



September 26, 2002

By Hand and Via Electronic Mail

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: NASD Proposed Member Regulatory Pricing Structure:
• Trading Activity Fee (File No. SR-NASD-2002-98)
• Gross Income Assessment and Personnel Assessment (File No. SR-NASD-2002-99)

Dear Mr. Katz:

The Securities Industry Association ("SIA")¹ appreciates the opportunity to comment on the National Association of Securities Dealer's ("NASD") proposed amendments to Schedule A of the NASD By-Laws regarding the member regulatory pricing structure. The NASD's proposal contemplates three types of fees and assessments: implementation of a new Trading Activity Fee ("TAF") that replaces the former Section 8(a) Regulatory Fee,² and modification of the existing Gross Income Assessment ("GIA") and Personnel Assessment ("PA").³ Although the NASD states that the fees and assessments taken together will be revenue neutral *to the NASD*, in fact, the proposal will impact different market participants in very different ways. Unfortunately,

¹ The Securities Industry Association brings together the shared interests of more than 600 securities firms to accomplish common goals. SIA member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 93 million investors directly and indirectly through corporate, thrift, and pension plans. In the year 2001, the industry generated \$198 billion in U.S. revenue and \$358 billion in global revenues. Securities firms employ approximately 750,000 individuals in the United States. (More information about SIA is available on its home page: <http://www.sia.com>.)

² See Securities Exchange Act Release No. 46416 (August 23, 2002), 67 FR 55901 ("Release No. 46416"), publishing notice of filing and immediate effectiveness of SR-NASD-2002-98.

³ See Securities Exchange Act Release No. 46417 (August 23, 2002), 67 FR 55893, publishing notice of SR-NASD-2002-99. The proposed changes to the GIA and PA include the elimination of deductions for the GIA and revised rates for both the GIA and PA.

the TAF was filed under Section 19(b)(3)(A) of the Securities Exchange Act of 1934 ("Act"), which provides for immediate effectiveness, without the effective rate announced, making it impossible for member firms to adequately assess the impact of all elements of the new pricing structure taken as a whole.⁴ In addition, numerous interpretive questions were raised by the TAF proposal.

SIA appreciates the efforts of the NASD to address questions the industry has raised since first announcing proposed changes to its fee structure.⁵ These efforts have included the NASD staff's participation in numerous SIA committee meetings and conference calls, and the recent issuance of Notice To Members 02-63 that addresses certain of the firms' questions. Significant issues remain, however, and SIA believes that the NASD, the Securities and Exchange Commission ("SEC" or "Commission") and firms would benefit from an opportunity to provide comments on the TAF and how it interrelates with the GIA and PA, as well as with the regulatory fees imposed by other self-regulatory organizations ("SROs"). We respectfully suggest, therefore, that the TAF proposal be filed under Section 19(b)(2) of the Act, and wish to comment at this time solely on this procedural issue.

Discussion

The TAF differs in many respects from the Section 8 Regulatory Fee that it replaces. The TAF is a transaction-based fee applied across all markets, whereas the Regulatory Fee is Nasdaq market-based. The Regulatory Fee is assessed on NASD members, through clearing and self-clearing firms, on all transactions reported through Nasdaq's Automated Confirmation Transaction system. The TAF, on the other hand, will be assessed through clearing and self-clearing firms on a per share basis on the sell-side of all member transactions in all covered securities regardless of where the trade is executed (with some exceptions). Covered securities include (1) all exchange-registered securities wherever executed (other than bonds, debentures and other evidence of indebtedness); (2) all other equity securities traded other than on an exchange; and (3) all security futures wherever executed. SIA believes that these constitute significant changes, which should have been subject to public comment before becoming effective.

SIA member firms are concerned that the manner in which the NASD's proposal became effective may not be consistent with the Commission's previously expressed position and the governing rules under Section 19(b), in that the TAF presents a significant change that warrants filing under Section 19(b)(2) of the Act, which allows for

⁴ The implementation date announced in Release No. 46416 is October 1, 2002.

