

discretionary price range reflected in the resting DO, and would therefore expect its order to be displayed and provide liquidity, rather than to execute. By contrast, the participant entering the resting DO has, by that fact, expressed a willingness to buy (sell) at prices higher (lower) than its displayed price, but not a willingness to make its potential interest at other price levels known to other market participants. Accordingly, Nasdaq believes that it is more in keeping with the parties' expectations, and therefore fairer, to base the determination of whether the interacting orders should be delivered or automatically executed on the status of the party entering the incoming order, rather than the status of the party that originally entered the DO. When an incoming order is matched against a resting DO entered by an Order-Delivery ECN at the displayed price of the resting DO, however, the incoming order would be delivered to the Order-Delivery ECN.

DOs may only be entered as DAY orders (reflecting Nasdaq's expectation that market participants would not generally seek to reflect discretionary trading interest at multiple price points on an inter-day basis). DOs may be entered (but not displayed or executed) prior to market open. Accordingly, DOs entered before market open that do not lock or cross other Quotes/Orders will be available for interaction with other orders at 9:30 a.m. DOs that would lock or cross another Quote/Order if they were displayed will be held in a time-priority queue (along with IOC orders) and processed by the NNMS at 9:30 a.m. Since a market participant entering a DO would prefer the order to execute at its displayed price (but is also willing to accept executions within its discretionary price range), Nasdaq believes it is appropriate to prevent executions of DOs prior to 9:30 a.m., since the comparatively scattered nature of trading before the market open makes it more likely that the DO would execute at a discretionary price. This is particularly the case during the "opening spin" described in NASD Rule 4710(b)(3)(B), where DOs would have a marked tendency to execute at prices away from their displayed price. For example, if a DO to buy at 10 with a discretionary price range of up to 10.05 was processed through the opening spin, and was entered in time after a Quote/Order to sell with a price of 10.02, the DO could execute at 10.05, since Quotes/Orders in the opening spin are executed at the price of the more recent Quote/Order.¹¹

DOs may not be preferenced or directed to another market participant. In conformity with NASD Rule 4706(a)(1)(C), the system will not allow a DO to sell short to be executed if its execution would violate the short sale rule. DOs entered by a market maker with an anti-internalization qualifier value of "Y" (i.e., that may not be internalized) will be cancelled if the only available trading interest is a bid/offer entered automatically by the system under NASD Rule 4710(b)(5) after the market maker's quote has been closed.¹²

Market participants may peg the displayed price of a DO in a manner similar to that of a pegged order.¹³ Thus, a market participant can elect to enter a pegged-discretionary order that has its displayed price pegged to equal the Nasdaq inside on the same side of the market as the DO. The discretionary price range of the DO would, in turn, move along with the displayed pegged price. As with a regular pegged order, the market participant entering the order can specify a price cap, so that the displayed price of the order will become permanently fixed if the Nasdaq inside equals the price cap. A DO cannot be designated as a reverse pegged order, however, since its discretionary price range would then lock or cross the price to which the order would be pegged. If Nasdaq suspends the entry of pegged orders during a period when they are negatively impacting system capacity and performance, as permitted by NASD Rule 4706(a)(1)(B), the suspension would apply to pegged-discretionary orders as well.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of section 15A of the Act,¹⁴ in general, and with section 15A(b)(6) of the Act,¹⁵ in particular, in that it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons 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. Nasdaq believes the proposed rule change would provide market participants with a voluntary tool to

express potential trading interest at multiple price levels. Nasdaq notes that the Commission has found a similar order offered by at least one other market center to be consistent with the Act.¹⁶

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

Nasdaq does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

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.

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

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the NASD consents, the Commission will:

(A) By order approve such proposed rule change; or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

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. Comments may also be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. SR-NASD-2003-165. This file number should be included on the subject line if e-mail is used. To help us process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written

¹² *Id.*

¹³ See Securities Exchange Act Release No. 48798 (November 17, 2003) (Notice of Filing and Immediate Effectiveness of SR-NASD-2003-150).

¹⁴ 15 U.S.C. 78o-3.

¹⁵ 15 U.S.C. 78o-3(b)(6).

¹⁶ See Securities Exchange Act Release No. 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (SR-PCX-00-25).

¹¹ *Id.*