

of a private contract between the NASD and the owner of an automated inter-dealer quotation system would more adequately address the needs of both the NASD and the system. In addition, Pink Sheets sought assurances that quotation data provided to the NASD pursuant to the proposed rule would not be redistributed in competition with Pink Sheets.

NASD Regulation has noted that it cannot rely on a contractual arrangement with the Pink Sheets. Because the NASD's jurisdiction extends only to its members and not to Pink Sheets and other inter-dealer quotation services, NASD Regulation believed that it could not impose a requirement on Pink Sheets to provide quotation data, and, therefore, Pink Sheets at any time could refuse to provide the quotation data. NASD Regulation stated that, although it could pursue legal action against the system operator for breach of such contract, it would be at risk of not having quotation data in the interim and thus would be unable to surveil effectively and monitor for compliance with applicable rules and regulations. Finally, NASD Regulation noted that it requires access to the quotation data for regulatory purposes and intends to use that data only for this purpose.<sup>18</sup> Further, in its letter dated June 14, 2001, NASD Regulation specifically represented that quotation data submitted to the NASD or NASD Regulation under the proposed rule will not be provided to The Nasdaq Stock Market by the NASD or NASD Regulation.<sup>19</sup> Also, in Amendment No. 3, the NASD represented that to the extent the member's Reporting Agent calculates an inside bid and/or offer and submits that inside bid and/or offer to the NASD, the NASD will not use this inside bid and/or offer for any commercial purposes.<sup>20</sup>

#### B. Responsibility for Compliance

In the proposed rule change, the NASD stated that an NASD member would be fully responsible for compliance with the proposed rule whether or not the member used a Reporting Agent to provide quotation information. Pink Sheets argued that requiring NASD members to bear the responsibility for ascertaining whether the NASD is receiving quotation data would impose an undue burden on NASD members. Pink Sheets therefore suggested that the proposed rule be amended to require the NASD to notify

its members or their Reporting Agents if the NASD knows or has reason to believe that the NASD is not receiving quotation data.

NASD Regulation responded that it believes member firms must be responsible for compliance with the proposed rule and must put procedures in place to ensure proper reporting of quotation information. NASD Regulation stated, however, that it would be willing, upon request, to confirm whether it is receiving quotation information submitted pursuant to the proposed rule.

#### C. Withdrawal of Quotations

As originally proposed, non-compliance with the proposed rule would require a member to immediately withdraw its priced quotations and unpriced indications of interest. Pink Sheets expressed concern that this might require NASD members to immediately withdraw their quotations where non-compliance is the result of data systems problems.

NASD Regulation responded that it recognizes members or their Reporting Agents may experience systems problems that temporarily restrict their ability to record and report quotation information. Therefore, NASD Regulation stated that if a member or its Reporting Agent were unable to record or report quotation information due to a systems problem, the member would not be required to withdraw its quotations or unpriced indications of interest, as long as the problem did not extend beyond one trading day. NASD Regulation further noted that if the systems problem extended beyond one trading day, the proposed rule would require that the member withdraw its quotations or unpriced indications of interest, if the member is unable to use an alternative means to comply with the proposed rule. Reflecting this approach, the NASD amended the proposed rule so that it no longer requires quotations to be withdrawn immediately.<sup>21</sup>

Pink Sheets also expressed concern that market makers required to withdraw their quotations and unpriced indications of interest might lose their "piggyback" status under Rule 15c2-11 of the Act.<sup>22</sup> Pink Sheets asserted that in

order to avoid this possible result, the proposed rule should be amended so that, in the case of non-compliance, members would only be required to withdraw their quotations, not their unpriced indications of interest. NASD Regulation responded that if quotation information, including unpriced indications of interest, is not properly recorded and reported, the NASD could not ensure that its members are in compliance with applicable rules.

#### D. Data Standards

The proposed rule would require members to record and report quotation data "in such form as is prescribed by the Association from time to time." The proposed rule, however, specifies the items of information the quotation activity must contain. Pink Sheets argued that no quotation system should be held to "such a subjective standard." NASD Regulation responded that, under the proposed rule, the NASD would, in a Notice to Members, prescribe the form in which it would require data to be transmitted to the Association. NASD Regulation stated that its staff has met with a representative of Pink Sheets to discuss data transmission alternatives. Further, NASD Regulation stated that if it were to now stipulate the use of a specific transmission method, the NASD would not have the ability, should it be necessary, "to address varying systems transmissions capabilities."

#### E. Inter-Dealer Quotation Systems Covered by the Rule

As amended, proposed NASD Rule 6630 would not require the recording and reporting of quotations that are displayed on an inter-dealer quotation system that is either: (1) Operated by a registered securities association or national securities exchange; or (2) operated by an NASD member. In addition, since the rule applies only to OTC equity securities, it would not apply to electronic bond quotation services. Pink Sheets objected to the proposed rule's original exclusion of systems qualified pursuant to section 17B of the Act, which, by definition, are operated by either a national securities association or a national securities exchange.<sup>23</sup> Pink Sheets expressed concern that there is no rule that requires members to remove their

Once the security is quoted regularly for 30 days, other broker-dealers can "piggyback" off of those quotations, *i.e.*, submit quotations without reviewing information about the issuer. 17 CFR 24.15c2-11(f)(3).

<sup>23</sup> Amendment No. 2, *supra* note 7, revised the text of this exclusion to expressly exclude quotations displayed on an inter-dealer quotation system operated by a registered securities association or national securities exchange.

<sup>18</sup> NASD Response to Comments and Amendment No. 1, *supra* note 5.

<sup>19</sup> NASD Letter, *supra* note 6.

<sup>20</sup> Amendment No. 3, *supra* note 8.

<sup>21</sup> If a systems problem extends beyond one trading day, causing quotation data to not be recorded or reported for a particular member, that member would then be required to withdraw from the quotation system. See NASD Response to Comments and Amendment No. 1, *supra* note 5.

<sup>22</sup> Rule 15c2-11 requires a broker-dealer to review current information about an issuer before it publishes a quotation for the issuer's security in the non-Nasdaq OTC markets. Because of the rule's "piggyback" provision, generally only the first broker-dealer is required to review this information.