Thus, the fee has not been assessed for changes to SuperMontage Quotes/ Orders that add liquidity or that occur when an order execution occurs.

Nasdaq has recently made several enhancements to the capacity of its network systems. Specifically, hardware upgrades and improvements in system architecture have resulted in a doubling of quote update processing capability since the time when the fee was first introduced. In addition, the decision of several electronic communications networks not to participate in SuperMontage will result in a decrease in Nasdaq's quote update traffic. As a result of these factors, Nasdaq has determined that the elimination of the quote update fee is unlikely to result in a volume of quotation updates that will strain the capacity of Nasdaq's systems. Accordingly, Nasdaq is eliminating the fee in order to lower the overall cost of market participants' use of SuperMontage. Nasdaq is also eliminating the fees for cancellation of non-directed and preferenced orders entered into SuperMontage, to allow a further reduction of market participants' costs.[7]

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,[8] including Section 15A(b)(5) of the Act,[9] which requires that the rules of the NASD provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system which the NASD operates or controls.

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.

[7] The elimination of order cancellation fees is correlative to the elimination of the fee for cancellation of Quotes/Orders, since Nasdaq's billing systems are not currently programmed to distinguish between cancellation messages that relate to orders entered as non-directed or preferenced orders and those that are entered as Quotes/Orders.

[8] 15 U.S.C. 78o–3.

[9] 15 U.S.C. 78o–3(b)(5).

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

The foregoing rule change establishes or changes a due, fee, or other charge and, therefore, has become effective immediately pursuant to Section 19(b)(3)(A)(ii) of the Act[10] and Rule 19b–4(f)(2) thereunder.[11] At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change 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.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change 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 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 in 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 file number SR–NASD–2003–10 and should be submitted by February 27, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[12]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03–2946 Filed 2–5–03; 8:45 am]

BILLING CODE 8010–01–P

[10] 15 U.S.C. 78s(b)(3)(A)(ii).

[11] 17 CFR 19b–4(f)(2).

[12] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–47301; File No. SR–NASD–2002–173]

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval to a Proposed Rule Change and Amendment Nos. 1, 2, and 3 Thereto by the National Association of Securities Dealers, Inc. To Establish a 90-Day Pilot Program To Allow NNMS Order Entry Firms To Enter Non-Marketable Limit Orders Into SuperMontage Using the SIZE MMID

January 31, 2003.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on December 2, 2002, the National Association of Securities Dealers, Inc. (''NASD''), through its subsidiary, the Nasdaq Stock Market, Inc. (''Nasdaq''), filed with the Securities and Exchange Commission (''Commission'') a proposed rule change, as described in Items I and II below, which Items have been prepared by Nasdaq. The NASD amended its proposal on December 23, 2002,[3] January 29, 2003,[4] and January 30, 2003.[5] The Commission is publishing

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b-4.

[3] *See* letter from Edwards S. Knight, Executive Vice President and General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division of Market Regulation (''Division''), Commission, dated December 20, 2002, replacing the original Form 19b-4 in its entirety (''Amendment No. 1''). In Amendment No. 1, Nasdaq clarified that NNMS Order Entry Firms would be allowed to enter multiple orders (with or without reserve size) at single or multiple price levels and be subject to automatic execution functionality of the system. Nasdaq also explained that any order entered by a NNMS Order Entry Firm that created a locked/ crossed market would be processed like other locking/crossing quotes/orders as set forth in Rule 4710(b)(3). Furthermore, Nasdaq made corrections to its rule text and requested accelerated approval of the proposed rule change on a 90-day pilot basis.

[4] *See* letter from Edwards S. Knight, Executive Vice President and General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division, Commission, dated January 29, 2003, replacing in its entirety the original Form 19b-4 and Amendment No. 1 (''Amendment No. 2''). In Amendment No. 2, Nasdaq represented that additional programming to distinguish NNMS Order Entry Firms from Nasdaq Quoting Market Participants for internalization purposes would be implemented on or before April 28, 2003. Furthermore, Nasdaq provided additional rational for its request for accelerated approval by the Commission, and made corrections to its rule text.

[5] *See* letter from Thomas P. Moran, Associate General Counsel, Nasdaq, to Katherine A. England, Assistant Director, Division, Commission, dated January 30, 2003 (''Amendment No. 3''). In Amendment No. 3, Nasdaq made conforming changes to its definitions in Rule 4701 and made corrections in Rule 4710(b)(1)(B) to incorporate the changes made under the proposed rule change, as amended.

this notice to solicit comments on the proposed rule change and Amendment Nos. 1, 2 and 3 from interested persons and to approve the proposal, as amended, on an accelerated basis.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

Nasdaq proposes to allow NNMS Order Entry Firms (''OE Firms'') to enter non-marketable limit orders into SuperMontage using the SIZE Market Maker Identifier (''SIZE MMID'' or ''SIZE'') for a 90-day pilot period that commences on February 10, 2003.[6] The proposed rule language follows. Proposed new language is italicized; proposed deletions are [bracketed].

