

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-66310; File No. SR-NASDAQ-2012-015)

February 2, 2012

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Rule 4618

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ notice is hereby given that on January 19, 2012, the NASDAQ Stock Market LLC (“NASDAQ”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change described in Items I and II below, which Items have been prepared primarily by NASDAQ. NASDAQ filed the proposal pursuant to Section 19(b)(3)(A) (iii) of the Act² and Rule 19b-4(f)(6)³ thereunder so that the proposal was effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the rule change from interested parties.

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

NASDAQ is filing this proposed rule change to amend Rule 4618. The text of the proposed rule change is shown below. Proposed new language is italicized, and proposed deletions are in brackets.

4618. Clearance and Settlement

(a) All transactions through the facilities of the Nasdaq Market Center shall be cleared and settled through a registered clearing agency using a continuous net settlement system. This

¹ 15 U.S.C. 78s(b)(1).

² 15 U.S.C. 78s(b)(3)(A)(iii).

³ 17 CFR 240.19b-4(f)(6).

requirement may be satisfied by direct participation, use of direct clearing services, [or] by entry into a correspondent clearing arrangement with another member that clears trades through such a[n] clearing agency[.], or by use of the services of CDS Clearing and Depository Services, Inc. in its capacity as a member of such a clearing agency.

(b) Notwithstanding paragraph (a), transactions may be settled "ex-clearing" provided that both parties to the transaction agree.

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

In its filing with the Commission, NASDAQ 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. NASDAQ has prepared summaries, set forth in sections (A), (B), and (C) below, of the most significant aspects of these statements.⁴

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

NASDAQ proposes to modify Rule 4618 to clarify that the use of a long-standing arrangement between National Securities Clearing Corporation ("NSCC") and CDS Clearing and Depository Services, Inc. ("CDS")⁵ for clearing transactions in US securities provides an acceptable method for clearing transactions executed on NASDAQ. Among other things, CDS operates Canada's national clearance and settlement operations for cash equities trading, performing a role analogous to NSCC in the US. CDS is regulated by the Ontario and Quebec

⁴ The Commission has modified the text of the summaries prepared by NASDAQ.

⁵ CDS was formerly known as The Canadian Depository for Securities Limited.

securities commissions and the Bank of Canada and has working and reporting relationships with the Canadian Securities Administrators, other Canadian provincial securities commissions, and the Canadian Office of the Superintendent of Financial Institutions. CDS is also a full service member of NSCC and a participant in The Depository Trust Company (“DTC”).

Currently, a Canadian broker-dealer seeking to buy or sell US securities may do so through a US registered broker-dealer with which it establishes a relationship for that purpose. In such a relationship, the US broker-dealer manages the clearance and settlement of the resulting trades, either through direct membership at NSCC or indirectly through a clearing broker with which it has established a relationship. Under the proposed change, a Canadian broker-dealer that is a member of CDS may make use of CDS, and its direct membership in NSCC, to clear and settle the resulting trades. Specifically, the clearing report for the trade will “lock in” CDS, making reference to the CDS membership of the Canadian broker-dealer, as a party to the trade.⁶ NSCC will then look to CDS for the satisfaction of the clearance and settlement obligations of the Canadian broker-dealer. NSCC requires CDS to commit collateral to the NSCC clearing fund like any other NSCC member, the amount of which is based on a risk-based margining methodology. In a similar manner, CDS requires its participants to commit collateral to CDS. The sole risk incurred by NASDAQ and then by NSCC in the arrangement is the highly remote risk that CDS itself might default on its obligations to clear and settle on behalf of the Canadian broker-dealer. This risk is conceptually indistinguishable from the risk of a clearing broker default, but because the value of the trades of the Canadian broker-dealers

⁶ As an NSCC member, CDS is responsible for the clearing and settling of its participants’ trades conducted with US broker-dealers. For purposes of “locking-in” parties, certain CDS participants have discrete NSCC participant codes that identify the Canadian broker-dealer and its participation in the NSCC/CDS clearing arrangement. On midnight of T+1, NSCC takes on the buyer’s credit risk and the seller’s delivery risk.

cleared through the mechanism is likely to be small in comparison to the values cleared through many large US clearing brokers, the magnitude of this risk is correspondingly smaller.

The relationship between NSCC and CDS was established more than two decades ago, and various aspects of the relationship have been recognized through several prior filings⁷ and no-action letters.⁸ A recent description of the parameters of the relationship may be found in NSCC's Assessment of Compliance with the CPSS/IOSCO Recommendations for Central Counterparties.⁹ The most prominent use of the relationship arises under FINRA Rule 7220A, which allows over-the-counter trades executed on behalf of CDS members to be reported through the FINRA/NASDAQ Trade Reporting Facility and cleared through the CDS/NSCC relationship. NASDAQ also understands that the EDGA Exchange and the EDGX Exchange permit clearance of trades executed on behalf of Canadian broker-dealers through this mechanism.

In order to clearly establish that use of the CDS/NSCC relationship is a permissible method of clearing transactions executed on NASDAQ, NASDAQ is proposing to

⁷ See, e.g., Securities Exchange Act Release No. 34-36918 (March 4, 1996), 61 FR 9739 (March 11, 1996) (SR-NASD-95-49) (approving access to Automated Confirmation Transaction Service for CDS members); Securities Exchange Act Release No. 34-40523 (October 6, 1998), 63 FR 54739 (October 13, 1998) (approving establishment of a CDS omnibus account at DTC to facilitate cross-border clearing).

