), 67 FR 44907 (July 5, 2002) (File No. SR-NASD-2002-46).

⁹ This group of bonds includes what was previously referred to as the FIPs 50 and which are now referred to as the TRACE 50. The list of 50 bonds is updated periodically based on criteria identified in Rule 6250(a)(2).

dissemination of TRACE transaction data.¹⁰ On the first day of “Phase II” dissemination (March 3, 2003), an additional approximately 3,800 corporate bonds became subject to dissemination, and on April 14, 2003, an additional approximately 120 triple-B-rated corporate bonds were also disseminated as part of “Phase II.”¹¹ In addition, in June 2003, reporting time for transactions in TRACE-eligible securities was reduced from 75 minutes to 45 minutes effective as of October 1, 2003.¹² In July 2003, the disseminated list of high-yield bonds referred to as the “TRACE 50” was updated.¹³

Since the launch of TRACE, NASD has enhanced the system with two major and five minor software releases in response to user needs, conducted routine monitoring of daily reported transaction data for accuracy, and undertaken regulatory activities to surveil the corporate debt market. TRACE incurs ongoing operating costs associated

¹⁰ In “Phase II” NASD began to disseminate transaction information on two additional categories of securities. On March 3, 2002, NASD began to disseminate transaction information on any TRACE-eligible security that is Investment Grade; is rated by Moody’s Investors Service, Inc. as “A3” or higher, and by Standard & Poor’s, a division of McGraw Hill Co., Inc., as “A-” or higher; 5 and has an original issue size of \$100 million or greater. In addition, a security that is required to be disseminated under the criteria above, on or after the effective date of this provision, will continue to be subject to dissemination unless the security is downgraded below “Baa3/BBB. A specified group of TRACE-eligible securities rated Baa/BBB, at the time of designation, were also approved for dissemination by the SEC. Originally, 90 securities were designated. See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 FR 6233 (February 6, 2003) (File No. SR-NASD-2002-174). However, in March 2003, NASD proposed to increase the number of “triple-B-rated” securities to approximately 120. See Securities Exchange Act Release No. 47566 (March 25, 2003), 68 FR 15490 (March 31, 2003) (File No. SR-NASD-2003-41). The 120 “triple-B-rated” securities were designated after the SEC approved SR-NASD-2003-41, and transaction information on the designated securities began to be disseminated on April 14, 2003.

¹¹ See Securities Exchange Act Release No. 47566 (March 25, 2003), 68 FR 15490 (March 31, 2003) (File No. SR-NASD-2003-41).

¹² See Securities Exchange Act Release No. 48056 (June 18, 2003), 68 FR 37886 (June 25, 2003) (File No. SR-NASD-2003-78).

¹³ The list of TRACE 50 bonds is updated periodically based on criteria identified in Rule 6250(a)(2).

with shared NASD infrastructure and resources as well as direct charges from outsourcing TRACE system support and development. Additionally, TRACE is supported by a dedicated team of NASD staff. For the first twelve months of operation (period ending June 30, 2003), these expenses have totaled approximately \$12.4 million including partial recovery of the original investment made in the development of TRACE.¹⁴

As detailed in this filing, revenues are derived from a combination of System Fees to access TRACE, Transaction Reporting Fees for trade reporting, and Market Data Fees for access and display of aggregated TRACE data. For the first twelve months of operation (period ending June 30, 2003), TRACE generated revenues of approximately \$12.4 million reflecting approximately \$2.0 million, \$8.9 million, and \$1.5 million for System Fees, Transaction Reporting Fees, and Market Data Fees, respectively.

The proposed fees are also divided into the same three general categories: (1) System fees paid by member firms based on the technology method chosen by the member to report corporate bond transactions; (2) transaction reporting fees paid by members to file trade reports and cancel or correct trade reports; and (3) market data fees paid by members and non-members that use or distribute the data collected through the TRACE system and disseminated by NASD. NASD is hereby seeking permanent approval of the fees relating to the TRACE system. However, NASD remains committed to reviewing and reassessing TRACE fees over time.

¹⁴

Under this approach the original investment costs are recovered over a 48-month period.

System Fees

A member may report TRACE transaction data to NASD by one of three approved methods: (1) web browser access; (2) direct computer-to-computer interface (“CTCI”); or (3) indirectly through third-parties, such as vendors, service bureaus, clearing firms, or the National Securities Clearing Corporation. The member determines the reporting method they would like to use based on such factors as volume, size, and cost.

Web Browser Access Fees

In response to requests from the industry, in January 2003, NASD introduced a modified web browser and adjusted the fees accordingly.¹⁵ The modified web browser separated reporting capabilities from query features that allow access to TRACE transaction data. NASD began offering two web browser service levels on January 1, 2003: (1) Level I Trade Report Only Web Browser access permits a member to report TRACE transaction data to NASD over the internet, but does not allow access to real-time TRACE data, and (2) Level II Full Service Web Browser access permits reporting of TRACE transaction data to NASD over the internet and allows access to real-time transaction data through a query function. The original charge for Level I service is \$25 per month, per user ID, and the charge for Level II service is \$85 per month, per user ID.

NASD is proposing to reduce the Level I charge from \$25 per month, per user ID, to \$20 per month, per user ID, and to reduce the Level II charge from \$85 per month, per user ID, to \$80 per month, per user ID. The modified web browser allows participants to

¹⁵ See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002) (File No. SR-NASD-2002-176).

satisfy their reporting obligations to NASD at a base level cost of \$20 per month, per user ID. Participants that wish to have access to additional services such as real-time data query, pay \$80 per month, per user ID. In this way, NASD believes that cost of delivering this service will be more equitably distributed to members that directly use this additional technology for their business.

In March 2003, NASD submitted a rule filing to the Commission proposing to (1) temporarily reduce the Level I Full Service Web Browser Access Fee, and (2) temporarily waive the BTDS Professional Real-Time Data Display Fee for a one-month period to be announced by NASD. NASD originally sought these temporary reductions to provide subscribers a “trial month” to explore the services. However, third-party vendors have raised concerns with NASD staff that the imposition of one “trial month” will be difficult for them to administer and may not have the desired effect of bringing on new TRACE data subscribers. Therefore, NASD is proposing to eliminate these temporary reductions.