* * * * *

4701. Definitions—Unless stated otherwise, the terms described below shall have the following meaning:

* * * * *

(a) The term ''Displayed Quote/Order'' shall mean both Attributable and Non-Attributable (as applicable) Quotes/Orders transmitted to Nasdaq by Quoting Market Participants *or NNMS Order Entry Firms.*

* * * * *

(o) The term ''Non-Attributable Quote/Order'' shall mean a bid or offer Quote/Order that is entered by a Nasdaq Quoting Market Participant *or NNMS Order Entry Firm* and is designated for display (price and size) on an anonymous basis in the Nasdaq Order Display Facility.

* * * * *

(w) The term ''NNMS Order Entry Firm'' shall mean a member of the Association who is registered as an Order Entry Firm for purposes of participation in NNMS [which permits the firm to enter orders for execution against NNMS Market Makers].

* * * * *

(bb) The term ''Quote/Order'' shall mean a single quotation or shall mean an order or multiple orders at the same price submitted to Nasdaq by a Nasdaq Quoting Market Participant *or NNMS Order Entry Firm* that is displayed in the form of a single quotation. Unless specifically referring to a UTP Exchange's agency Quote/Order (as set out in Rule 4710(f)(2)(b)), when this term is used in connection with a UTP Exchange, it shall mean the best bid and/or the best offer quotation transmitted to Nasdaq by the UTP Exchange.

* * * * *

(dd) The term ''Reserve Size'' shall mean the system-provided functionality that permits a Nasdaq Quoting Market Participant *or NNMS Order Entry Firm* to display in its Displayed Quote/Order part of the full size of a proprietary or agency order, with the remainder held in reserve on an undisplayed basis to be displayed in whole or in part after the displayed part is reduced by executions to less than a normal unit of trading.

* * * * *

4706. Order Entry Parameters

(a) Non-Directed Orders—(1) General. The following requirements shall apply to Non-Directed Orders Entered by NNMS Market Participants: (A) An NNMS Participant may enter into the NNMS a Non-Directed Order in order to access the best bid/best offer as displayed in Nasdaq. (B) A Non-Directed Order must be a market or limit order, must indicate whether it is a buy, short sale, short-sale exempt, or long sale, and [if entered by a Quoting Market Participant] may be designated as ''Immediate or Cancel'', or as a ''Day'' or a ''Good-till-Cancelled'' order. If a priced order designated as ''Immediate or Cancel'' (''IOC'') is not immediately executable, the unexecuted order (or portion thereof) shall be returned to the sender. If a priced order designated as a ''Day'' order is not immediately executable, the unexecuted order (or portion thereof) shall be retained by NNMS and remain available for potential display/execution until it is cancelled by the entering party, or until 4:00 p.m. Eastern Time on the day such order was submitted, whichever comes first, whereupon it will *be* returned to the sender. If the order is designated as ''Good-till-Cancelled'' (''GTC''), the order (or unexecuted portion thereof) will be retained by NNMS and remain available for potential display/execution until cancelled by the entering party, or until 1 year after entry, whichever comes first. Starting at 7:30 a.m., until the 4:00 p.m. market close, IOC and Day Non-Directed Orders may be entered into NNMS (or previously entered orders cancelled), but such orders entered prior to market open will not become available for execution until 9:30 a.m. Eastern Time. GTC orders may be entered (or previously entered GTC orders cancelled) between the hours 7:30 a.m. to 6:30 p.m. Eastern Time, but such orders entered prior to market open, or GTC orders carried over from previous trading days, will not become available for execution until 9:30 a.m. Eastern Time. Exception: Non-Directed Day and GTC orders may be executed prior to market open if required under Rule 4710(b)(3)(B).

(C) The system will not process a Non-Directed Order to sell short if the execution of such order would violate NASD Rule 3350.

(D) Non-Directed Orders will be processed as described in Rule 4710.

(E) The NNMS shall not accept Non-Directed Orders that are All-or-None, or have a minimum size of execution.

(F) A NNMS Market Participant may enter a Non-Directed Order that is either a market order or a limit order prior to the market's open. Market orders and limit orders designated as Immediate or Cancel orders shall be held in a time-priority queue that will begin to be processed by NNMS at market open. If an Immediate or Cancel limit order is unmarketable at the time it reaches the front of time-priority processing queue, it will be returned to the entering market participant. Limit orders that are not designated as Immediate or Cancel orders shall be retained by NNMS for potential display in conformity with Rule 4707(b) and/or potential execution in conformity with Rule 4710(b)(1)(B).

(2) Entry of Non-Directed Orders by NNMS Order Entry Firms—In addition to the requirements in paragraph (a)(1) of this rule, the following conditions shall apply to Non-Directed Orders entered by NNMS Order-Entry Firms:

(A) All Non-Directed orders shall be designated as Immediate or Cancel, *GTC or Day but shall be required to be entered as Non-Attributable if not entered as IOC.* [As such] *For IOC Orders,* if after entry into the NNMS of a Non-Directed Order that is marketable, the order (or the unexecuted portion thereof) becomes non-marketable, the system will return the order (or unexecuted portion thereof) to the entering participant.

