

match any non-directed buy and sell quotes/orders entered by an NNMS Order Entry Firm against the quotes/orders of that same NNMS Order Entry Firm on the other side of the market if such a quote/order on the other side of the market is at the best bid/offer in Nasdaq. Nasdaq expects to implement the proposed rule change within 60 days after approval by the Commission. The text of the proposed rule change is set forth below. Proposed new language is in *italics*; proposed deletions are in [brackets].

4710. Participant Obligations in NNMS

(a) No change.
 (b) Non-Directed Orders
 (1) No change.
 (A) No change.
 (B) No change.
 (i) through (iii) No change.
 (iv) Exceptions—The following exceptions shall apply to the above execution parameters:
 (a) If a Nasdaq Quoting Market Participant *or NNMS Order Entry Firm* enters a Non-Directed Order into the system, before sending such Non-Directed Order to the next Quoting Market Participants in queue, the NNMS will first attempt to match off the order against the Nasdaq Quoting Market Participant's *or NNMS Order Entry Firm's* own Quote/Order if the participant is at the best bid/best offer in Nasdaq. [This exception shall not apply to Non-Directed Orders entered by NNMS Order Entry Firms.] Nasdaq Quoting Market Participants *and NNMS Order Entry Firms* may [, and NNMS Order Entry Firms must,] avoid any attempted automatic system matching permitted by this paragraph through the use of an anti-internalization qualifier (AIQ) quote/order flag containing the following values: "Y" or "I", subject to the following restrictions:

Y—if the Y value is selected, the system will execute the flagged quote/order solely against attributable and non-attributable quotes/orders (displayed and reserve) of Quoting Market Participants and NNMS Order Entry Firms other than the party entering the AIQ "Y" flagged quote/order. If the only available trading interest is that of the same party that entered the AIQ "Y" flagged quote/order, the system will not execute at an inferior price level, and will instead return the latest entered of those interacting quote/orders (or unexecuted portions thereof) to the entering party.

I—if the I value is selected, the system will execute against all available trading interest, including the quote/orders of the NNMS Order Entry Firm or Nasdaq

Quoting Market Participant that entered the AIQ "I" flagged order, based exclusively on the execution algorithm selected when entering the AIQ I flagged quote/order.

[The I value described above shall be available for the use of Nasdaq Quoting Market Participants on May 12, 2003.]

- (b) No change.
- (2) through (8) No change.
- (c) through (e) No change.

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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, as amended, 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 such statements.

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

1. Purpose

Currently, SuperMontage rules provide a general exception to the system's execution algorithms that allow non-directed orders entered by NNMS Market Makers and NNMS ECNs to first match off against any quotes/order previously entered by that same party on the opposite side of the market if that previously entered quote/order is at the best bid/offer in Nasdaq.⁴ Market participants can voluntarily avoid or control this automatic matching functionality through use of anti-internalization qualifiers that will either skip quotes/orders entered by them on the opposite side of the market or execute against them based solely on the execution algorithm selected.

NNMS Order Entry Firms are currently prohibited from using this automatic matching functionality and are instead required to enter all non-directed orders with an anti-

internalization qualifier that prevents an automatic match. Nasdaq represents that, in response to requests from NNMS Order Entry Firms, it seeks to give NNMS Order Entry Firms the same capability as all other NNMS users to have their non-directed orders match off against quote/orders previously entered by them on the opposite side of the market if those previously entered quotes/orders are at the best bid or offer price in Nasdaq, as appropriate. Like all other system users, NNMS Order Entry Firms would have the voluntary ability to prohibit or control any automatic matching through the use of an anti-internalization qualifier. Nasdaq believes that providing NNMS Order Entry Firms with the opportunity to have their quotes/orders on opposite sides of the market match off against each other will provide an additional incentive for such firms to post increased liquidity in the SuperMontage system, thereby benefiting all users.⁵

2. Statutory Basis

Nasdaq believes that the proposed rule change, as amended, is consistent with the provisions of Section 15A of the Act,⁶ in general, and with Section 15A(b)(6) of the Act,⁷ in particular, because it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with person engaged in 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.

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.

⁴ Nasdaq clarified that the rules governing UTP Exchanges do not explicitly permit this function, although NASD Rule 4710(e) contemplates that such a function may be provided by Nasdaq to a UTP Exchange pursuant to contract. Consequently, at the request of Nasdaq, Commission staff has removed a reference to UTP Exchanges contained in the original filing. Telephone conversation between Thomas P. Moran, Associate General Counsel, Nasdaq, and Ann E. Leddy, Attorney, Division, Commission (October 8, 2003).

⁵ See Amendment No. 1, *supra* note 3.

⁶ 15 U.S.C. 78o-3.

⁷ 15 U.S.C. 78o-3(b)(6).