CTCI Fees and Third-Party Vendor Fees

The charge for CTCI service and for reporting data through third-party vendors will remain the same - \$25 per month. NASD had originally provided participants the option of reporting TRACE data to NASD through a secure, private data network. However, no subscribers registered for this service and in a rule filing submitted to the SEC on December 16, 2002, NASD proposed to eliminate this service and the corresponding fee as of January 1, 2003. NASD proposes to make this change permanent.

NASD believes that the TRACE system fees are reasonable and non-discriminatory because members may select the technology link that best suits their particular needs. The Web Browser Access Fees have been significantly modified from the original level established in July 2002.¹⁶ Firms that have a smaller volume of TRACE transactions now have a cost-effective reporting option (e.g., Level I Trade Report Web Browser). Larger volume firms have generally been reporting TRACE transaction data either through a CTCI line at a charge of \$25 per month, or through third-parties at a charge of \$25 per month.

Transaction Reporting Fees

Trade Reporting Fees

Following the start of operations of TRACE, NASD staff has been collecting data on trade reporting fees incurred by participants. The revenues generated by this fee were higher than originally forecasted. As a result, as of January 1, 2003, NASD reduced trade reporting fees by 5% from the original fee levels.¹⁷ NASD seeks permanent approval of the reduced trade reporting fees. Trade Reporting Fees will continue to be on a sliding scale, based upon the size of the transaction reported, in an effort to distribute the fees

¹⁶ In the original fee approval order, the Web Browser Access Fee for each registered participant was: \$85 per month, per user ID, for the first user ID; \$75 per month for the second through ninth user ID; and \$70 per month for the second through tenth or more user ID, if the participant registers ten or more user IDs. For the fourth quarter of 2002, the Web Browser Access Fee was reduced to \$25 per month, per user ID for participants that reported less than 25 transactions during the months of October, November, and December 2002.

¹⁷ The original Trade Reporting Fees were also based on a sliding scale that ranges from \$0.50 to \$2.50 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value are charged a \$0.50 fee per trade; trades between \$201,000 par value and \$999,999 par value are charged a fee of \$0.0025 multiplied by the number of bonds traded; and trades of \$1,000,000 par value or more are charged a fee of \$2.50 per trade.

more equitably between retail oriented firms and institutionally oriented firms.¹⁸ The range for trade reporting fees will be from \$0.475 to \$2.375 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.475 fee per trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.002375 multiplied by the number of bonds traded, and trades of \$1,000,000 par value or more will be charged a fee of \$2.375 per trade.

Corrective Transaction Fees

NASD proposes to set the permanent Cancel or Correct Fee at \$1.50 per corrected trade and the “As of” Trade Late reporting fee at \$3.00 per late trade. Cancel, correct, and “As of” transactions are used by participants to modify original trade entries. While a certain level of corrective transactions will always be necessary, NASD staff 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. Further, continued high levels of corrective transactions will increase NASD’s technology costs.

The original charge for the Cancel or Correct Fee and the “As of” Late Fee was \$3.00 for each such reported transaction. However, in the original fee proposal, NASD delayed the effectiveness of the Cancel or Correct Fee and the “As of” Late Fee to October 1, 2002. Based on NASD staff review of the data collected on such fees after the first three months of TRACE operation, on November 15, 2002, NASD submitted a

¹⁸ In approving the original TRACE fees on a pilot basis, the Commission stated that “[t]he Commission believes that this sliding scale structure promotes an equitable distribution of the relevant fees while reducing the possibility of unfair discrimination between customers, issuers,

proposed rule change to the SEC to phase in the implementation of the two fees during the last quarter of 2002 to allow participants greater time to adjust to the new system and focus on methods to reduce the likelihood of incurring such fees.¹⁹ For the month of October 2002, the Cancel or Correct Fee and the “As of” Late Fee charge assessed to each participant were reduced from \$3.00 per trade to \$1.50 per trade (a 50% discount), and for the month of November 2002, the Cancel or Correct Fee and the “As of” Late Fee were reduced from \$3.00 per trade to \$2.25 per trade (a 25% discount). On December 16, 2002, NASD submitted a rule filing to reduce the Cancel or Correct Fee from \$3.00 to \$1.50 effective January 1, 2003.

NASD staff has been working with the industry to determine the causes of erroneous transactions as part of a goal of reducing the number of corrective transactions reported to TRACE. NASD staff believes that over time the number of corrective transactions submitted to the system will decline. However, NASD believes that fees for corrective transactions are necessary to discourage erroneous reporting and to improve the integrity of disseminated data. Therefore, NASD is proposing that the SEC permanently approve the current corrective transaction fees.

Browse and Query Fees

NASD is proposing to eliminate the Browse and Query Fee of \$0.05 per page after the first page. This feature allows firms to review previously reported transaction data. Firms will continue to have access to this service, however, there will no longer be a fee associated with such service.

brokers, or dealers.” See SEC Approval Order File No. SR-NASD-2002-63, Securities Exchange Act Release No. 46145 (June 28, 2002).

Market Data Fees

The current market data fees are as follows: (1) BTDS Professional Real-Time Data Display Fee - \$60 per month, per terminal; (2) BTDS Internal Usage Authorization Fee - \$500 per month, per application/service; (3) BTDS External Usage Authorization Fee - \$1,000 per month, per application/service; and (4) BTDS Non-Professional Real-Time Fee - \$1 per month, per terminal.

NASD is proposing to define the terms “Real-Time” and “Delayed-Time” as they relate to market data fees for TRACE transaction data. “Real-Time” as used in Rule 7010(k)(3) shall mean that period of time starting from the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending four hours thereafter. “Delayed-Time” as used in Rule 7010(k)(3) shall mean that period of time starting four hours after the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending at 11:59:59 p.m. Eastern Time that calendar day.

In addition, NASD is proposing to establish a charge to professionals for the use of Delayed-Time TRACE transaction data. Discussions with members of the bond industry indicate that there is increasing demand for Delayed-Time TRACE transaction data by professionals. Market professionals have indicated to NASD staff that, as a result of relatively low individual bond trading activity levels on any given day, Delayed-Time transaction data is useful to see overall patterns and trends, especially in pricing. Because of the time lag between trades in less active issues often exceeds four hours, the value of the last sale information on a four hour Delayed-Time basis often equals that of the real-time information. NASD staff believes that professionals who use this data in the course

See SR-NASD-2002-167 (November 15, 2002).

of their business or commercial activities should pay for the use of the data.

Consequently, NASD staff believes that a charge for professionals for Delayed-Time data is appropriate.