⁵ See NASD Notice To Members 02-09 in which the NASD requested comment on revisions to the regulatory fee imposed under Section 8 of Schedule A to the NASD By-Laws. In response to negative comment from the industry, NASD developed this alternative, which was described in NASD Notice To Members 02-41 and filed with the SEC for approval in File Nos. SR-NASD-2002-98 and SR-NASD-2002-99.

a public comment period before a proposal becomes effective. We note that the SEC states in the release adopting amendments to Rule 19b-4 that proposals of SROs to adopt significant new fees should be filed under Section 19(b)(2) rather than Section 19(b)(3)(A). Specifically, the release states:

[U]nder Section 19(b)(3)(A)(ii) of the Act, rule changes that establish or change a due, fee, or other charge imposed by the SRO may become effective upon filing. The Commission notes that the filing of a proposed fee applicable to members may nonetheless raise significant regulatory issues and thus be required, consistent with current Commission policy, to be submitted pursuant to Section 19(b)(2). In addition, the Commission continues to believe that, as a matter of general policy, an SRO proposed rule change that establishes or changes a due, fee or other charge applicable to a non-member or non-participant must be filed under Section 19(b)(2) for full notice and comment. While filings concerning fees applicable to non-members have not been eligible to become effective upon filing under Section 19(b)(3)(A)(ii), some such filings now may qualify for expedited treatment under the noncontroversial category.⁶ [footnotes omitted]

Even though the SIA is focusing on process at this time, members have expressed concerns about the policy issues underlying the rule change and other substantive matters. For example, certain member firms believe that the TAF raises significant regulatory issues, particularly with its reach across all markets. These firms question whether all SROs may impose fees on transactions in all markets. In addition, firms note that because the new fees in the aggregate are "revenue neutral" does not mean that they do not raise significant issues – the new fees may impact different market participants in very different and material ways.⁷

Member firms also believe that the implementation date is unrealistic because firms do not yet know the rate of the fee and important interpretive questions have only recently been addressed. Without an established rate for the TAF,⁸ it is difficult to assess the implications of the TAF – both separately⁹ and in combination with the GIA and

⁶ Securities Exchange Act Release No. 35123 (December 28, 1994), 59 FR 66692.

⁷ In regard to the NASD's statement that the fees and assessments are revenue neutral to the NASD, some firms would have appreciated further information from the NASD showing that the NASD has conducted a financial analysis demonstrating the revenue neutrality of the pricing structure. Firms also question the impact of changing economic conditions on the overall fee proposal and question whether additional assurances should be made by the NASD regarding maintaining fee levels.

⁸ The NASD, in Notice To Members 02-63, states that it will publish the applicable rate no later than the implementation date of October 1, 2002.

⁹ *E.g.*, firms have questions regarding the TAF on actual costs, calculation of the fees, and whether and how the fees (and any potential rebates) could be passed on to customers and how that would be disclosed on customer confirmations.

PA.¹⁰ With regard to interpretive questions, the SIA recognizes and appreciates the NASD's efforts to date to address these questions, including through the recent issuance of a new Notice to Members.¹¹ Member firms, however, would have preferred resolving their questions, such as those regarding coverage of securities and application of the fee to floor based brokers dually registered with the NASD, prior to any such significant rule change becoming effective.

In addition, after the interpretive issues have been resolved and a rate established, firms must undertake programming changes to capture and report the new TAF. In light of the significant systems infrastructure and programming changes necessitated by various other recent initiatives including the Patriot Act, the SEC's books and records rules, NASD's INSITE and TRACE systems, and the Sarbanes-Oxley Act, firms would appreciate substantially more lead time for implementation of this fee change. In summary, SIA believes the NASD should publish significant rule changes such as the TAF sufficiently in advance of the effective date so that firms have an opportunity to analyze and comment on the financial impact to their businesses, and to implement and test the systems and operational changes required.

Conclusion

The SIA requests on behalf of member firms that the SEC review the NASD's TAF rule filing in light of the SEC's stated position to ensure that it was filed consistent with existing standards, and then act appropriately upon its review and take remedial action if necessary.

The SIA appreciates this opportunity to provide comments on certain procedural aspects of NASD's proposal to amend Schedule A to the NASD By-Laws to amend its member regulatory pricing structure. If we can provide further information or clarification of the points made in this letter, please contact me or Ann Vlcek, Associate General Counsel, at 202-296-9410.

Sincerely,

Stuart J. Kaswell
Senior Vice President and
General Counsel

¹⁰ *I.e.*, firms stated that the lack of the TAF rate makes it difficult to assess and comment on the GIA and PA rule proposals for which a comment period was provided.

¹¹ See NASD Notice To Members 02-63 issued on September 18, 2002.

Jonathan G. Katz
Secretary
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