

the original rule filing.³ The proposed rule change, as amended, was published for comment in the **Federal Register** on December 9, 2002.⁴ The Commission received no comments on the proposal. This order approves the proposed rule change, as amended.

II. Description of the Proposal

Nasdaq proposes to amend NASD rule 11890, which provides Nasdaq with the authority to nullify or modify transactions.

a. Review of Transactions Pursuant to Complaint of Market Participant

Under NASD rule 11890, Nasdaq has the authority to receive petitions from market participants requesting that designated officers of Nasdaq review the terms of a transaction and nullify or modify it if the transaction is found to be clearly erroneous. Among other things, NASD rule 11890, as amended by this proposal, will explicitly limit Nasdaq's purview to transactions arising out of the use or operation of Nasdaq execution or communication systems and explicitly require that the parties to a reviewable transaction be readily identifiable by Nasdaq through its systems. Amended NASD rule 11890 will also clarify, in part, that it covers transactions entered into by a member of a UTP exchange through a Nasdaq execution system. Thus, the rule will cover transactions executed between a Nasdaq member and a member of a UTP exchange that had agreed to accept automatic executions through SuperSOES or SuperMontage, but will not cover transactions where the UTP exchange merely posted a quote and was accessible only via telephone. The amended rule would also clarify that information submitted by parties to Nasdaq must be received by Nasdaq within the time frames specified in the rule.

b. Review of Transactions on Nasdaq's Own Motion

Nasdaq proposes to amend NASD rule 11890 to state that Nasdaq's authority to review transactions based upon its own motion may be exercised in the event of extraordinary market conditions or other circumstances in which the nullification or modification of transactions may be necessary for the maintenance of a fair and orderly market or the protection of investors

and the public interest. Amended NASD rule 11890 will also clarify that Nasdaq's authority to review transactions based upon its own motion may be applied to any transaction arising out of or reported through a Nasdaq quotation, execution, communication, or trade reporting system, including transactions entered into by a member of a UTP exchange through a Nasdaq execution system (but excluding transactions entered into through, or reported to, a UTP exchange).

Additionally, the proposed rule change will amend the time frame for action to require that the Nasdaq officer, either the Nasdaq President or Executive Vice President designated by the President, on Nasdaq's own motion, act, except in extraordinary circumstances, no later than 3 p.m. on the next trading day. Finally, Nasdaq is adding interpretative material after the rule to provide that it shall be considered conduct inconsistent with just and equitable principles of trade for a member to refuse to take action that is necessary to effectuate a final decision of a Nasdaq officer or the Market Operations Review Committee ("MORC").

c. Review by the Market Operations Review Committee

NASD rule 11890 governs review by the MORC, a standing committee composed of representatives of member firms as well as "non-industry" representatives. Persons seeking to appeal a determination by Nasdaq must submit their appeal within the time parameters specified by the rule. Both parties are then given the opportunity to submit supporting arguments in writing, and the matter is submitted to the MORC for a determination. Nasdaq proposes, however, that an officer empowered to review transactions on Nasdaq's own motion (*i.e.*, the President or an Executive Vice President) may determine that the number of transactions affected by a decision to break or modify trades on Nasdaq's own motion is such that the decision must be accorded immediate finality in order to maintain a fair and orderly market and to protect investors and the public interest.

d. Communications Between Nasdaq and Market Participants

Amended NASD rule 11890 will describe in greater detail the parameters for communications between Nasdaq and market participants. Specifically, the proposal will provide that materials submitted to Nasdaq or the MORC must be submitted via facsimile machine and

must be received within the time parameters specified by the rule. However, if requested, Nasdaq staff may authorize submission of materials via electronic mail on a case-by-case basis.⁵ Materials shall be deemed received at the time indicated by a facsimile machine or computer that receives the materials. Nasdaq reserves the right to reject or accept material that is not received within the time parameters specified by the rule.

Nasdaq will provide notice of determinations under the rule via facsimile machine, electronic mail, or telephone (including voicemail). However, in cases where an officer nullifies or modifies a large number of transactions pursuant to Nasdaq's authority to act on its own motion, individual notice may not be practicable. In that case, Nasdaq may provide notice to market participants via the Nasdaq Workstation II Service, a press release, or any other method reasonably expected to provide rapid notice to many market participants.

III. Discussion

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association,⁶ and in particular, the requirements of section 15A(b)(6) of the Act,⁷ which, among other things, requires that the association's rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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, the Commission believes that Nasdaq's proposal may clarify the scope of Nasdaq's authority to review erroneous transactions and the procedural aspects of reviewing such transactions.

Nasdaq proposes to delineate, in part, the conditions under which Nasdaq will consider petitions by market participants to review transactions. Proposed NASD rule 11890 explicitly

⁵ For example, if a party wishes to submit, pursuant to subparagraph (a)(2)(A) of the amended rule, a large document containing supporting information, it may be preferable to submit the document via electronic mail. Electronic mail may be used only when specifically authorized by Nasdaq staff, however, because it is impossible to control the delivery time of electronic mail.

⁶ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

⁷ 15 U.S.C. 78o-3(b)(6).

³ See letter from Mary M. Dunbar, Vice President and Deputy General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission, dated November 1, 2002.

⁴ See Securities Exchange Act Release No. 46939 (December 3, 2002), 67 FR 72994 (December 9, 2002) (SR-NASD-2002-127).