The fee for the BTDS Professional Delayed-Time Data Display would be \$15 per month, per terminal, for each device receiving Delayed-Time TRACE transaction data.²⁰ Professionals subscribing for the BTDS Professional Real-Time Data Display Fee of \$60 per month, per terminal, to receive Real-Time TRACE transaction data would not pay this charge for Delayed-Time data in addition to the \$60 fee for Real-Time data. Subject to the execution of appropriate agreements with NASD, certain summary market information of Delayed-Time TRACE transaction data may be published or distributed by newspapers, press associations, newsletters, or similar media sources (including in some cases members) without charge. NASD is also proposing to clarify that charges for BTDS Internal Usage and BTDS External Usage apply to Real-Time and/or Delayed-Time TRACE transaction data.

In addition, NASD proposes to clarify the definition of “non-professional.” Since the start of TRACE, numerous individuals have questioned whether they qualify as a “non-professional.” To clear up confusion, NASD is proposing to add language to the definition to state that a natural person can qualify as a “non-professional” only if they receive TRACE market data primarily for personal, non-commercial use.

In the original fee proposal, NASD had provided for a daily list fax service that would provide subscribers with daily additions, deletions, and modifications to the list of

²⁰ Transaction data for TRACE-eligible securities disseminated by NASD after this time frame will be provided free of charge.

TRACE-eligible securities. The charge for this service was \$15 per month, per fax number/addressee. One user subscribed for this service and it was no longer cost effective for NASD to continue providing the service. As a result, NASD proposed in a rule filing submitted to the SEC on December 16, 2002 to eliminate this service and the corresponding fee as of January 1, 2003.²¹ NASD proposes to make this change permanent.

NASD believes the market data fees are reasonable and non-discriminatory. The fees are charged only to market professionals that wish to subscribe for these optional services. NASD believes that this use-based approach appropriately aligns costs with member usage and is consistent with equitable distribution of fees.

Other Requests for Data

From time to time, members, vendors, and other persons request certain ad hoc services or uses of the TRACE system and transaction data that are not otherwise covered by Rule 7010(k). NASD believes that providing such services to the industry, academia, or others is useful and proposes to collect charges when fulfilling these requests. Charges would be commensurate with the higher of a) NASD's associated costs or b) similar products or services available in the marketplace.

Permanent Approval of Fees

NASD is seeking permanent approval of the TRACE fee structure prior to the expiration of the pilot program for TRACE fees that is scheduled to expire on January 31,

²¹ See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002)(File No. SR-NASD-2002-176).

2004. NASD believes that the proposed fee structure for TRACE is reasonable and non-discriminatory. In its original approval of the TRACE fees pilot, the Commission stated that it believes that the fees allow users great flexibility in how they will interact with the system, and are scaled according to objective criteria applied across-the-board to all categories of users.²²

NASD believes the fee structure is equitable and the charges are based on actual usage of the system. For example, trade reporting fees are based on a sliding scale that varies depending on the size of the transaction reported, with fees ranging from \$0.475 (for the smallest trades) to \$2.375 (for the largest trades). System fees allow participants to select the most cost-effective reporting method and web browser fees are based on usage (users of the real-time transaction query feature pay more for the additional service). Similarly, market data fees are lower for users who limit their use of the TRACE transaction data to internal distribution, and relatively higher for users who use or distribute the data externally.

For these reasons, NASD believes the fees set forth above are reasonably related to the costs of developing the facility and to meeting the estimated operating expenses of the TRACE system. The fees are also designed to fund the regulatory activities necessary to surveil the market. In addition, NASD staff believes that it has responded promptly to the concerns of members by reducing TRACE fees.

As part of the initiative by the Commission to create price transparency in the corporate bond market, the NASD has worked diligently to develop the TRACE system.

²² See SEC Approval Order File No. SR-NASD-2002-63, Securities Exchange Act Release No. 46145 (June 28, 2002).

NASD staff continues to work closely with the Bond Transaction Reporting Committee, which is jointly staffed by members designated by NASD and The Bond Market Association. In addition, NASD staff has met formally and informally with members of the industry and listened to their questions and concerns. Overall, NASD believes the TRACE fee structure is reasonable and non-discriminatory, and that the proposed fees are necessary to achieve a practical, market-driven system for processing and disseminating reliable and uniform corporate bond data. NASD is committed to taking a proactive role in supervising the corporate bond market and promoting investor confidence in the fairness of the corporate bond market generally.

NASD remains committed to reviewing and reassessing the appropriateness of TRACE fees over time to ensure that the fees are reasonable and equitable for participants in the TRACE system.

Based on the above, the NASD believes the proposed rule change is consistent with the provisions of Section 15A(b)(5)²³ of the Act in that the proposal provides for the equitable allocation of reasonable dues, fees, and other charges among members and other persons using any facility or system which the association operates or controls.

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, 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.

²³ 15 U.S.C. 78o-3(b)(5).

In addition, NASD believes that the proposed rule change is consistent with Section 15A(b)(5) of the Act, 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. NASD is seeking permanent approval of the TRACE fee structure and believes that the proposed fee structure is reasonable.

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.

6. Extension of Time Period for Commission Action

NASD does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

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

Not applicable.

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

Not applicable.

9. Exhibits

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

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD, INC.

BY: _____
Barbara Z. Sweeney , Senior Vice President and
Corporate Secretary

Date: October 14, 2003

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34- [leave space] ; File No. SR-NASD-2003-157)
[leave space for date]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Permanent Fee Structure for the Trade Reporting and Compliance Engine (TRACE)

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on October __, 2003, 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.

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) relating to fees for the Trade Reporting and Compliance Engine (“TRACE”) prior to the expiration of the pilot program for fees on January 31, 2004 and seeking permanent approval of the fee structure. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

7010. System Services

(a) through (j) No Change.

¹ 15 U.S.C. § 78s(b)(1).

