

## V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>23</sup> that the proposed rule change (SR-NASD-2006-039), as amended, be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>24</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54984; File No. SR-NASD-2006-135]

### Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposal Relating to Implementation of Certain Approved Rule Changes Reflecting the Complete Separation of Nasdaq from NASD

December 20, 2006.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on December 20, 2006, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been substantially prepared by NASD. NASD has filed this proposal pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder<sup>4</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

NASD has filed a proposed rule change relating to a phased implementation of SR-NASD-2006-104, which was approved by the Commission on November 21, 2006.<sup>5</sup> Specifically, NASD is proposing to

implement on December 20, 2006, amendments to the Plan of Allocation and Delegation of Functions by NASD to Subsidiaries ("Delegation Plan") and the By-Laws of NASD, NASD Regulation and NASD Dispute Resolution, and the deletion of The Nasdaq Stock Market Inc. ("Nasdaq") By-Laws, which were previously approved in SR-NASD-2006-104, to reflect Nasdaq's complete separation from NASD, and, on that same date, dissolve NASD's controlling share in Nasdaq.

### 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

##### 1. Purpose

##### Background

On June 30, 2006, the Commission approved proposed rule change SR-NASD-2005-087, which, among other things, amended NASD's Delegation Plan, By-Laws and NASD rules to reflect the operation of The NASDAQ Stock Market LLC (the "Nasdaq Exchange") as a national securities exchange for Nasdaq-listed securities.<sup>6</sup> For a transitional period that commenced on August 1, 2006, the Nasdaq Exchange has been operating as an exchange for Nasdaq-listed securities only. Nasdaq, as a subsidiary of NASD, continues to perform its obligations under the Delegation Plan with respect to over-the-counter ("OTC") quoting, trading and execution of non-Nasdaq exchange-listed securities, including the operation of, among other things, its SuperIntermarket ("SiM") trading platform. Nasdaq no longer performs any functions under the Delegation Plan relating to Nasdaq-listed securities.

On November 21, 2006, the Commission approved SR-NASD-2006-104.<sup>7</sup> Pursuant to SR-NASD-2006-104, NASD proposed to delete the Nasdaq

By-Laws and amend the Delegation Plan, the By-Laws of NASD, NASD Regulation and NASD Dispute Resolution, and NASD rules to reflect the separation of Nasdaq from NASD upon the operation of the Nasdaq Exchange as a national securities exchange for non-Nasdaq exchange-listed securities. In addition, NASD proposed to amend NASD rules for OTC quoting and trading in non-Nasdaq exchange-listed securities to reflect the manner in which NASD will be satisfying its regulatory obligations under the Exchange Act and the rules thereunder on a temporary basis until NASD's Alternative Display Facility ("ADF") is able to satisfy those obligations ("Modified SiM Rules").<sup>8</sup> Finally, NASD proposed to expand the scope of the NASD/Nasdaq Trade Reporting Facility rules to include trade reporting in non-Nasdaq exchange-listed securities and make other clarifying and conforming changes. As approved, SR-NASD-2006-104 will be effective on the date on which the Nasdaq Exchange operates as a national securities exchange with respect to non-Nasdaq exchange-listed securities. When SR-NASD-2006-104 was originally filed, that date was anticipated to be October 2006; however, it is now anticipated to be in the first quarter of 2007.

### Separation of Nasdaq from NASD and Proposed Phased Implementation of SR-NASD-2006-104

As noted above, Nasdaq continues to exercise regulatory authority under the Delegation Plan. Therefore, NASD retains control of Nasdaq through a single share of Series D Preferred Stock (the "Series D Share") that allows NASD to cast a majority of the votes in any matter submitted to Nasdaq's stockholders, including the election of Nasdaq directors. Once the delegation to Nasdaq is no longer necessary, the Series D Share will automatically lose its voting rights and will be redeemed by Nasdaq for \$1.00.

In light of the delay in implementation of portions of SR-NASD-2006-104, NASD is proposing to eliminate its delegation and effectuate

<sup>8</sup> This is one of the conditions required by the Commission before the Nasdaq Exchange can operate as an exchange for non-Nasdaq exchange-listed securities. The Commission approved the Nasdaq Exchange application on January 13, 2006. See Securities Exchange Act Release No. 53128, 71 FR 3550 (January 23, 2006) (File No. 10-131). See also Securities Exchange Act Release No. 54085 (June 30, 2006), 71 FR 38910 (July 10, 2006), which modified the conditions set forth in the Nasdaq Exchange approval order to allow the Nasdaq Exchange to operate as a national securities exchange solely with respect to Nasdaq-listed securities.

<sup>23</sup> 15 U.S.C. 78s(b)(2).

<sup>24</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

<sup>5</sup> See Securities Exchange Act Release No. 54798, 71 FR 69156 (November 29, 2006) (order approving SR-NASD-2006-104).