(B) A Non-Directed Order that is either a market order or a limit order may be entered prior to the market's open. Such limit and market orders will be held in a time-priority queue that will begin to be processed at market open. [If a] *A* limit order *that is designated as IOC and* is not marketable at the time it reaches the front of the time-priority processing queue [, it] will be returned to the entering participant.

(b) through (e) No Change.

* * * * *

4707. Entry and Display of Quotes/Orders

(a) Entry of Quotes/Orders—Nasdaq Quoting Market Participants may enter Quotes/Orders into the NNMS*, and NNMS Order Entry Firms may enter*

[6] This filing also makes certain non-substantive corrective and conforming changes to the written rules of the NNMS.

Non-Attributable Orders into the NNMS, subject to the following requirements and conditions:

(1) Nasdaq Quoting Market Participants shall be permitted to transmit to the NNMS multiple Quotes/Orders at a single as well as multiple price levels. Such Quote/Order shall indicate whether it is an ''Attributable Quote/Order'' or ''Non-Attributable Quote/Order,'' and the amount of Reserve Size (if applicable). *NNMS Order Entry Firms shall be permitted to transmit to NNMS multiple Non-Attributable Quotes/Orders at a single as well as multiple price levels and the amount of Reserve Size (if applicable).*

(2) Upon entry of a Quote/Order into the system, the NNMS shall time-stamp it, which time-stamp shall determine the ranking of the Quote/Order for purposes of processing Non-Directed Orders as described in Rule 4710(b). For each subsequent size increase received for an existing quote at a given price, the system will maintain the original time-stamp for the original quantity of the quote and assign a separate time-stamp to that size increase.

(3) Consistent with Rule 4613, an NNMS Market Maker is obligated to maintain a two-sided Attributable Quote/Order at all times, for at least one normal unit of trading.

(4) Nasdaq Quoting Market Participants may continue to transmit to the NNMS only their best bid and best offer Attributable Quotes/Orders. Notwithstanding NASD Rule 4613 and subparagraph (a)(1) of this rule, nothing in these rules shall require a Nasdaq Quoting Market Participant to transmit to the NNMS multiple Quotes/Orders.

(b) Display of Quotes/Orders in Nasdaq—The NNMS will display [a Nasdaq Quoting Market Participant's] Quotes/Orders *submitted to the system* as follows:

(1) Attributable Quotes/Orders—The price and size of a Nasdaq Quoting Market Participant's best priced Attributable Quote/Order on both the bid and offer side of the market will be displayed in the Nasdaq Quotation Montage under the Nasdaq Quoting Market Participant's MMID, and also will be displayed in the Nasdaq Order Display Facility as part of the aggregate trading interest at a particular price when the price of such Attributable Quote/Order falls within the number of price levels authorized for aggregation and display pursuant to Rule 4701(ee) on either side of the market. Upon execution or cancellation of the Nasdaq Quoting Market Participant's best-priced Attributable Quote/Order on a particular side of the market, the NNMS will automatically display the participant's next best Attributable Quote/Order on that side of the market.

(2) Non-Attributable Quotes/Orders—The price and size of a Nasdaq Quoting Market Participant's *and NNMS Order Entry Firm's* Non-Attributable Quote/Order on both the bid and offer side of the market will be displayed in the Nasdaq Order Display Facility as part of the aggregate trading interest at a particular price when the price of such Non-Attributable Quote/Order falls within the number of price levels authorized for aggregation and display pursuant to Rule 4701(ee) on either side of the market. A Non-Attributable *Quote/*Order will not be displayed in the Nasdaq Quotation Montage under the Nasdaq Quoting Market Participant's MMID. Non-Attributable Quotes/Orders that are the best priced Non-Attributable bids or offers in the system will be displayed in the Nasdaq Quotation Montage under an anonymous MMID, which shall represent and reflect the aggregate size of all Non-Attributable Quotes/Orders in Nasdaq at that price level. Upon execution or cancellation of a Nasdaq Quoting Market Participant's *or NNMS Order Entry Firm's* Non-Attributable Quote/Order, the NNMS will automatically display a Non-Attributable Quote/Order in the Nasdaq Order Display Facility (consistent with the parameters described above) if it falls within the number of price levels authorized for aggregation and display pursuant to Rule 4701(ee) on either side of the market.