(k) Trade Reporting and Compliance Engine (TRACE)

[(Rule 7010(k) shall expire on January 31, 2004, 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
[From 07/01/02 to 12/31/02: Web Browser Access: \$85/month for 1 user ID; \$75/month for 2-9 user IDs; \$70/month for 2-10+ user IDs, except] [If less than 25 trades per month, in October, November, or December 2002 - \$25/month per user ID] [From 01/01/03 to 01/31/04: Level I Trade Report Only Web Browser Access - \$25/month per user ID] [Level II Full Service Web Browser Access - \$85/month per user ID, except] <u>Level I Trade Report Only Web Browser Access - \$20/month per user ID</u> <u>Level II Full Service Web Browser Access - \$80/month per user ID</u> [For a period of one calendar month to be announced: Level II Full Service Web Browser Access – will be \$25/month per user ID]	[From 07/01/02 to 12/31/02: 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] [From 01/01/03 to 01/31/04:] Trades up to and including \$200,000 par value - \$0.475/trade; Trades between \$201,000 and \$999,999 par value - \$0.002375 times the number of bonds traded/trade; Trades of \$1,000,000 par value or more - \$2.375/trade]	BTDS Professional <u>Real-Time Data Display</u> - \$60/month per terminal, except [For a period of one calendar month to be announced: Waiver of fee (\$0)]

CTCI/ <u>Third Party</u> - \$25/month/per firm	[From 07/01/02 to 12/31/02: Cancel/Correct - \$3/trade, except For October 2002 - \$1.50/trade For November 2002 - \$2.25/trade] [From 01/01/03 to 01/31/04:]Cancel/Correct - \$1.50/trade	<u>BTDS Professional Delayed-Time Data Display - \$15/month per terminal</u>
[Third Party - \$25/month]	[From 07/01/02 to 12/31/02: “As of” Trade Late - \$3/trade, except For October 2002 - \$1.50/trade For November 2002 - \$2.25/trade] [From 01/01/03 to 01/31/04:] “As of” Trade Late - \$3/trade	BTDS Internal Usage Authorization - \$500/month per application/service for <u>Real-Time and Delayed-Time Data</u>
	[Browse & Query - \$0.05 after first page]	BTDS External Usage Authorization - \$1,000/month per application/service for <u>Real-Time and Delayed-Time Data</u>
`		BTDS Non-Professional <u>Real-Time Data Display</u> - \$1/month per terminal

(1) System Related Fees. There are three methods by which a member may report corporate bond transactions that are reportable to NASD pursuant to the Rule 6200 Series. A member may choose among the following methods to report data to NASD: (a) a TRACE web browser; (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

[(i) For the period commencing July 1, 2002 and ending December 31, 2002, the charge to be paid by a member that elects to report TRACE data to NASD 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.]

[(ii) For the period commencing January 1, 2003 and ending January 31, 2004, the charge to be paid by a member that elects to report TRACE data to NASD via a TRACE web browser shall be as follows: \$25 per month, per user ID for Level I Web Trade Report Only Browser Access and \$85 per month, per user ID for Level II Full Service Web Browser Access.] The charge to be paid by a member that elects to report TRACE data to NASD via a TRACE web browser shall be as follows: \$20 per month, per user

ID for Level I Web Trade Report Only Browser Access and \$80 per month, per user ID for Level II Full Service Web Browser Access. [Notwithstanding the above sentence, following the effective date of increased bond data dissemination as approved by the SEC on January 31, 2003, NASD shall announce a period of one calendar month during which the charge for Level II Full Service Web Browser Access shall be \$25 per month, per user ID.]

(B) Computer-to-Computer Interface Access

The charge to be paid by a member that elects to report TRACE data to NASD via a CTCI line shall be \$25 per month, per firm[line], regardless of whether the line is or is not dedicated exclusively for TRACE.[⁶]¹

(C) Third Party Access – Indirect Reporting

A member may elect to report TRACE data indirectly to NASD via third-party reporting intermediaries, such as vendors, service bureaus, or the National Securities Clearing Corporation (“NSCC”). The charge to be paid by a member shall be \$25 per month, per firm. Nothing in this Rule shall prevent such third-party intermediaries from charging additional fees for their services.

(2) Transaction Reporting Fees. For each transaction in corporate bonds that is reportable to NASD pursuant to the Rule 6200 Series, the following

charges shall be assessed against the member responsible for reporting the transaction:

(A) Trade Reporting Fee

[(i) For the period commencing July 1, 2002 and ending December 31, 2002, a member shall be charged a Trade Reporting Fee based upon a sliding scale ranging from \$0.50 to \$2.50 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.50 fee per trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.0025 multiplied by the number of bonds traded per trade; and trades of \$1,000,000 par value or more will be charged a fee of \$2.50 per trade.]

[(ii) For the period commencing January 1, 2003 and ending January 31, 2004, a]A member shall be charged a Trade Reporting Fee based upon a sliding scale ranging from \$0.475 to \$2.375 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.475 fee per trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.002375 multiplied by the number of bonds traded per trade; and trades of \$1,000,000 par value or more will be charged a fee of \$2.375 per trade.

(B) Cancel or Correct Trade Fee

[For the period commencing July 1, 2002 and ending December 31, 2002, 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. For the period commencing January 1, 2003 and ending January 31, 2004, a]A member shall be charged a Cancel or Correct Trade Fee of \$1.50 per canceled or corrected transaction.

(C) “As of” Trade Late Fee

[For the period commencing July 1, 2002 and ending December 31, 2002, a]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. For the period commencing January 1, 2003 and ending January 31, 2004, a member shall be charged an “As of” Trade Late Fee of \$3.00 per canceled or corrected transaction.]

[(D) Browse and Query Fee]

Members may review their own previously reported transaction data through a Browse and Query function. A member shall be charged \$0.05 for each returned page of the query beyond the first page.]

(3) Market Data Fees

Professionals and non-professionals may subscribe to receive R[real-T[time and Delayed-Time] TRACE data disseminated by NASD in one or more of the following ways for the charges specified. Members, vendors and other redistributors shall be required to execute appropriate agreements with NASD.

(A) Professional Fees. Professionals may subscribe for the following:

(i) Bond Trade Dissemination Service (“BTDS”) Professional Real-Time Data Display Fee of \$60 per month, per terminal charge for each interrogation or display device receiving R[real-T[time] TRACE transaction data. [Notwithstanding the above sentence, following the effective date of increased bond data dissemination as approved by the SEC on January 31, 2003^[7], NASD shall announce a period of one calendar month during which NASD shall waive the \$60 per terminal, per month charge.]

(ii) BTDS Professional Delayed-Time Data Display Fee of \$15 per month, per terminal charge for each interrogation or display device receiving Delayed-Time TRACE transaction data; provided, that subscribers to the BTDS Professional Real-Time Data Display Fee described above shall not be charged this additional fee. Subject to the execution of appropriate agreements with NASD, certain summary market information of Delayed-Time TRACE transaction data may be published or distributed by newspapers, press associations, newsletters, or similar media sources without charge.

