

December 11, 2002



Mr. R. Cromwell Coulson  
Chairman and CEO  
Pink Sheets LLC  
304 Hudson Street  
2<sup>nd</sup> Floor  
New York, NY 10013

Re: Application of NASD Rules to Member Firms using Pink Sheets Linkage

Dear Mr. Coulson:

I am writing in response to your letter dated March 19, 2002, in which you requested interpretive guidance concerning the application of NASD Rules to communications made through the Pink Link ("PLINK"), an electronic instant messaging service operated by Pink Sheets LLC as a replacement for telephone contact between your subscribers' trading desks.

In your letter, you stated that Pink Sheets LLC has developed an electronic instant messaging service, called PLINK, which allows NASD member broker/dealers that chose to subscribe to the Pink Sheets quotation service to send messages to other subscribers. You state that PLINK essentially allows NASD member broker/dealers to automate the telephonic process of communicating with over-the-counter ("OTC") market makers, supplanting the need for verbal contact between trading desks. You state that PLINK will identify incoming and outgoing messages, allow traders to see subsequent messages and responses, and display different identifiers to indicate whether a message has been sent, cancelled or responded to, as well as whether the message is in transit to the PLINK server or has been received by the other party. You represent that all PLINK messages will be time stamped and retained in the Pink Sheets historical database. Finally, you state that upon request, as with Pink Sheets quotations, Pink Sheets LLC will make available to NASD all PLINK messages.

In your letter, you request interpretive guidance relating to three issues. First, you ask whether NASD members' responsibilities under NASD Rules will be the same as they currently are for oral communications via telephone when using PLINK to send messages to and receive messages from other subscribers. More specifically, you inquire about an OTC market maker's responsibilities under NASD Rules if the market maker has chosen to participate in PLINK and receives an electronic order message from another member via PLINK. Second, you inquire how, and in what time frame, an OTC market maker should respond to an electronic order message from another broker/dealer via PLINK, at a price for which the market maker is publishing a firm quotation and liable under Rule 3320. Third, you inquire how an OTC market maker should respond to electronic order messages via PLINK for which, according to your letter, the market maker is no longer liable because it has executed a prior order at the quoted price and size and is in the process of immediately updating the quotation. You ask

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further whether the market maker should decline the electronic order message under the stated circumstances and in what time frame the market maker should respond.

In order to determine an OTC market maker's obligations under NASD Rules you must look at the particular facts and circumstances. In general, NASD members are obligated to comply with all applicable securities laws and NASD rules.<sup>1</sup> For example, an OTC market maker's responsibilities during trading generally include, but are not limited to, those stated in NASD Rule 2110 (just and equitable principles of trade), Rule 3310 (bona fide publication of transactions and quotations), Rule 3320 (firm quote rule), IM-3320 (specifically applying Rule 3320 to the OTC market, including National Quotation Bureau sheets), and Rule 6750 (minimum quotation size requirements for OTC equity securities).<sup>2</sup> In assessing the applicability of a particular NASD rule to a particular transaction, the regulatory staff would normally look at the relevant facts and circumstances surrounding the transaction, including a working knowledge of how the quoting or trade reporting facility operates. NASD staff, however, is unfamiliar with PLINK's functionality and protocols. Accordingly, it is difficult to determine with any precision what responsibilities market makers have under NASD rules in the specific context of PLINK electronic instant messaging service.

Having set forth the applicable rules to the questions posed in your letter, we do not believe that reaching further conclusions regarding specified events, that may or may not take place within PLINK, are either necessary or appropriate. We assume from your letter that the rules and interpretive materials cited herein are clear in their language and unambiguous in their application.<sup>3</sup> It is not the medium through which events transpire that controls the applicability of these rules; rather these rules apply and are triggered by the occasion of the facts and circumstances that give rise to the obligations specified in these rules.

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<sup>1</sup> NASD members will, among other things, continue to be required to comply with record retention standards in conformity with all applicable laws, rules, regulations, and statements of policy. While members are generally not required to record the contents of oral communications via the telephone, NASD Rule 3010 and SEC Rules 17a-3 and 17a-4 would likely require recording and preservation of PLINK messages. The responsibilities of NASD members to record and preserve PLINK messages is beyond the scope of this letter and, accordingly, is not addressed.

<sup>2</sup> Rule 2110 requires a member, in the conduct of its business, to observe high standards of commercial honor and just and equitable principles of trade. Rule 3310 generally prohibits a member from publishing or circulating any report of a securities transaction or any quotation for a security unless the member believes it is bona fide and that nominal quotations, if used, are identified as such. Rule 3320 provides that "no member shall make an offer to buy from or sell to any person any security at a stated price unless such member is prepared to purchase or sell, as the case may be, at such price and under such conditions as are stated at the time of such offer to buy or sell." Rule 6750 provides that every member firm that functions as a market maker in OTC equity securities on an inter-dealer quotation system that permits quotation updates on a real-time basis, must honor those quotations for the minimum size applicable to the market maker's firm bid or ask.

<sup>3</sup> Your letter does not articulate any ambiguity in the language or application of the rules cited in this response. The staff does not consider a question concerning the application of certain rules as setting forth any ambiguity with respect to such rules unless the party seeking interpretive guidance expressly sets forth the basis for the lack of clarity in the rule language or its application.

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Please note that the opinions expressed in this letter are staff opinions only and have not been reviewed or endorsed by the Board of NASD. This letter responds only to the issues you have raised based on the facts as you have described them in your letter, and does not necessarily address any other rule or interpretation of NASD or all the possible regulatory and legal issues involved.

Sincerely,

Kathleen A. O'Mara  
Associate General Counsel

cc. Cathleen Shine, Senior Vice President and District Director  
NASD, District No. 10