(3) Exceptions—The following exceptions shall apply to the display parameters set forth in paragraphs (1) and (2) above:

(A) Odd-lots, Mixed Lots, and Rounding—The Nasdaq system (and all accompanying data feeds) shall be capable of displaying trading interest in round lot amounts. For quote display purposes, Nasdaq will aggregate all shares, including odd-lot share amounts, entered by a Quoting Market Participant *and NNMS Order Entry Firm* at a single price level and then round that total share amount down to the nearest round-lot amount for display and dissemination, consistent with subparagraphs (b)(1) and (b)(2) of this rule. Though rounded, any odd-lot portion of a [Quoting Market Participant's trading interest] *Quote/Order* that is not displayed as a result of this rounding process will remain in the system, with the time-priority of their original entry, and be continuously available for execution. Round-lots that are subsequently reduced by executions to a mixed lot amount will likewise be rounded for display purposes by the system to the nearest round-lot amount at that same price level. Any odd-lot number of shares that do not get displayed as a result of this rounding will remain in the system with the time-priority of their original entry and thus be continuously available for execution. If executions against an Attributable Quote/Order result in there being an insufficient (odd-lot) amount of shares at a price level to display an Attributable Quote/Order for one round-lot, the system will display the Quoting Market Participant's next best priced Attributable Quote/Order consistent with Rule 4710(b)(2). If all Attributable Quotes/Orders on the bid and/or offer side of the market are exhausted so that there are no longer any Attributable Quotes/Orders, the system may refresh a market maker's exhausted bid or offer quote using the process set forth in Rule 4710(b)(5). With the exception of Legacy Quotes, odd-lot remainders that are not displayed will remain in the system at their original price levels and continue to be available for execution.

(c) through (e) No Change.

* * * * *

4710. Participant Obligations in NNMS

(a) No Change.

(b) Non-Directed Orders.

(1) General Provisions—A Quoting Market Participant in an NNMS Security, as *well as NNMS Order Entry Firms,* shall be subject to the following requirements for Non-Directed Orders:

(A) Obligations For each NNMS security in which it is registered, a Quoting Market Participant must accept and execute individual Non-Directed Orders against its quotation, in an amount equal to or smaller than the combination of the Displayed Quote/Order and Reserve Size (if applicable) of such Quote/Order, when the Quoting Market Participant is at the best bid/best offer in Nasdaq. *This obligation shall also apply to the Non-Attributable Quotes/Orders of NNMS Order Entry Firms. Quoting Market Participants, and NNMS Order Entry Firms,* shall participate in the NNMS as follows:

(i) NNMS Market Makers, [and] NNMS Auto-Ex ECNs*, and NNMS Order Entry Firms to the extent they enter a Non-Attributable Quote/Order* shall participate in the automatic-execution functionality of the NNMS, and shall accept the delivery of an execution up to the size of the participant's Displayed Quote/Order and Reserve Size.

(ii) NNMS Order-Delivery ECNs shall participate in the order-delivery functionality of the NNMS, and shall accept the delivery of an order up to the size of the NNMS Order-Delivery ECN's Displayed Quote/Order and Reserve Size. The NNMS Order-Delivery ECN shall be required to execute the full size of such order (even if the delivered order is a mixed lot or odd lot) unless that interest is no longer available in the ECN, in which case the ECN is required to execute in a size equal to the remaining amount of trading interest available in the ECN.

(iii) UTP Exchanges that choose to participate in the NNMS shall do so as described in subparagraph (f) of this rule and as otherwise described in the NNMS rules and the UTP Plan.

(B) Processing of Non-Directed Orders—Upon entry of a Non-Directed Order into the system, the NNMS will ascertain who the next Quoting Market Participant *or NNMS Order Entry Firm* in queue to receive an order is (based on the algorithm selected by the entering participant, as described in subparagraph (b)(B)(i)–(iii) of this rule), and shall deliver an execution to Quoting Market Participants *or NNMS Order Entry Firms* that participate in the automatic-execution functionality of the system, or shall deliver a Liability Order to Quoting Market Participants that participate in the order-delivery functionality of the system; provided however, that the system always shall deliver an order (in lieu of an execution) to the Quoting Market Participant next in queue when the participant that entered the Non-Directed Order into the system is a UTP Exchange that does not provide automatic execution against its Quotes/Orders for Nasdaq Quoting Market Participants and NNMS Order Entry Firms. Non-Directed Orders entered into the NNMS system shall be delivered to or automatically executed against Quoting Market Participants' *or NNMS Order Entry Firms'* Displayed Quotes/Orders and Reserve Size in strict price/time priority, as described in the algorithm contained in subparagraph (b)(B)(i) of this rule. Alternatively, an NNMS Market Participant can designate that its Non-Directed Orders be executed based on a price/time priority that considers ECN quote-access fees, as described in subparagraphs (b)(B)(ii) of this rule, or executed based on price/size/time priority, as described in subparagraph (b)(B)(iii) of this rule. The individual time priority of each Quote/Order submitted to NNMS shall be assigned by the system based on the date and time such Quote/Order was received. Remainders of Quote/Orders reduced by execution, if retained by the system, shall retain the time priority of their original entry. For purposes of the execution algorithms described in paragraphs (i), (ii) and (iii) below, ''Displayed Quotes/Orders'' shall also include any odd-lot, odd-lot portion of a mixed-lot, or any odd-lot remainder of a round-lot(s) reduced by execution, share amounts that while not displayed in the Nasdaq Quotation Montage, remain in system and available for execution.