(iii) BTDS Internal Usage Authorization Fee of \$500 per month, per application/service [charge] for internal dissemination of R[r]eal-T[t]ime and/or Delayed-Time TRACE transaction data used in one or more of the following ways in a single application/service: internal operational and processing systems, internal monitoring and surveillance systems, internal price validation, internal portfolio valuation services, internal analytical programs leading to purchase/sale or other trading decisions, and other related activities.⁸₂.

(iv) BTDS External Usage Authorization Fee of \$1,000 per month, per application/service [charge] for dissemination of R[r]eal-T[t]ime and/or Delayed-Time TRACE transaction data used in one or more of the following ways in a single application/service: repackaging of market data

for delivery and dissemination outside the organization, such as indices or other derivative products.^[9]³

(B) Non-Professional Fees

The charge to be paid by a non-professional for each terminal receiving all or any portion of R[r]eal-T[t]ime TRACE transaction data disseminated through TRACE shall be \$1.00 per month, per terminal.

(C) Definitions

(i) “Delayed-Time” as used in Rule 7010(k)(3) shall mean that period of time starting four hours after the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending at 11:59:59 p.m. Eastern Time that calendar day.

(ii) “Non-Professional”- A non-professional subscriber must provide certain information to NASD and shall receive TRACE market data primarily for his or her personal, non-commercial use. As used in Rule 7010(k)(3) [A]a “non-professional” is a natural person who is neither:

(a) registered nor qualified in any capacity with the Commission, the Commodity Futures Trading Commission, any state securities agency, any securities exchange or association, or any commodities or futures contract market or association, or an employee of the above who uses such information primarily for business-related activities; [or]

- (b) engaged as an “investment adviser” as that term is defined in Section 202(a)(11) of the Investment Advisers Act of 1940 (whether or not registered or qualified under that Act), or an employee of the above who uses such information primarily for business-related activities;
- (c) employed by a bank, insurance company or other organization exempt from registration under federal or state securities laws to perform functions that would require registration or qualification if such functions were performed for an organization not so exempt; or
- (d) engaged in, or has the intention to engage in, any redistribution of all or any portion of the information disseminated through TRACE.

(iii) “Real-Time” as used in Rule 7010(k)(3) shall mean that period of time starting from the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending no more than four hours thereafter.

(D) Other Requests for Data

NASD may impose and collect charges for data NASD supplied upon request, where there is no provision elsewhere in this Rule 7010(k) for charges for such service or sale.

[6]¹ The charges that may be imposed by third parties, such as CTCI line providers, are not

included in these fees.

- [7] [On January 31, 2003, the SEC approved amendments to NASD Rule 6250 of the TRACE rules that will allow NASD to begin disseminating transaction information on more than 4,000 qualifying Investment Grade corporate debt securities. See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 FR 6233 (February 6, 2003) (File No. SR-NASD-2002-174).]
- [8]2 Under this service, R[real-T]ime and/or Delayed-Time TRACE transaction data may not be used in any interrogation display devices, any systems that permit end users to determine individual transaction pricing[in real-time], or disseminated to any external source.
- [9]3 Under this service, R[real-T]ime and/or Delayed-Time TRACE transaction data may not be used in any interrogation display devices or any systems that permit end users to determine individual transaction pricing[in real-time].

* * * * *

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

(a) Purpose

NASD is proposing the rule change to establish a permanent fee structure for the TRACE system. TRACE became effective on July 1, 2002. At such time, the Commission approved the original fee structure for TRACE on a pilot basis. Since then, NASD staff has been committed to reassessing the TRACE fee structure based on actual information collected such as the number of participants, debt securities transaction

volume, and subscribers for transaction data. During the last fourteen months, in response to industry concerns and emerging trends, NASD staff has revised the TRACE fee structure five times. Following more than a year of reassessment of the originally approved TRACE fees, NASD believes the fees are reasonable and necessary to ensure recovery of developmental costs of the TRACE system, fund ongoing operational costs, and fund the regulatory activities necessary for surveillance of the market. NASD believes the proposed rule change will equitably distribute the costs to participants of the TRACE system. While NASD is seeking permanent approval of the TRACE fees, NASD remains committed to periodically reassessing the appropriateness of TRACE fees.

Background

In 1998, former U. S. Securities and Exchange Commission (“SEC”) Chairman Arthur Levitt requested NASD to provide increased transparency in, and better surveillance of, the corporate debt market by (i) requiring that NASD members report corporate bond transactions to NASD; (ii) developing a system or systems to surveill the corporate debt market, including an audit trail of reported transactions; and (iii) delivering price and other information to large and small investors and other debt market participants. At that time, NASD began to develop TRACE and make it operational.

On June 28, 2002, the SEC 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, 2002.³ As part of that rule filing (Amendment No. 3 to SR-

³ 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).

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.

On November 15, 2002 NASD filed, for immediate effectiveness, a rule filing to reduce certain TRACE fees for the 4th quarter of 2002.⁴ On December 16, 2002, NASD filed for immediate effectiveness, a rule filing to extend the pilot program for TRACE fees to February 28, 2003 and modify certain fees effective January 1, 2003.⁵ On February 27, 2003, NASD filed, for immediate effectiveness, a rule filing to extend the pilot program for TRACE fees to June 30, 2003.⁶ On June 17, 2003 NASD filed, for immediate effectiveness, a rule filing to extend the pilot for TRACE fees to January 31, 2004.⁷

Operational Information

Since TRACE reporting began on July 1, 2002, approximately 1,800 NASD member firms have registered for TRACE reporting. Currently, approximately 28,000 corporate debt issues are subject to TRACE reporting requirements. Dissemination, however, currently occurs for approximately 4,700 of these corporate debt issues as TRACE transaction data is being disseminated in phases.⁸ In January 2001, the

⁴ See Securities Exchange Act Release No. 46893 (November 22, 2002), 67 FR 72008 (December 3, 2002) (File No. SR-NASD-2002-167).

⁵ See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002) (File No. SR-NASD-2002-176).

⁶ See Securities Exchange Act Release No. 47444 (March 4, 2003), 68 FR 11602 (March 11, 2003) (File No. SR-NASD-2003-25).

⁷ See Securities Exchange Act Release No. 48110 (July 7, 2003), 68 FR 40315 (June 30, 2003) (File No. SR-NASD-2003-97).

⁸ NASD continues to review proposals to increase the number of TRACE-eligible securities that will be subject to dissemination.

