

strategy, if they see a pattern in which they see Citigroup or another broker or dealer that normally handles institutional orders actively buying a stock, in anticipation of a strong buy demand. Citigroup compared this to the full anonymity offered by ECNs and exchanges that prevents market sensitive data from being disseminated on a real-time basis.

The Commission recognizes that in certain securities, specific market makers may be viewed as price leaders, and other market participants may follow the quoting patterns of such market makers, which could result in price changes that frustrate a firm's ability to efficiently work large orders for its customers or obtain executions at improved prices. Therefore, the Commission believes that Nasdaq's proposal may reduce the type of market intelligence that can contribute to market impact. Further, the Commission believes that the proposal may assist broker-dealers in their efforts to satisfy their duty of best execution in working customer orders.

The Commission notes that one commenter stated that the proposal "discriminates unfairly" against ECNs because the execution reports would reveal contra-party identity when the quote of an Order Delivery ECN is decremented.⁴⁶ Another commenter, however, expressed concern that Nasdaq and market participants must make special accommodation for fee-charging ECNs.⁴⁷ The Commission believes that the contra-party identity exception does not unfairly discriminate against Order Delivery ECNs. Instead, the Commission believes that Nasdaq has attempted to accommodate the business models of ECNs and the manner that they participate in SuperMontage.

In the Notice, Nasdaq explained that trades executed with Order Delivery ECNs are processed differently because they have the discretion to reject trades with certain contra-parties if the ECN is in dispute with the contra-party concerning its quote access fee.⁴⁸ Thus, to provide fee-charging Order Delivery ECNs with the opportunity to reject trades with certain members, Nasdaq determined to continue to disclose each contra-party's identity in trades through SIZE where one of the contra-parties is a liquidity providing, fee-charging Order Delivery ECN. Nasdaq believes that this exception also benefits members that execute against the fee-charging Order Delivery ECN by enabling them to track

the fee charges accumulated with each Order Delivery ECN. OE Firms and market makers must accept automatic executions in SuperMontage and do not charge access fees. Therefore, the same disclosure of contra-party information is not required.

As a result, the Commission believes that the proposed rule change reasonably accommodates the different entities; Order Delivery ECNs that charge access fees, market makers, OE Firms, and ECNs that do not charge a fee. As noted by Nasdaq, an ECN may alter the way it participates in SuperMontage to achieve full anonymity. Further, the Commission notes the original SuperMontage filing was amended, in response to ECN comments, to reveal the identity of Nasdaq market participants trading through SIZE by affixing the MPID of the sender on delivered orders and identifying the contra-parties in execution reports.⁴⁹ With regard to trade reports, the system will essentially work in the manner that it does today for Order Delivery ECNs when their quote is hit, which permits them to evaluate their risk on a trade-by-trade basis.⁵⁰ Accordingly, the Commission believes that Nasdaq has reasonably balanced the divergent interests of its members in a manner that is consistent with the Act.

The Commission believes that Nasdaq has also adequately addressed concerns related to risk management. In particular, under the proposed rule change, Nasdaq will: (1) Provide an intra-day concentration report that will disclose a member's aggregate dollar value of purchases and sales with other members with whom it has traded anonymously; (2) report the identities of the members and the aggregated trading listed on the intra-day concentration reports after 4 p.m. Eastern Time; (3) provide the NSCC with real-time trade information for trades executed in SuperMontage; and (4) coordinate disclosure with the NSCC of trades executed anonymously with a firm that the NSCC has ceased to act for and any

firms that cleared through that the NSCC participant.

The Commission believes that this information will assist market participants in managing their risk. The Commission emphasizes that the NSCC and Nasdaq will continue to maintain the identities of all contra-parties for trades that occur through SIZE. In particular, the NSCC will be able to continue its normal risk management functions and settle anonymous trades in the manner that it does today. The only difference will be that the NSCC will withhold the identities of the contra-parties on the contract sheets issued to participants to preserve anonymity through settlement.

The Commission also believes that the proposal should enhance NSCC's ability to incorporate trade execution information into its risk analysis since Nasdaq will be providing this information on a real-time basis. The Commission believes that this may assist the NSCC in deciding sooner to cease to act for a participant, which would prevent other members from executing any additional trades with the firm or a firm that clears through that participant. The Commission notes that Nasdaq developed this process in conjunction with the NSCC and believes that it is consistent with section 15A(b)(6), which requires, in part, that the rules of the NASD foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities.⁵¹

The Commission notes that Bloomberg and Brut stated that the proposal created a systemic risk due to Nasdaq's failure to guarantee trades prior to the attachment of the NSCC guarantee at T + 1.⁵² After carefully considering these comments and Nasdaq's response, the Commission does not believe that the proposed rule change adds new risk that does not currently exist for Nasdaq market participants. Currently, Nasdaq does not act as a guarantor of trades prior to the NSCC guarantee attaching,⁵³ and

⁴⁹ Specifically, Nasdaq amended the original SuperMontage filing, in response to comments regarding credit risk by Bloomberg and Island, so that execution reports immediately revealed the identities of contra-parties for trades that occurred through SIZE. See Securities Exchange Act Release No. 43863 (January 19, 2001), 66 FR 8020, 8033 (January 26, 2001) ("Original SuperMontage Approval Order").

⁵⁰ Bloomberg suggested that Nasdaq could have opted to reveal the contra-party identity through an execution file at the end of the trading day. Nasdaq, however, believed it would be unfair to those members that traded with Bloomberg to expose their identities immediately while masking Bloomberg's identity until the end of the day. See Nasdaq Response Letter.

⁵¹ See Securities Exchange Act Release Nos. 48122 (July 2, 2003), 68 FR 41410 (July 11, 2003) (Notice of File No. NSCC-2003-14) and 48526 (September 23, 2003) (Order approving File No. NSCC-2003-14 to allow NSCC to list an acronym instead of the actual contra-side for a trade in its report of trade data to members).

⁵² Generally, transactions are guaranteed as of the later of: (i) Midnight of T + 1, and (ii) midnight of the day they are reported as compared or as of midnight on the day they appear on T-Contracts for locked-in trades. See Addendum K to NSCC Rules and Procedures for additional explanation.

⁵³ See NASD Rule 4705(g). The Commission notes that other self-regulatory organizations expressly

⁴⁶ See Bloomberg Letter.

⁴⁷ See Citigroup Letter.

⁴⁸ See Notice, *supra* note 5.