(i) Default Execution Algorithm—Price/Time—The system will default to a strict price/time priority within Nasdaq, and will attempt to access interest in the system in the following priority and order:

(a) Displayed Quotes/Orders of NNMS Market Makers[,] *and* NNMS ECNs, *displayed Non-Attributable Quotes/Orders of NNMS Order Entry Firms,* and *displayed* non-attributable agency Quotes/Orders of UTP Exchanges (as permitted by subparagraph (f) of this rule), in time priority between such participants' Quotes/Orders[:]*;*

(b) Reserve Size of Nasdaq Quoting Market Participants *and NNMS Order Entry Firms,* in time priority between such participants' Quotes/Orders; and

(c) Principal Quotes/Orders of UTP Exchanges, in time priority between such participants' Quotes/Orders.

(ii) Price/Time Priority Considering Quote-Access Fees—If this option[s] is chosen, the system will attempt to access interest in the system in the following priority and order:

(a) Displayed Quotes/Orders of NNMS Market Makers, *displayed Non-Attributable Quotes/Orders of NNMS Order Entry Firms, displayed Quotes/Orders of* NNMS ECNs that do not charge a separate quote-access fee to non-subscribers, and non-attributable agency Quotes/Orders of UTP Exchanges (as permitted by subparagraph (f) of this rule), as well as Quotes/Orders from NNMS ECNs that charge[s] a separate quote-access fee to non-subscribers where the ECN entering such Quote/Order indicates that the price improvement offered by the specific Quote/Order is equal to or exceeds the separate quote-access fee the ECN charges, in time priority between such participants' Quotes/Orders;

(b) Displayed Quotes/Orders of NNMS ECNs that charge a separate quote-access fee to non-subscribers, in time priority between such participants' Quotes/Orders;

(c) Reserve Size of NNMS Market Makers *and NNMS Order Entry Firms,* and NNMS ECNs that do not charge a separate quote-access fee to non-subscribers, as well as Reserve Size of Quotes/Orders from NNMS ECNs that charge[s] a separate quote-access fee to non-subscribers where the ECN entering such Quote/Order has indicated that the price improvement offered by the specific Quote/Order is equal to or exceeds the separate quote-access fee the ECN charges, in time priority between such participants' Quotes/Orders;

(d) Reserve Size of NNMS ECNs that charge a separate quote-access fee to non-subscribers, in time priority between such participants' Quotes/Orders; and

(e) Principal Quotes/Orders of UTP Exchanges, in time priority between such participants' Quotes/Orders.

(iii) Price/Size Priority—If this option is chosen, Non-Directed Orders shall be executed in price/size/time priority against:

(a) Displayed Quotes/Orders of NNMS Market Makers, *displayed Non-Attributable Quotes/Orders of NNMS Order Entry Firms, displayed Quotes/Orders of* NNMS ECNs, and non-attributable agency Quotes/Orders of UTP Exchanges (as permitted by subparagraph (f) of this rule), in price/size/time priority between such participants' Quotes/Orders[:] ;

(b) the Reserve Size of Nasdaq Quoting Market Participants *and NNMS Order Entry Firms,* in price/size/time priority between such participants' Quotes/Orders, which size priority shall be based on the size of the Displayed Quote/Order, and not on the amount held in Reserve Size; and

(c) Principal Quotes/Orders of UTP Exchanges, in price/size/time priority between such participants' Quotes/Orders.

(iv) Exceptions—The following exceptions shall apply to the above execution parameters:

(a) If a Nasdaq Quoting Market Participant 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 own Quote/Order if the participant is at the best bid/best offer in Nasdaq. *Effective February 10, 2003, until April 28, 2003 (or such earlier date as determined by Nasdaq with appropriate notice to the Securities and Exchange Commission and market participants), this processing shall also apply to Non-Directed Orders of NNMS Order Entry Firms. Thereafter, this exception shall not apply to Non-Directed Orders entered by NNMS Order Entry Firms.*

(b) If an NNMS Market Participant enters a Preferenced Order, the order shall be executed against (or delivered in an amount equal to) both the Displayed Quote/Order and Reserve Size of the Quoting Market Participant to which the order is being directed, if that Quoting Market Participant is at the best bid/best offer when the Preferenced

Order is next in line to be delivered (or executed). Any unexecuted portion of a Preferenced Order shall be returned to the entering NNMS Market Participant. If the Quoting Market Participant is not at the best bid/best offer when the Preferenced Order is next in line to be delivered (or executed), the Preferenced Order shall be returned to the entering NNMS Market Participant.

(c) If an NNMS Market Participant enters a Quote or Non-Directed Order that would result in NNMS either: (1) Delivering an execution to a Quoting Market Participant(s) *or an NNMS Order Entry Firm* that participates in the automatic-execution functionality of the system at a price substantially away from the current inside bid/offer in that security; or (2) delivering a Liability Order to a Quoting Market Participant(s) that participates in the order-delivery functionality of the system at a price substantially away from the current inside bid/offer in that security, the system shall instead process only those portions of the order that will not result in either an execution or delivery at a price substantially away from the current inside best bid/offer in the security and return the remainder to the entering party. For purposes of this subsection only, an execution or delivery based on a sell order shall be deemed to be substantially away from the current inside bid if it is to be done at a price lower than a break-price established by taking the inside bid, reducing it by 10% of the bid's value, and then subtracting $0.01. For example, in a stock with a current inside bid of $10.00, the maximum price at which a single sell order could be executed would be $8.99 calculated as follows: ($10.00 − ($10.00 × .10 e.g $1) − $.01 = $8.99). For offers, an execution or delivery based on a buy order shall be deemed to be substantially away from the current inside offer if it is done a price higher than a break-price established by taking the inside offer, adding 10% of the offer's value to it, and then adding $0.01. For example, in a stock with a current inside offer of $10.00, the highest price at which a single sell order could be executed would be $11.01 calculated as follows: ($10.00 + ($10.00 × .10 e.g. $1) + $.01 = $11.01.