Commission initially approved “Phase I” dissemination of TRACE transaction data.⁹ On the first day of “Phase I” dissemination (July 1, 2002), approximately 550 corporate bonds became subject to dissemination.¹⁰ In January 2003, the Commission approved “Phase II” dissemination of TRACE transaction data.¹¹ On the first day of “Phase II” dissemination (March 3, 2003), an additional approximately 3, 800 corporate bonds became subject to dissemination, and on April 14, 2003, an additional approximately 120 triple-B-rated corporate bonds were also disseminated as part of “Phase II.”¹² In addition, in June 2003, reporting time for transactions in TRACE-eligible securities was reduced from 75 minutes

⁹ Specifically, under Rule 6250, transactions in two types of securities were subject to the TRACE dissemination requirements that took effect on July 1, 2002: (1) those transactions in a TRACE-eligible security having an initial issuance size of \$1 billion or greater that is Investment Grade at the time of receipt of the transaction report as set forth in Rule 6250(a)(1); and (2) those transactions in 50 TRACE-eligible debt securities that are actively traded, rated Non-Investment Grade, and meet other criteria set forth in Rule 6250(a)(2). See Securities Exchange Act Release No. 46144 (June 28, 2002), 67 FR 44907 (July 5, 2002) (File No. SR-NASD-2002-46).

¹⁰ This group of bonds includes what was previously referred to as the FIPs 50 and which are now referred to as the TRACE 50. The list of 50 bonds is updated periodically based on criteria identified in Rule 6250(a)(2).

¹¹ In “Phase II” NASD began to disseminate transaction information on two additional categories of securities. On March 3, 2002, NASD began to disseminate transaction information on any TRACE-eligible security that is Investment Grade; is rated by Moody's Investors Service, Inc. as "A3" or higher, and by Standard & Poor's, a division of McGraw Hill Co., Inc., as "A-" or higher; 5 and has an original issue size of \$100 million or greater. In addition, a security that is required to be disseminated under the criteria above, on or after the effective date of this provision, will continue to be subject to dissemination unless the security is downgraded below "Baa3/BBB. A specified group of TRACE-eligible securities rated Baa/BBB, at the time of designation, were also approved for dissemination by the SEC. Originally, 90 securities were designated. See Securities Exchange Act Release No. 47302 (January 31, 2003), 68 FR 6233 (February 6, 2003) (File No. SR-NASD-2002-174). However, in March 2003, NASD proposed to increase the number of “triple-B-rated” securities to approximately 120. See Securities Exchange Act Release No. 47566 (March 25, 2003), 68 FR 15490 (March 31, 2003) (File No. SR-NASD-2003-41). The 120 “triple-B-rated” securities were designated after the SEC approved SR-NASD-2003-41, and transaction information on the designated securities began to be disseminated on April 14, 2003.

¹² See Securities Exchange Act Release No. 47566 (March 25, 2003), 68 FR 15490 (March 31, 2003) (File No. SR-NASD-2003-41).

to 45 minutes effective as of October 1, 2003.¹³ In July 2003, the disseminated list of high-yield bonds referred to as the “TRACE 50” was updated.¹⁴

Since the launch of TRACE, NASD has enhanced the system with two major and five minor software releases in response to user needs, conducted routine monitoring of daily reported transaction data for accuracy, and undertaken regulatory activities to surveil the corporate debt market. TRACE incurs ongoing operating costs associated with shared NASD infrastructure and resources as well as direct charges from outsourcing TRACE system support and development. Additionally, TRACE is supported by a dedicated team of NASD staff. For the first twelve months of operation (period ending June 30, 2003), these expenses have totaled approximately \$12.4 million including partial recovery of the original investment made in the development of TRACE.¹⁵

As detailed in this filing, revenues are derived from a combination of System Fees to access TRACE, Transaction Reporting Fees for trade reporting, and Market Data Fees for access and display of aggregated TRACE data. For the first twelve months of operation (period ending June 30, 2003), TRACE generated revenues of approximately \$12.4 million reflecting approximately \$2.0 million, \$8.9 million, and \$1.5 million for System Fees, Transaction Reporting Fees, and Market Data Fees, respectively.

The proposed fees are also divided into the same three general categories: (1) System fees paid by member firms based on the technology method chosen by the member

¹³ See Securities Exchange Act Release No. 48056 (June 18, 2003), 68 FR 37886 (June 25, 2003) (File No. SR-NASD-2003-78).

¹⁴ The list of TRACE 50 bonds is updated periodically based on criteria identified in Rule 6250(a)(2).

¹⁵ Under this approach the original investment costs are recovered over a 48-month period.

to report corporate bond transactions; (2) transaction reporting fees paid by members to file trade reports and cancel or correct trade reports; and (3) market data fees paid by members and non-members that use or distribute the data collected through the TRACE system and disseminated by NASD. NASD is hereby seeking permanent approval of the fees relating to the TRACE system. However, NASD remains committed to reviewing and reassessing TRACE fees over time.

System Fees

A member may report TRACE transaction data to NASD by one of three approved methods: (1) web browser access; (2) direct computer-to-computer interface (“CTCI”); or (3) indirectly through third-parties, such as vendors, service bureaus, clearing firms, or the National Securities Clearing Corporation. The member determines the reporting method they would like to use based on such factors as volume, size, and cost.

Web Browser Access Fees

In response to requests from the industry, in January 2003, NASD introduced a modified web browser and adjusted the fees accordingly.¹⁶ The modified web browser separated reporting capabilities from query features that allow access to TRACE transaction data. NASD began offering two web browser service levels on January 1, 2003: (1) Level I Trade Report Only Web Browser access permits a member to report TRACE transaction data to NASD over the internet, but does not allow access to real-time TRACE data, and (2) Level II Full Service Web Browser access permits reporting of

TRACE transaction data to NASD over the internet and allows access to real-time transaction data through a query function. The original charge for Level I service is \$25 per month, per user ID, and the charge for Level II service is \$85 per month, per user ID.

NASD is proposing to reduce the Level I charge from \$25 per month, per user ID, to \$20 per month, per user ID, and to reduce the Level II charge from \$85 per month, per user ID, to \$80 per month, per user ID. The modified web browser allows participants to satisfy their reporting obligations to NASD at a base level cost of \$20 per month, per user ID. Participants that wish to have access to additional services such as real-time data query, pay \$80 per month, per user ID. In this way, NASD believes that cost of delivering this service will be more equitably distributed to members that directly use this additional technology for their business.

