

NASD filed a response to the comment letters and simultaneously amended the proposed rule change.⁶ This order approves the proposed rule change as modified as Amendment No. 1. Simultaneously, the Commission provides notice of filing of Amendment No. 2 and grants accelerated approval of Amendment No. 2.

II. Summary of Comments

The Commission received 13 comment letters on the proposed rule change, all in opposition to the proposal.⁷

("NFA") to Jonathan G. Katz, Secretary, Commission ("NFA Letter"); September 19, 2002 letter from Patrice Blanc, Chairman and Chief Executive Officer, Fimat USA, Inc. ("Fimat") to Jonathan G. Katz, Secretary, Commission ("Fimat Letter"); September 20, 2002 letter from Catherine D. Dixon, Assistant Secretary of the Commission, U.S. Commodity Futures Trading Commission ("CFTC") to Jonathan G. Katz, Secretary, Commission ("CFTC Letter"); September 26, 2002 letter from Stuart J. Kaswell, Senior Vice President and General Counsel, Securities Industry Association ("SIA") to Jonathan G. Katz, Secretary, Commission ("SIA Letter"); September 20, 2002 letter from David J. Vitale, President and Chief Executive Officer, Board of Trade of the City of Chicago, Inc., James J. McNulty, President and Chief Executive Officer, Chicago Mercantile Exchange, Inc., and J. Robert Collins, President and Chief Executive Officer, New York Mercantile Exchange, Inc. to Jonathan G. Katz, Secretary, Commission ("Mercantile Letter"); September 23, 2002 letter from Christopher K. Hehmeyer, Co-Chairman, and Carl W. Gilmore, General Counsel, both of Goldenberg, Hehmeyer and Co. ("Goldenberg") to Jonathan G. Katz, Secretary, Commission ("Goldenberg Letter"); September 20, 2002 letter from John M. Damgard, President, Futures Industry Association, Inc. ("FIA") to Jonathan G. Katz, Secretary, Commission ("FIA Letter"); September 23, 2002 letter from Brad W. Corey, Chief Financial Officer, Man Financial Inc. ("Man") to Jonathan G. Katz, Secretary, Commission ("Man Letter"); September 26, 2002 letter from Ronald H. Filler, Senior Vice President, Lehman Brothers, Inc. ("Lehman") to Jonathan G. Katz, Secretary, Commission ("Lehman Letter"); September 20, 2002 letter from Thomas O'Brien, Chief Financial Officer, TransMarket Group, L.L.C. ("TransMarket") to Jonathan G. Katz, Secretary, Commission ("TransMarket Letter").

² November 27, 2002 letter from Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, NASD, to Katherine A. England, Assistant Director, Division, Commission ("NASD Response Letter") and attachments (collectively, "Amendment No. 2"). In Amendment No. 2, the NASD excluded commodities income from Gross Revenue for purposes of the GIA.

⁷ See footnote 5, *supra*. The Commission notes that, in proposing to modify its regulatory pricing structure, the NASD filed the instant proposed rule change in tandem with SR-NASD-2002-98. See Securities Exchange Act Release No. 46416 (August 23, 2002), 67 FR 55901 (August 30, 2002). SR-NASD-2002-98 was effective upon filing with the Commission. 15 U.S.C. 78s(b)(3)(A)(ii), 17 CFR 240.19b-4(f)(2). Because the NASD's proposed changes to its regulatory pricing structure were split between two separate yet related rule filings, some of the commenters expressed opposition to the restructuring, generally, without raising specific concerns about SR-NASD-2002-99. See NYSE Letter; Phlx Letter; and SIA Letter at 1-2 (absence of the effective rate of the NASD's proposed trading

Many commenters objected to the proposal because they believe the proposed fees are not limited to recovery of costs for services performed by the NASD.⁸ For example, commenters expressed disapproval of the NASD's proposed changes to the manner in which it calculates the GIA, stating the new method of calculating the GIA would include revenue from transactions for which there is no regulatory nexus between the transactions and the NASD, including transactions that do not involve securities.⁹ Some commenters disapprove of the proposal because they believe the amount of the GIA will have an inverse relationship to the resources that the NASD must expend on firms. In other words, the new method of calculating the GIA allegedly would result in a greater financial impact on firms for which the NASD plays a smaller regulatory role.¹⁰

Commenters objected to the proposal because they believe the NASD will be charging its members who have dual memberships for regulatory services in relation to transactions in covered securities (as defined in the proposals) that are effected on other markets.¹¹ Additionally, the commenters expressed concern about the precedent the proposal will set. For example, if the NASD is allowed to assess a fee based on its member's futures business, the

activity fee makes it impossible for SIA member firms to determine the impact of all elements of the NASD's proposed pricing structure). No commenters objected to the Personnel Assessment specifically. Some commenters questioned whether the NASD's proposed restructuring as a whole would be revenue neutral. See e.g., NFA Letter at 1 ("NASD claims that its entire proposal would be revenue neutral, but it does not provide any figures to support that claim.").