(C) through (D) No Change.

(2) Refresh Functionality.

(A) Reserve Size Refresh—Once a Nasdaq Quoting Market Participant's *or NNMS Order Entry Firm's* Displayed Quote/Order size on either side of the market in the security has been decremented to an amount less than one normal unit of trading due to NNMS processing, Nasdaq will refresh the displayed size out of Reserve Size to a size-level designated by the Nasdaq Quoting Market Participant *or NNMS Order Entry Firm,* or in the absence of such size-level designation, to the automatic refresh size. The amount of shares taken out of reserve to refresh display size shall be added to any shares remaining in the Displayed Quote/Order and shall be of an amount that when combined with the number of shares remaining in the Nasdaq Quoting Market Participant's Displayed Quote/Order before it is refreshed will equal the displayed size-level designated by the Nasdaq Quoting Market Participant or, in the absence of such size-level designation, to the automatic refresh size. If there are insufficient shares available to produce a Displayable Quote/Order, the Nasdaq Quoting Market Participant's Quote/Order, and any odd-lot remainders, will be refreshed, updated, or retained, in conformity with NNMS Rules 4707 and 4710 as appropriate. To utilize the Reserve Size functionality, a minimum of 100 shares must initially be displayed in the Nasdaq Quoting Market Participant's *or NNMS Order Entry Firm's* Displayed Quote/Order, and the Displayed Quote/Order must be refreshed to at least 100 shares. This functionality will not be available for use by UTP Exchanges.

(B) Auto Quote Refresh (''AQR'')—No Change.

(3) Entry of Locking/Crossing Quotes/Orders The system shall process locking/crossing Quotes/Orders as follows:

(A) Locked/Crossed Quotes/Orders During Market Hours—If during market hours, a [Quoting Market] [P]participant enters into the NNMS a Quote/Order that will lock/cross the market (as defined in NASD Rule 4613(e)), the system will not display the Quote/Order as a quote in Nasdaq; instead the system will treat the Quote/Order as a marketable limit order and enter it into the system as a Non-Directed Order for processing (consistent with subparagraph (b) of this rule) as follows:

(i) For locked-market situations, the order will be routed to the Quoting Market Participant *or NNMS Order Entry Firm* next in queue who would be locked, and the order will be executed (or delivered for execution) at the lock price;

(ii) For crossed-market situations, the order will be entered into the system and routed to the next Quoting Market Participants *or NNMS Order Entry Firms* in queue who would be crossed, and the order will be executed (or delivered for execution) at the price of the Displayed Quote/Order that would have been crossed.

Once the lock/cross is cleared, if the participant's order is not completely filled, the system will reformat the order and display it in Nasdaq (consistent with the parameters of the Quote/Order) as a Quote/Order on behalf of the entering Quoting Market Participant *or Order Entry Firm.*

(B) No Change.

(4) through (8) No Change.

(c) No Change.

(d) NNMS Order Entry Firms.

All entries in NNMS shall be made in accordance with the procedures and requirements set forth in the NNMS User Guide *and these rules.* Orders may be entered in NNMS by the NNMS Order Entry Firm through either its Nasdaq terminal or computer interface. The system will transmit to the firm on the terminal screen and printer, if requested, or through the computer interface, as applicable, an execution report generated immediately following the execution.

(e) No Change.

* * * * *

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, as amended. The text of these statements may be examined at the places specified in Item III 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, OE Firms must designate all limit orders they enter into SuperMontage as ''Immediate-or-Cancel'' (''IOC''). This designation, while allowing such orders to potentially execute if marketable when they reach the front of the SuperMontage processing queue, also instructs the system to return the order to the OE Firms if the order's price precludes an immediate execution. In short, OE Firms can enter market orders and marketable limit orders, but cannot enter non-marketable limit orders. Nasdaq believes that the result is that all SuperMontage participants are deprived of the additional liquidity these rejected orders represent and the supply/demand information they provide the market as a whole.

In response to both the negative market impacts rejection of these orders engender, and requests from order entry market participants for enhanced access to the SuperMontage system, Nasdaq proposes that OE Firms be permitted to voluntarily enter non-marketable limit orders into SuperMontage without the IOC designation and have such order retained for potential execution [7] through display under the SIZE MMID [8] on a pilot basis for 90-days commencing February 10, 2003.