In March 2003, NASD submitted a rule filing to the Commission proposing to (1) temporarily reduce the Level I Full Service Web Browser Access Fee, and (2) temporarily waive the BTDS Professional Real-Time Data Display Fee for a one-month period to be announced by NASD. NASD originally sought these temporary reductions to provide subscribers a “trial month” to explore the services. However, third-party vendors have raised concerns with NASD staff that the imposition of one “trial month” will be difficult for them to administer and may not have the desired effect of bringing on new TRACE data subscribers. Therefore, NASD is proposing to eliminate these temporary reductions.

¹⁶ See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002) (File No. SR-NASD-2002-176).

CTCI Fees and Third-Party Vendor Fees

The charge for CTCI service and for reporting data through third-party vendors will remain the same - \$25 per month. NASD had originally provided participants the option of reporting TRACE data to NASD through a secure, private data network. However, no subscribers registered for this service and in a rule filing submitted to the SEC on December 16, 2002, NASD proposed to eliminate this service and the corresponding fee as of January 1, 2003. NASD proposes to make this change permanent.

NASD believes that the TRACE system fees are reasonable and non-discriminatory because members may select the technology link that best suits their particular needs. The Web Browser Access Fees have been significantly modified from the original level established in July 2002.¹⁷ Firms that have a smaller volume of TRACE transactions now have a cost-effective reporting option (e.g., Level I Trade Report Web Browser). Larger volume firms have generally been reporting TRACE transaction data either through a CTCI line at a charge of \$25 per month, or through third-parties at a charge of \$25 per month.

¹⁷

In the original fee approval order, the Web Browser Access Fee for each registered participant was: \$85 per month, per user ID, for the first user ID; \$75 per month for the second through ninth user ID; and \$70 per month for the second through tenth or more user ID, if the participant registers ten or more user IDs. For the fourth quarter of 2002, the Web Browser Access Fee was reduced to \$25 per month, per user ID for participants that reported less than 25 transactions during the months of October, November, and December 2002.

Transaction Reporting Fees

Trade Reporting Fees

Following the start of operations of TRACE, NASD staff has been collecting data on trade reporting fees incurred by participants. The revenues generated by this fee were higher than originally forecasted. As a result, as of January 1, 2003, NASD reduced trade reporting fees by 5% from the original fee levels.¹⁸ NASD seeks permanent approval of the reduced trade reporting fees. Trade Reporting Fees will continue to be on a sliding scale, based upon the size of the transaction reported, in an effort to distribute the fees more equitably between retail oriented firms and institutionally oriented firms.¹⁹ The range for trade reporting fees will be from \$0.475 to \$2.375 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value will be charged a \$0.475 fee per trade; trades between \$201,000 par value and \$999,999 par value will be charged a fee of \$0.002375 multiplied by the number of bonds traded, and trades of \$1,000,000 par value or more will be charged a fee of \$2.375 per trade.

Corrective Transaction Fees

NASD proposes to set the permanent Cancel or Correct Fee at \$1.50 per corrected trade and the “As of” Trade Late reporting fee at \$3.00 per late trade. Cancel,

¹⁸ The original Trade Reporting Fees were also based on a sliding scale that ranges from \$0.50 to \$2.50 per transaction based on the size of the reported transaction. Trades up to and including \$200,000 par value are charged a \$0.50 fee per trade; trades between \$201,000 par value and \$999,999 par value are charged a fee of \$0.0025 multiplied by the number of bonds traded; and trades of \$1,000,000 par value or more are charged a fee of \$2.50 per trade.

¹⁹ In approving the original TRACE fees on a pilot basis, the Commission stated that “[t]he Commission believes that this sliding scale structure promotes an equitable distribution of the relevant fees while reducing the possibility of unfair discrimination between customers, issuers, brokers, or dealers.” See SEC Approval Order File No. SR-NASD-2002-63, Securities Exchange Act Release No. 46145 (June 28, 2002).

correct, and “As of” transactions are used by participants to modify original trade entries. While a certain level of corrective transactions will always be necessary, NASD staff 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. Further, continued high levels of corrective transactions will increase NASD’s technology costs.

The original charge for the Cancel or Correct Fee and the “As of” Late Fee was \$3.00 for each such reported transaction. However, in the original fee proposal, NASD delayed the effectiveness of the Cancel or Correct Fee and the “As of” Late Fee to October 1, 2002. Based on NASD staff review of the data collected on such fees after the first three months of TRACE operation, on November 15, 2002, NASD submitted a proposed rule change to the SEC to phase in the implementation of the two fees during the last quarter of 2002 to allow participants greater time to adjust to the new system and focus on methods to reduce the likelihood of incurring such fees.²⁰ For the month of October 2002, the Cancel or Correct Fee and the “As of” Late Fee charge assessed to each participant were reduced from \$3.00 per trade to \$1.50 per trade (a 50% discount), and for the month of November 2002, the Cancel or Correct Fee and the “As of” Late Fee were reduced from \$3.00 per trade to \$2.25 per trade (a 25% discount). On December 16, 2002, NASD submitted a rule filing to reduce the Cancel or Correct Fee from \$3.00 to \$1.50 effective January 1, 2003.

NASD staff has been working with the industry to determine the causes of erroneous transactions as part of a goal of reducing the number of corrective transactions

reported to TRACE. NASD staff believes that over time the number of corrective transactions submitted to the system will decline. However, NASD believes that fees for corrective transactions are necessary to discourage erroneous reporting and to improve the integrity of disseminated data. Therefore, NASD is proposing that the SEC permanently approve the current corrective transaction fees.

Browse and Query Fees

NASD is proposing to eliminate the Browse and Query Fee of \$0.05 per page after the first page. This feature allows firms to review previously reported transaction data. Firms will continue to have access to this service, however, there will no longer be a fee associated with such service.

Market Data Fees

The current market data fees are as follows: (1) BTDS Professional Real-Time Data Display Fee - \$60 per month, per terminal; (2) BTDS Internal Usage Authorization Fee - \$500 per month, per application/service; (3) BTDS External Usage Authorization Fee - \$1,000 per month, per application/service; and (4) BTDS Non-Professional Real-Time Fee - \$1 per month, per terminal.