⁸ See e.g., NYSE Letter; CBOE Letter at 3; NFA Letter at 3-4; Fimat Letter at 1-2; Mercantile Letter at 1; Lehman Letter at 2; Man Letter at 2; TransMarket Letter; FIA Letter at 1 (the proposal " * * * unfairly penalizes member firms that derive a significant portion of their revenue from activities unrelated to their securities business, which are not subject to the oversight of the NASD and with respect to which the NASD provides no regulatory services.") and at 4-5.

⁹ See e.g., CFTC Letter at 1; NFA Letter at 1-2 (GIA will collect income via FOCUS reports that is unrelated to securities, such as over-the-counter derivatives, cash commodities, futures, and foreign exchange); Fimat Letter (GIA will have adverse and disproportionate impact on combined broker-dealers/futures commission merchants by allowing the NASD to collect fees on revenue that does not come from securities-related business); Mercantile Letter at 1, 3 (" * * * there is no nexus between the NASD fee and its regulatory responsibilities in the commodity industry."); Goldenberg Letter at 1 (Goldenberg will experience significant increase in its GIA, though "not a single customer * * * would be entitled to utilize any of the regulatory services of the NASD.").

¹⁰ See NFA Letter at 4-5; FIA Letter at 2-3; Man Letter at 3.

¹¹ See Phlx Letter at 1; Mercantile Letter at 1.

NFA may determine that it is acceptable to assess fees based on its members' securities business.¹²

In its response to the commenters, the NASD focused only on comments made in connection with the instant proposed rule change.¹³ The NASD expressed its belief that the proposed changes to the GIA are fair and equitable, because they will "ensure that all NASD members use the same simplified fee structure and will be assessed on the same uniform basis."¹⁴

With regard to the commenters' concerns that there is no clear nexus between the NASD's proposed fees and the NASD's regulatory services provided, the NASD explained that most of the commenters objected to including commodities in the GIA.¹⁵ By reinstating the exclusion for commodities income, the NASD believes it has addressed the commenters' concerns in this regard. The NASD stated that it believes that the requirement that fees be reasonable and equitably allocated does not require a fee structure "so specific and complex as to tie specific self-regulatory programs and related expenses to specific business lines within a firm[.]" The NASD reiterated the position outlined in the proposal—that total revenues of a broker-dealer member, combined with trading activity of those members and the number of registered persons, serves as an effective measure of what drives the NASD's regulatory costs.¹⁶ Regarding the concern that other markets may institute fees similar to the

¹² Mercantile Letter at 4 ("NFA could also decide to impose fees on dually registered members with respect to their securities-related transactions * * * duplicative fees would be imposed at the expense of members' profit margin, or, alternatively, such fees would merely be passed on by the members to the ultimate customers."). See also Fimat Letter at 2.

¹³ NASD Response Letter at 2-3. The Commission notes that the NASD Response Letter speaks of 15 comment letters, because the NASD listed comment letters received on the instant filing and on SR-NASD-2002-98. There are only 13 letters specific to the instant filing, however, and the NASD will address comments relating to SR-NASD-2002-98 at a later time.

¹⁴ *Id.* at 5. The NASD also noted that it removed deductions and exclusions that were used inconsistently by member firms from the GIA equation. *Id.* However, the NASD reinstated the exclusion for commodities income. Noting that some of its member firms conduct securities and commodities business in a single, jointly registered entity, while other members conduct a substantially similar business in separate entities with separate registrations, the NASD determined that "to subject those conducting securities and commodities business in a single jointly registered entity to the increased expense burden (when the commodities income is already assessed under a comparable regulatory scheme) would result in similar entities receiving different treatment." *Id.*

¹⁵ NASD Response Letter at 7.

¹⁶ *Id.* at 8.