With one exception, Non-Attributable Orders entered into the system by OE Firms would be processed in the same manner as other non-attributable orders placed into SIZE by NNMS Market Makers. The only exception would be that, unlike the quotes/orders of Nasdaq Quoting Market Participants, SuperMontage would not first attempt to have Non-Attributable Orders submitted by OE Firms match off against orders entered by the same OE Firm on the other side of the market. Instead, OE Firm orders would execute based solely on the algorithm selected by the entering party (price/time, price/time with fee consideration, or price/size) against the quotes/orders of other SuperMontage users—including orders from the same OE firm entered on the other side of the market. However, the technology to support this functionality will not be available at the start of the pilot program on February 10, 2003. Instead, for a limited period, OE Firms would have their orders processed in a manner similar to Nasdaq Quoting Market Participants in that the system would first attempt to match off OE Firm orders against orders from the same OE Firm on the other side of the market. Nasdaq is working to program its system and formally commits to having the technology in place to inhibit this automatic matching, as proposed in this filing, on or before April 28, 2003.

[7] Under the proposal, OE Firms would be able to designate orders as IOC, ''Good-till-Cancelled,'' or ''Day.''

[8] The SIZE MMID is the anonymous MMID that represents the aggregate size of all Non-Attributable Quotes and Orders entered by market participants in Nasdaq at a particular price level. Non-Attributable Quotes/Orders are not displayed in the Nasdaq Quotation Montage using the market participant's MMID. Instead, the SIZE MMID is displayed and represents the aggregate, Non-Attributable trading interest at a particular price level in the Nasdaq Quotation Montage. Telephone conversation between Thomas P. Moran, Associate General Counsel, Nasdaq, and Marc F. McKayle, Special Counsel, Division, Commission, on January 30, 2003 (making corrections to the text in the footnote).

Under the proposal, OE Firms would be allowed to enter multiple orders (with or without reserve size) at single or multiple price levels, and such orders would be subject to the automatic execution functionality of the system. If any order entered by an OE Firm would create a locked/crossed market, such orders would be processed like other locking/crossing quotes/orders as set forth in NASD Rule 4710(b)(3).

Nasdaq believes that the above proposal is an important step in its ongoing process to make its systems more accessible to all NASD member firms, while ensuring that market participants who undertake the burdens of continuous liquidity provision are provided benefits commensurate with their activities. Nasdaq believes that most important, however, are the improvements to market quality that can be expected from the proposed rule change's swift implementation. In addition to enhanced liquidity and informational benefits, retention of non-marketable limit orders from OE Firms in SuperMontage can be expected, in Nasdaq's view, to reduce fragmentation of trading interest, thereby improving execution quality and speed and shrinking the costs market participants now incur when searching for trading partners in multiple venues. Finally, to the extent that any currently rejected OE Firm order is retained, Nasdaq believes that it would reduce the potential for locked/crossed markets that can occur if such rejected trading interest is subsequently displayed in an unlinked market center and thus does not benefit from SuperMontage processing that eliminated locks or crosses among all quotes and orders residing in the system.

2. Statutory Basis

Nasdaq believes that the proposed rule change, as amended, is consistent with Section 15A of the Act [9] in general, and furthers the objectives of Section 15A(b)(6) [10] in particular, in that it is 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.

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

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

[9] 15 U.S.C. 78*o*–3.

[10] 15 U.S.C. 78*o*–3(b)(6).

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. 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 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 in 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 file number SR–NASD–2002–173 and should be submitted by February 27, 2003.

IV. Commission Findings and Order Granting Accelerated Approval of the Proposed Rule Change

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 and, in particular, with the requirements of Section 15A(b)(6) of the Act,[11] in that it is 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.[12] The Commission believes that allowing OE Firms to enter non-marketable limit orders into SuperMontage using the SIZE MMID should provide greater

[11] 15 U.S.C. 78*o*–3(b)(6).

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

access to the system by all NASD members, as well as encourage OE Firms to enter orders into SuperMontage and thereby increase liquidity in the market to the benefit of all market participants. Further, even though the orders of OE Firms will not be matched off against orders entered by the same OE Firm on the other side of the market,[13] Nasdaq has represented that in all other respects, Non-Attributable Orders entered by OE Firms will be processed in the same manner as other non-attributable orders placed into SIZE by NNMS Market Makers. As a result, the Commission believes that OE Firms will have far greater access to the SuperMontage then currently exists.

The Commission further believes that the proposal is consistent with the goals of Section 11A(a)(1)(C), particularly Congress' finding that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly market to assure the economically efficient execution of securities transactions. The proposal should provide OE Firms with greater flexibility to reflect buying and selling interest at various price levels by entering Non-Attributable Orders directly into SuperMontage, instead of relying on electronic communications networks and NNMS Market Makers to post their trading interest.

