

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Part 240

[Release No. 34-47849; File No. S7-11-03]

RIN 3235-A186

### Request for Comment on Nasdaq Petition Relating to the Regulation of Nasdaq-Listed Securities

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Concept release; request for comment.

**SUMMARY:** The Securities and Exchange Commission ("Commission") seeks comment on a petition submitted by the Nasdaq Stock Market, Inc. ("Nasdaq") concerning the regulation of Nasdaq-listed securities. Specifically, Nasdaq requests that the Commission amend the rules of all markets that trade Nasdaq-listed securities to establish uniform trading rules, and to ensure equal surveillance and enforcement of those rules; order that the exchanges' costs of regulation, including costs associated with proper data collection, surveillance, and enforcement, be aggregated and deducted from the market data revenue collected pursuant to the Nasdaq Unlisted Trading Privileges Plan ("UTP Plan"); and prohibit the launch or continuation of Nasdaq trading by any market that fails to protect investors as required under the Securities Exchange Act of 1934 ("Act"). In addition, the Commission requests comment on whether the same actions would be appropriate for the regulation and trading of exchange-listed securities.

**DATES:** Comments must be received on or before June 19, 2003.

**ADDRESSES:** To help us process and review your comments more efficiently, comments should be sent by one of the two methods specified below. Persons wishing to submit written comments should send three copies to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Comments also may be submitted electronically at the following E-mail address: [rule-comments@sec.gov](mailto:rule-comments@sec.gov). All comment letters should refer to File No. S7-11-03. Comments submitted by E-mail should include this file number in the subject line. Comment letters received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549-1001. Electronically submitted comment letters will be posted on the

Commission's Internet Web site (<http://www.sec.gov>).<sup>1</sup>

#### FOR FURTHER INFORMATION CONTACT:

Terri L. Evans at (202) 942-4162 or Ian K. Patel at (202) 942-0089 in the Division of Market Regulation, Commission, 450 Fifth Street, NW., Washington, DC 20549-1001.

#### SUPPLEMENTARY INFORMATION:

##### I. Introduction

On April 14, 2003, the Commission received a petition from Nasdaq requesting that the Commission take certain actions ("Nasdaq Petition") to respond to the greater fragmentation of trading in Nasdaq-listed securities across markets. The Commission is publishing Nasdaq's Petition to expedite and facilitate dialogue among all market participants on the issues raised by Nasdaq. The Commission is not endorsing Nasdaq's characterization of the regulation of Nasdaq-listed securities or its proposed solutions. Rather, the Commission is seeking comment on Nasdaq's Petition and, more generally, the issues raised by the Nasdaq Petition.

##### II. Background

###### A. Duties of a Self-Regulatory Organization

In fashioning the Act, Congress chose to develop a unique pattern of regulation combining both industry and government responsibility.<sup>2</sup> This pattern calls upon the exchanges and the National Association of Securities Dealers, Inc. ("NASD") to exercise delegated governmental power to enforce at their own initiative compliance by members of the securities industry with both the legal requirements laid down in the Act and ethical standards which go beyond those requirements.<sup>3</sup> As a result, the regulatory roles that self-regulatory organizations ("SROs") play are a vital element in the regulation of the securities industry. An SRO is required to carry out the purposes of the Act, as well as enforce compliance by its members, and persons associated with

its members, with the federal securities laws and the SRO's rules.<sup>4</sup>

An SRO is required to have rules designed, among other things, to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and to refrain from imposing any unnecessary or inappropriate burdens on competition.<sup>5</sup> For example, an SRO must maintain procedures to surveil against rule violations, including insider trading and market manipulation. While different market structures may imply different procedures for accomplishing this task, SROs are required to expend sufficient resources, in terms of both staff and technology, to support their surveillance functions. This includes having officers with expertise in monitoring for compliance with federal securities laws and SRO rules, and an understanding of the role of a registered exchange or association as an SRO. An SRO must deploy adequate examination and surveillance systems and maintain an audit trail of the transactions in its system. And SROs must have adequate measures in place to maintain listing and maintenance standards. SROs' regulatory programs, including those related to the trading of Nasdaq securities, are periodically inspected by the Commission.

An SRO also is required to enforce compliance with applicable laws and rules, and discipline members for violations relating to transactions executed in its market.<sup>6</sup> This responsibility includes the establishment of a disciplinary process including appropriate sanctions for violations of the rules and a fair procedure for administering the

<sup>4</sup> See section 6(b)(1) of the Act, 15 U.S.C. 78f(b)(1) and section 15A(b)(2), 15 U.S.C. 78o-3(b)(2).

<sup>5</sup> See section 6(b)(5) of the Act, 15 U.S.C. 78f(b)(5); section 6(b)(8) of the Act, 15 U.S.C. 78f(b)(8); section 15A(b)(6), 15 U.S.C. 78o-3(b)(6); and section 15A(b)(9), 15 U.S.C. 78o-3(b)(9). For example, an SRO must also have written listing and maintenance standards, as well as an adequate regulatory staff to apply those standards. See section 12(d) of the Act, 15 U.S.C. 78l(d); Rule 12d2-2, 17 CFR 240.12d2-2 (requiring national securities exchanges to file an application with the Commission to strike a security from listing and registration). In addition, an SRO must have rules that ensure that no member's order is unfairly disadvantaged and all members are treated fairly. An SRO also is expected to have rules establishing procedures for the clearance and settlement of trades effected on the exchange. See Regulation of Exchanges and Alternative Trading Systems, Exchange Act Release No. 40760 (December 8, 1998), 63 FR 70844 (December 22, 1998), at section IVB(1).

<sup>6</sup> See 19(g)(1) of the Act, 15 U.S.C. 78s(g)(1); See also Regulation of Exchanges and Alternative Trading Systems, Exchange Act Release No. 40760 (December 8, 1998), 63 FR 70844 (December 22, 1998), at section IVB(1).

<sup>1</sup> Personal identifying information, such as names or e-mail addresses, will not be edited from electronic submission. Submit only information that you wish to make publicly available.

<sup>2</sup> H.R. Doc. No. 123, 94th Cong., 1st Sess. 48 (1975), Legislative History of the Securities Reform Act of 1975.

<sup>3</sup> *Id.* The Commission is charged with supervising the exercise of this regulatory power to assure that it is used effectively to fulfill the responsibilities assigned to the self-regulatory organizations and that it is not used in a manner inimical to the public interest.