<sup>6</sup> See Securities Exchange Act Release No. 54084 (June 30, 2006), 71 FR 38935 (July 10, 2006) (order approving SR-NASD-2005-087).

<sup>7</sup> See note 5 supra.

complete separation with Nasdaq, including dissolution of the Series D Share, prior to commencement of operation of the Nasdaq Exchange as an exchange for non-Nasdaq exchange-listed securities. However, for a transitional period, Nasdaq will continue to perform the same services it does today, including operation of the SiM trading platform, on NASD's behalf via the Transitional System and Regulatory Services Agreement. NASD anticipates that this transitional period will be brief, commencing on December 20, 2006 and concluding once SR-NASD-2006-104 is fully implemented in the first quarter of 2007.

To effectuate this phased implementation, NASD is proposing to implement on December 20, 2006 certain portions of SR-NASD-2006-104 to reflect the separation of Nasdaq from NASD and that Nasdaq will no longer be operating under the Delegation Plan. Specifically, NASD is proposing to: (1) Remove references in the Delegation Plan to Nasdaq as a subsidiary and remove the delegation of authority to Nasdaq (Section III) and the delegation of authority relating to Stockwatch (Section IV); (2) revise the NASD By-Laws, NASD Regulation By-Laws and NASD Dispute Resolution By-Laws to remove references to Nasdaq as a subsidiary of NASD; and (3) delete the Nasdaq By-Laws. During this transitional period, references to "Nasdaq" in NASD's rules shall be deemed to mean "Nasdaq operating on behalf of NASD via the Transitional System and Regulatory Services Agreement." Additionally, NASD notes that during this transitional period, the Market Operations Review Committee, which was validly constituted pursuant to a delegation by the NASD Board, will continue to exist in its current form and perform the functions set forth in NASD Rules 5265 and 11890. All remaining changes approved in SR-NASD-2006-104 will become effective on the date upon which the Nasdaq Exchange operates as an exchange for non-Nasdaq exchange-listed securities.<sup>9</sup> As such,

<sup>9</sup> As permitted by the terms of the Transitional System and Regulatory Services Agreement, NASD may, in its sole discretion, determine to continue to use Nasdaq as a vendor to operate SiM, even upon the Nasdaq Exchange's operation as an exchange for non-Nasdaq exchange-listed securities. In that event, the current rules relating to SiM will remain in place and the approved rule changes in SR-NASD-2006-104 relating to Modified SiM Rules will not be implemented. All other rule changes that are part of SR-NASD-2006-104 (e.g., amendments to the NASD/Nasdaq Trade Reporting Facility Rules) will become operative upon the operation of NASD's ADF for non-Nasdaq exchange-listed securities as approved by the Commission on September 28, 2006. See Securities Exchange Act Release No. 54537 (September 28,

during this transitional period, there will be no changes from the perspective of users or participants of NASD facilities operated by Nasdaq.

NASD has filed the proposed rule change for immediate effectiveness. NASD is proposing that the operative date of the proposed rule change be December 20, 2006, the date on which NASD proposes to effectuate the complete separation of Nasdaq from NASD.

## 2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>10</sup> which requires, among other things, that NASD rules 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. NASD believes that the proposed rule change will provide an effective mechanism and regulatory framework for effectuating Nasdaq's complete separation from NASD.

### B. Self-Regulatory Organization's Statement on Burden on Competition

NASD does not believe that the proposed rule change would result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### 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

Because the proposal does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days after the date of the filing, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>11</sup> and Rule 19b-4(f)(6) thereunder.<sup>12</sup>

2006), 71 FR 59173 (October 6, 2006) (order approving SR-NASD-2006-91). NASD will submit a filing to the Commission to effectuate this.

<sup>10</sup> 15 U.S.C. 78o-3(b)(6).

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>12</sup> 17 CFR 240.19b-4(f)(6). As required by Rule 19b-4(f)(6)(iii) of the Act, NASD provided the Commission with written notice of its intent to file the proposed rule change, along with a brief

NASD has requested that the Commission waive the 30-day operative delay under Rule 19b-4(f)(6)(iii),<sup>13</sup> and designate the proposed rule change effective immediately. The Commission believes that it is consistent with the protection of investors and the public interest to waive the 30-day operative delay,<sup>14</sup> as such waiver is necessary so that the complete separation of Nasdaq from NASD can be effectuated on December 20, 2006.<sup>15</sup>

At any time within 60 days of the filing of such proposed rule change the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASD-2006-135 on the subject line.

### Paper Comments

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASD-2006-135. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements

description of the text of the proposed rule change, at least five business days prior to the date of the filing of the proposed rule change.

<sup>13</sup> 17 CFR 240.19b-4(f)(6)(iii).