Accordingly, the Commission finds good cause, pursuant to Sections 15A(b)(6) and 19(b)(2) of the Act,[14] for approving the proposed rule change, as amended, prior to the thirtieth day after the date of publication of notice of filing thereof in the **Federal Register**. The Commission believes that accelerated approval of the pilot will enable Nasdaq to allow OE Firms to enter orders into Nasdaq and thereby, remove a barrier to access to the SuperMontage, while enabling the Commission, NASD, Nasdaq, and market participants to gain actual experience with the pilot before the Commission considers permanent approval of the pilot.[15] As a result, market participants will be able to better assess the impact of the proposal and offer insightful and valuable public comment on the pilot. Further, the Commission notes that several commenters suggested that OE Firms be allowed to enter orders directly into the order display facility as part of the original public comment process on the SuperMontage proposal.[16] The Commission notes that the proposed rule change addresses those comments.

I. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act[17], that the proposed rule change, as amended, (File No. SR–NASD–2002–173) be, and it hereby is, approved on an accelerated basis, as a 90-day pilot beginning on February 10, 2003 and expiring on May 12, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[18]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 03–2950 Filed 2–5–03; 8:45 am]

BILLING CODE 8010–01–P

[13] Nasdaq's proposed rule change would eliminate the ability of OE Firms to use this feature no later than April 28, 2003.

[14] 15 U.S.C. 78*o*–3(b)(6) and 78s(b)(2).

[15] The Commission notes that approval of the pilot should not be interpreted as suggesting that the Commission is predisposed to approving the proposal on a permanent basis if requested by the NASD.

[16] *See* Securities Exchange Act Release No. 43863 (January 19, 2001), 66 FR 8020 (January 26, 2001).

[17] 15 U.S.C. 78s(b)(2).

[18] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–47295; File No. SR–PCX–2002–64]

Self-Regulatory Organizations; Order Approving Proposed Rule Change by Pacific Exchange, Inc., Relating to Rules Governing the Intermarket Linkage, and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 1 Thereto

January 31, 2003.

I. Introduction

On September 26, 2002, the Pacific Exchange, Inc. (''PCX'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (the ''Act''),[1] and Rule 19b-4 thereunder,[2] a proposed rule change to adopt new rules, governing the operation of the intermarket linkage (the ''Linkage''). The proposed rule change was published for comment in the **Federal Register** on December 26, 2002.[3] The Commission received no comments on the proposed rule change. On January 29, 2003, the Exchange filed Amendment No. 1 to the proposed rule change.[4] This order approves the proposed rule change, provides notice of filing of Amendment No. 1 and grants accelerated approval to Amendment No. 1.

II. Description of Proposal

In general, the proposed rules contain relevant definitions, establish the conditions pursuant to which market makers may enter Linkage orders, impose obligations on the Exchange regarding how it must process incoming Linkage orders, and establish a general standard that members should avoid trade-throughs.[5] The proposed rules establish potential regulatory liability for members who engage in a pattern or practice of trading through other exchanges, whether or not the exchanges traded through participate in the Linkage, provide procedures to unlock and uncross markets, and codify the ''80/20 Test'' contained in section 8(b)(iii) of the Plan for the Purpose of Creating and Operating an Intermarket Options Linkage (the ''Plan''),[6] which provides that a market maker on an Exchange would be restricted from sending principal orders (other than P/A orders, which reflect unexecuted customer orders) through the Linkage if the market maker effects less than 80 percent of specified order flow on the Exchange.

III. Discussion

The Commission has reviewed the PCX's proposed rule change and finds that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange,[7] and with the requirements of section 6(b).[8] In particular the Commission finds that the proposed rule change is designed to

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b-4.

[3] *See* Securities Exchange Act Release No. 47026 (December 18, 2002), 67 FR 78843.

[4] *See* letter from Mai S. Shiver, Senior Attorney, Regulatory Policy, PCX, to Nancy J. Sanow, Assistant Director, Division of Market Regulation, Commission, dated January 28, 2003 (''Amendment No. 1''). In Amendment No. 1, the Exchange proposed to amend: (1) The definition of ''Linkage Order'' contained in PCX Rule 6.92(a)(12) to state that such orders are immediate or cancel orders; (2) PCX Rule 6.93(e) to clarify the Lead Market Market's obligation to address a linkage order when such order is not eligible to be automatically executed; (3) PCX Rule 6.94(a) to clarify language regarding liability for trade-throughs at the end of the trading day and to request approval of this provision only for a one-year pilot period; and (4) PCX Rule 6.94(e) to clarify that members may not engage in a pattern or practice of trading through.

[5] Trade-throughs occur when broker-dealers execute customer orders on one exchange at prices inferior to another exchange's disseminated quote.

[6] Approved by the Commission in Securities Exchange Act Release No. 43086 (July 28, 2000), 65 FR 48023 (August 4, 2000), as subsequently amended. *See* Securities Exchange Act Release No. 44482 (June 27, 2001), 66 FR 35470 (July 5, 2001) (''Initial Amendment Order'') and Securities Exchange Act Release No. 46001 (May 30, 2002), 67 FR 38687 (June 5, 2002); 47274 (January 29, 2003); and 47298 (January 31, 2003).

[7] In approving this rule proposal, the Commission notes that it has also considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[8] 15 U.S.C. 78f(b).