⁸ See, e.g., Letter from Dan W. Schneider, Deputy Associate Director, Commission, to Karen L. Saperstein, Assistant General Counsel, NSCC (November 26, 1984) (available at 1984 WL 47355) (taking no-action position with respect to use of CDS and NSCC with respect to clearing of trades executed on behalf of Canadian broker-dealers on the Boston Stock Exchange); Letter from Dan W. Schneider, Deputy Associate Director, Commission, to Karen L. Saperstein, Assistant General Counsel, NSCC (October 24, 1984) (available at 1984 WL 47356) (taking no-action position with respect to CDS becoming a member of NSCC).

⁹ "Assessment of Compliance with the CPSS/IOSCO Recommendations for Central Counterparties," NSCC (November 14, 2011) (available at http://www.dtcc.com/legal/compliance/NSCC_Self_Assessment.pdf).

amend Rule 4618. Currently, the rule provides that trades must be cleared through a registered clearing agency using a continuous net settlement (“CNS”) system and that this requirement may be satisfied by direct participation, use of direct clearing services, or by entry into a correspondent clearing arrangement with another member that clears trades through such an agency. NSCC is currently the only registered clearing agency using a CNS system for trades executed on NASDAQ. While it is possible that the term “direct clearing services” could be construed to cover CDS’s participation in NSCC on behalf of its members because CDS is a direct member of NSCC for the purpose of providing clearing services to its members the term has not previously been construed by NASDAQ in that manner. Accordingly, NASDAQ believes that the clarity of the rule would be enhanced by directly recognizing the CDS/NSCC relationship in the rule text. NASDAQ proposes amending the rule to provide that the rule may be satisfied through “use of the services of CDS Clearing and Depository Services, Inc. in its capacity as a member of such a clearing agency.” Whenever a clearing arrangement making use of CDS’s membership in NSCC is established, the NASDAQ member, the Canadian broker on whose behalf it is acting, CDS, and NASDAQ will sign a short agreement addressed to NSCC in which the parties acknowledge their use of the CDS/NSCC arrangement.

2. Statutory Basis

NASDAQ believes that the proposed rule change is consistent with the provisions of Section 6 of the Act¹⁰ in general and with Section 6(b)(5) of the Act¹¹ in particular in that the proposal is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable practices of trade, to foster cooperation and coordination with persons engaged in

¹⁰ 15 U.S.C. 78f.

¹¹ 15 U.S.C. 78f(b)(5).

regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system and in general to protect investors and the public interest. Specifically, by allowing Canadian broker-dealers whose trades are executed on NASDAQ to make use of the long-standing arrangement between NSCC and CDS for clearing transactions, NASDAQ believes that the proposed rule change will directly foster cooperation and coordination with the two primary North American cash equities clearinghouses and their respective members and will thereby promote a free and open market. Because the arrangement between NSCC and CDS, which has been in place in varying forms for over two decades, includes mechanisms to provide for the collateralization of the obligations arising thereunder, NASDAQ believes that the proposed change is fully consistent with the protection of investors and the public interest.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASDAQ does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed change will ensure that Canadian broker-dealers whose trades are executed on NASDAQ are able to make use of an additional option for clearing such transactions, thereby promoting competition with respect to the availability of clearing services. The change will enhance NASDAQ's ability to compete in the over-the-counter market with other exchanges that offer the ability to clear through the CDS/NSCC relationship.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments relating to the proposed rule change have not been solicited or received. NASDAQ will notify the Commission of any written comments received by NASDAQ.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not significantly affect the protection of investors or the public interest, does not impose any significant burden on competition, and, by its terms, does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become immediately effective pursuant to Section 19(b)(3)(A) of the Act¹² and Rule 19b-4(f)(6) thereunder.¹³

NASDAQ has requested that the Commission waive the 30-day operative waiting period contained in Exchange Act Rule 19b-4(f)(6)(iii). The Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest because the arrangement between NSCC and CDS countenanced by the proposed rule change has been in place and has been used for over two decades, includes mechanisms to provide for the collateralization of the obligations arising thereunder, and has long been recognized under FINRA and NASD rules for use in clearing over-the-counter transactions. The technology

¹² 15 U.S.C. 78s(b)(3)(A).

¹³ 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied the five-day prefiling requirement.

changes at NASDAQ necessary to allow implementation of the proposed rule change have already been made. Accordingly, the Commission believes that the change does not significantly affect the protection of investors or the public interest and does promote competition.

Conversely, because delay of implementation would only serve to delay the availability of a well-established clearing mechanism for clearing certain trades executed on NASDAQ and would thereby inhibit customer choice and flexibility without advancing any regulatory goal, it would be consistent with the protection of investors and the public interest to waive the waiting period. Therefore, the Commission designates the proposed rule change as operative upon filing.¹⁴

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend 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. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule change should be approved or disapproved.

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:

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

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. Please include File Number SR-NASDAQ-2012-015 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASDAQ-2012-015. 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 website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements 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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filings also will be available for inspection and copying at the principal office of NASDAQ.

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-NASDAQ-2012-015 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission by the Division of Trading and Markets, pursuant to delegated authority.¹⁵

Kevin O'Neill
Deputy Secretary

¹⁵ 17 CFR 200.30-3(a)(12).