<sup>14</sup> For purposes only of waiving the 30-day operative delay of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>15</sup> Furthermore, the amendments proposed herein were subject to notice and comment and approved by the Commission on November 21, 2006. See note 5 *supra*.

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 also will be available for inspection and copying at the principal office of NASD. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASD-2006-135 and should be submitted on or before January 18, 2007.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>16</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54970; File No. SR-NYSE-2006-114]

### Self-Regulatory Organizations; New York Stock Exchange LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Exchange Rule 123A.30 to Eliminate the Two Tick Rule to Allow for the Execution of CAP-DI Orders at Consecutive Destabilizing Prices Without Floor Official Approval

December 19, 2006.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on December 14, 2006, the New York Stock Exchange LLC ("NYSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been substantially prepared by the Exchange. The Exchange filed the proposed rule change as a "non-controversial" rule change pursuant to Section 19(b)(3)(A) of the Act<sup>3</sup> and Rule

19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange is proposing to amend Exchange Rule 123A.30 to allow a CAP-DI order to be executed at consecutive destabilizing prices without Floor Official approval.

The text of the proposed rule change is available at NYSE, the Commission's Public Reference Room, and [www.nyse.com](http://www.nyse.com).

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

In its filing with the Commission, the Exchange 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. The Exchange 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

###### 1. Purpose

Exchange Rules 13 and 123A.30 describe a type of percentage order<sup>5</sup> called a "convert and parity, destabilizing, immediate-or-cancel" (CAP-DI) order and the manner in which such orders are elected or converted and executed.

CAP-DI orders are "elected" into limit orders when a trade on the Exchange occurs at or within a CAP-DI order's limit price. The size and price of such limit order is the same as the electing trade. The election and execution of CAP-DI orders is automatic.

CAP-DI orders may also be "converted" into limit orders to trade with the NYSE bid and offer or to

establish a new NYSE best bid or offer as prescribed by Rule 123A.30. When first adopted, CAP-DI orders were converted by specialists in accordance with the instructions of the Floor broker who entered the order. Today, CAP-DI orders are automatically converted and trade in certain situations—when the specialist trades for its dealer account in an automatic execution.<sup>6</sup> In that situation, CAP-DI orders that have been entered and are capable of trading at that price are automatically converted and trade along with the specialist.<sup>7</sup> This process benefits customers by ensuring that CAP-DI orders are executed in accordance with their expectations—*i.e.* that they participate in NYSE trades at or within their limit and thereby do not lag behind the market.

The "D" designation on CAP-DI orders stands for "destabilizing" and allows the order to be converted to participate in stabilizing or destabilizing transactions<sup>8</sup> or to bid (offer) in a destabilizing manner.<sup>9</sup>

The "I" designation of the CAP-DI order stands for "immediate execution or cancel" and allows for the cancellation of any converted portion of the order that is not executed immediately at the price of the electing transaction or better. Any portion that is not immediately executed reverts to its status as a CAP-DI order, eligible for subsequent election or conversion and execution.

CAP-DI orders are subject to certain restrictions on conversions to trade and quote that were intended to minimize the specialist's ability to move the price direction of a security through the conversion of the CAP-DI orders.<sup>10</sup> Thus, Exchange Rule 123A.30 provides that CAP-DI orders may not be converted "at consecutively higher or lower prices such that consecutive up or down ticks (as the case may be), follow one another in rapid succession, unless [the specialist] obtains the prior

<sup>6</sup> This occurs either because the specialist has algorithmically generated a trading message or is part of a quote that is automatically executed.

<sup>7</sup> By its terms (convert and parity), specialists and CAP-DI orders trade on parity.

<sup>8</sup> A "destabilizing" trade is a trade that follows the direction of the market as, for example, a purchase on a plus tick or a sale on a minus tick. A stabilizing trade is one that counters the direction of the market as, for example, a purchase on a minus tick or a sale on a plus tick.

<sup>9</sup> Rule 123A.30 sets forth certain size and maximum price restrictions on CAP-DI conversions. The Exchange is not proposing to amend these requirements.

<sup>10</sup> See Securities Exchange Act Release No. 24505 (May 22, 1987), 52 FR 20484 (June 1, 1987) (SR-NYSE-85-1) (approving amendment to Rule 123A.30 permitting conversion of percentage orders on destabilizing ticks under certain restrictions).

<sup>16</sup> 17 CFR 200.30-3(a)(12).

<sup>15</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

<sup>5</sup> Percentage orders are limited price orders to buy or sell a certain volume of the specified security after a trade occurs at or within the order's limit. As such, all percentage orders, including CAP-DI orders, are referred to as "go along orders" because they generally want to trade at prices established by other market participants and do not want to initiate a significant price change or lag behind the market.