

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

1. Purpose

Nasdaq's InterMarket is a quotation, communication, and execution venue that allows NASD members to quote and trade stocks listed on the New York Stock Exchange, Inc. ("NYSE") and the American Stock Exchange LLC ("Amex"). The InterMarket competes with regional exchanges like the Chicago Stock Exchange, Inc., the Boston Stock Exchange, Inc., and the Cincinnati Stock Exchange, Inc. for retail order flow in stocks listed on the NYSE and the Amex. Through the InterMarket, Nasdaq operates the Computer Assisted Execution System ("CAES"), a system that facilitates the execution of trades in listed securities between NASD members that participate in InterMarket, and the InterMarket Trading System ("ITS"), a national market plan system that permits trades between NASD members and specialists on the floors of national securities exchanges that trade listed securities.⁸

Nasdaq proposes to modify the InterMarket Transaction Credit Program (the "Program"). Under the Program, Nasdaq shares a portion of the tape revenues that it receives (through the NASD) from the Consolidated Tape Association ("CTA"), by providing a transaction credit to members who engage in over the counter ("OTC") trading activity in CTA-eligible securities. Nasdaq calculates two separate pools of revenue from which credits can be earned: one representing 50% of the revenues received from the CTA for providing trade reports in NYSE-listed securities executed in the InterMarket for dissemination by the CTA, the other representing 50% of the revenue received from the CTA for reporting Amex trades.

On November 22, 2002, the CTA met and unanimously approved a modification to its capacity planning and payment process. As a result of this modification, Nasdaq and other CTA participants will incur CTA expenses based on predicted capacity rather than on an ex-post basis. Further, participants will be billed this cost directly as opposed to CTA deducting all operating costs from the Consolidated Tape ("CT") and Consolidated Quotation ("CQ") revenues collected. This is a change from the prior CTA practice of

deducting operational system costs directly from the CT and CQ gross income available for distribution prior to the disbursement of transaction credits to plan participants.

Nasdaq proposes to amend its transaction credit formula in order to adjust to this CTA billing change. Specifically, prior to Nasdaq distributing 50% of data revenues it receives from CTA, Nasdaq will deduct the capacity expense allocated to Nasdaq by the CTA. Nasdaq will allocate this capacity expense to Tape A and Tape B according to each tape's percentage of total trades executed on Nasdaq.⁹ Deducting the capacity expense prior to distributing tape revenue effectively preserves the current arrangements, whereby Nasdaq and its InterMarket members share these capacity costs.

2. Statutory Basis

Nasdaq believes that the proposed rule change, as amended, is consistent with the Act, including section 15A(b)(5) of the Act,¹⁰ which requires that the rules of the NASD provide for the equitable allocation of reasonable fees, dues, and other charges among members and issuers and other persons using any facility or system which the NASD operates or controls. Nasdaq represents that the proposed rule change, as amended, will maintain the current cost of conducting business through InterMarket for members that provide liquidity through ITS or CAES. Nasdaq believes that continuing to encourage members to provide liquidity will enhance the efficiency of InterMarket and benefit investors whose trades are routed to InterMarket by increasing the likelihood that they will be promptly executed.

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

Nasdaq does not believe that the proposed rule change, as amended, will 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.

⁹ For example, if Nasdaq incurs \$100,000 in capacity expenses, and its members execute 700 transactions in Tape A securities and 300 transactions in Tape B securities, Nasdaq will allocate \$70,000 of capacity expense to Tape A and \$30,000 to Tape B.

¹⁰ 15 U.S.C. 78o-3(b)(5).

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

The forgoing rule change has become effective on April 3, 2003, upon filing of Amendment No. 1 to the proposed rule change pursuant to section 19(b)(3)(A)(ii) of the Act¹¹ and subparagraph (f)(2) of Rule 19b-4 thereunder¹² in that it establishes or changes a due, fee, or other charge imposed by the Nasdaq. At any time within 60 days of the filing of a rule change pursuant to section 19(b)(3)(A) of the Act, the Commission may summarily abrogate the rule change, as amended, 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.¹³

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change, as amended, 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 at the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to the File No. SR-NASD-2003-63 and should be submitted by May 6, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁴

Margaret H. McFarland,
Deputy Secretary.

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¹¹ 15 U.S.C. 78s(b)(3)(A)(iii).

¹² 17 CFR 240.19b-4(f)(2).

¹³ For purposes of determining the effective date of the filing and calculating the 60-day abrogation date, the Commission considers the period to commence on April 3, 2003, the date Nasdaq filed Amendment No. 1.

¹⁴ 17 CFR 200.30-3(a)(12).

⁸ See CAES/ITS User Guide, p. 5, at www.intermarket.nasdaqtrader.com.