NASD is proposing to define the terms “Real-Time” and “Delayed-Time” as they relate to market data fees for TRACE transaction data. “Real-Time” as used in Rule 7010(k)(3) shall mean that period of time starting from the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending four hours thereafter. “Delayed-Time” as used in Rule 7010(k)(3) shall mean that period of time starting four

hours after the time of dissemination by NASD of transaction data on a TRACE-eligible security, and ending at 11:59:59 p.m. Eastern Time that calendar day.

In addition, NASD is proposing to establish a charge to professionals for the use of Delayed-Time TRACE transaction data. Discussions with members of the bond industry indicate that there is increasing demand for Delayed-Time TRACE transaction data by professionals. Market professionals have indicated to NASD staff that, as a result of relatively low individual bond trading activity levels on any given day, Delayed-Time transaction data is useful to see overall patterns and trends, especially in pricing. Because of the time lag between trades in less active issues often exceeds four hours, the value of the last sale information on a four hour Delayed-Time basis often equals that of the real-time information. NASD staff believes that professionals who use this data in the course of their business or commercial activities should pay for the use of the data. Consequently, NASD staff believes that a charge for professionals for Delayed-Time data is appropriate.

The fee for the BTDS Professional Delayed-Time Data Display would be \$15 per month, per terminal, for each device receiving Delayed-Time TRACE transaction data.²¹ Professionals subscribing for the BTDS Professional Real-Time Data Display Fee of \$60 per month, per terminal, to receive Real-Time TRACE transaction data would not pay this charge for Delayed-Time data in addition to the \$60 fee for Real-Time data. Subject to the execution of appropriate agreements with NASD, certain summary market information of Delayed-Time TRACE transaction data may be published or distributed by newspapers,

²¹ Transaction data for TRACE-eligible securities disseminated by NASD after this time frame will be provided free of charge.

press associations, newsletters, or similar media sources (including in some cases members) without charge. NASD is also proposing to clarify that charges for BTDS Internal Usage and BTDS External Usage apply to Real-Time and/or Delayed-Time TRACE transaction data.

In addition, NASD proposes to clarify the definition of “non-professional.” Since the start of TRACE, numerous individuals have questioned whether they qualify as a “non-professional.” To clear up confusion, NASD is proposing to add language to the definition to state that a natural person can qualify as a “non-professional” only if they receive TRACE market data primarily for personal, non-commercial use.

In the original fee proposal, NASD had provided for a daily list fax service that would provide subscribers with daily additions, deletions, and modifications to the list of TRACE-eligible securities. The charge for this service was \$15 per month, per fax number/addressee. One user subscribed for this service and it was no longer cost effective for NASD to continue providing the service. As a result, NASD proposed in a rule filing submitted to the SEC on December 16, 2002 to eliminate this service and the corresponding fee as of January 1, 2003.²² NASD proposes to make this change permanent.

NASD believes the market data fees are reasonable and non-discriminatory. The fees are charged only to market professionals that wish to subscribe for these optional

²² See Securities Exchange Act Release No. 47056 (December 19, 2002), 67 FR 79205 (December 27, 2002)(File No. SR-NASD-2002-176).

services. NASD believes that this use-based approach appropriately aligns costs with member usage and is consistent with equitable distribution of fees.

Other Requests for Data

From time to time, members, vendors, and other persons request certain ad hoc services or uses of the TRACE system and transaction data that are not otherwise covered by Rule 7010(k). NASD believes that providing such services to the industry, academia, or others is useful and proposes to collect charges when fulfilling these requests. Charges would be commensurate with the higher of a) NASD's associated costs or b) similar products or services available in the marketplace.

Permanent Approval of Fees

NASD is seeking permanent approval of the TRACE fee structure prior to the expiration of the pilot program for TRACE fees that is scheduled to expire on January 31, 2004. NASD believes that the proposed fee structure for TRACE is reasonable and non-discriminatory. In its original approval of the TRACE fees pilot, the Commission stated that it believes that the fees allow users great flexibility in how they will interact with the system, and are scaled according to objective criteria applied across-the-board to all categories of users.²³

NASD believes the fee structure is equitable and the charges are based on actual usage of the system. For example, trade reporting fees are based on a sliding scale that varies depending on the size of the transaction reported, with fees ranging from \$0.475 (for the smallest trades) to \$2.375 (for the largest trades). System fees allow participants

²³ See SEC Approval Order File No. SR-NASD-2002-63, Securities Exchange Act Release No. 46145 (June 28, 2002).

to select the most cost-effective reporting method and web browser fees are based on usage (users of the real-time transaction query feature pay more for the additional service). Similarly, market data fees are lower for users who limit their use of the TRACE transaction data to internal distribution, and relatively higher for users who use or distribute the data externally.

For these reasons, NASD believes the fees set forth above are reasonably related to the costs of developing the facility and to meeting the estimated operating expenses of the TRACE system. The fees are also designed to fund the regulatory activities necessary to surveil the market. In addition, NASD staff believes that it has responded promptly to the concerns of members by reducing TRACE fees.

As part of the initiative by the Commission to create price transparency in the corporate bond market, the NASD has worked diligently to develop the TRACE system. NASD staff continues to work closely with the Bond Transaction Reporting Committee, which is jointly staffed by members designated by NASD and The Bond Market Association. In addition, NASD staff has met formally and informally with members of the industry and listened to their questions and concerns. Overall, NASD believes the TRACE fee structure is reasonable and non-discriminatory, and that the proposed fees are necessary to achieve a practical, market-driven system for processing and disseminating reliable and uniform corporate bond data. NASD is committed to taking a proactive role in supervising the corporate bond market and promoting investor confidence in the fairness of the corporate bond market generally.

NASD remains committed to reviewing and reassessing the appropriateness of TRACE fees over time to ensure that the fees are reasonable and equitable for participants in the TRACE system.

Based on the above, the NASD believes the proposed rule change is consistent with the provisions of Section 15A(b)(5)²⁴ of the Act in that the proposal provides for the equitable allocation of reasonable dues, fees, and other charges among members and other persons using any facility or system which the association operates or controls.

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, 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 Section 15A(b)(5) of the Act, 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. NASD is seeking permanent approval of the TRACE fee structure and believes that the proposed fee structure is reasonable.

²⁴ 15 U.S.C. 78o-3(b)(5).

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.

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, 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 Section 15A(b)(5) of the Act, 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. NASD is seeking permanent approval of the TRACE fee structure and believes that the proposed fee structure is reasonable.

(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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

A. by order approve such proposed rule change, or

B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. 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 NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland
Deputy Secretary