

submission of a filing with the Commission regarding proposed rule changes.

By the Commission.

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Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49266; File No. SR-NASD-2004-015]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the National Association of Securities Dealers, Inc. To Restore the Pre-Trade Only Anonymity Function for SuperMontage

February 17, 2004.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 27, 2004, the National Association of Securities Dealers, Inc. (“NASD”), through its subsidiary, The Nasdaq Stock Market, Inc. (“Nasdaq”), submitted to the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. On February 5, 2004, Nasdaq filed Amendment No. 1 to the proposal.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

Nasdaq is proposing to restore the pre-trade only anonymity option for orders submitted to the Nasdaq National Market Execution System (commonly known as SuperMontage).

The text of the proposed rule change is below. Proposed new language is italicized; deleted language is bracketed.

\* \* \* \* \*

#### 4719. Anonymity

##### (a) Pre-Trade Anonymity.

(1) *With the exception of those transactions described in paragraph (a)(2) below, the identity of the member submitting a Non-Attributable Quote/Orders seeking pre-trade anonymity will remain anonymous until execution, at which time the member’s identity will be revealed to its contra party.*

(2) *A Non-Attributable Quote/Order seeking pre-trade anonymity will be processed on a fully anonymous basis in accordance with paragraph (b) below when it matches and executes against a Non-Attributable Quote/Order seeking full anonymity.*

##### (b) Full Anonymity.

[(a)](1) Transactions executed in NNMS in which at least one member submits a Non-Attributable Quote/Order seeking full anonymity will be processed anonymously. The transaction reports will indicate the details of the transactions, but will not reveal contra party identities.

[(b)(1)](2)(A) The processing described in paragraph [(a)](b)(1) shall not apply to transactions executed in NNMS when the member whose Quote/Order is decremented is an Order-Delivery ECN that charges an access fee.

[(2)](B) Except as required to comply with the request of a regulator, or as ordered by a court or arbitrator, Order-Delivery ECNs shall not disclose the identity of the member that submitted a Non-Attributable Quote/Order that decremented the Order-Delivery ECN’s Quote/Order.

[(c)](3) The Association will reveal a member’s identity in the following circumstances:

[(1)](A) when the National Securities Clearing Corporation (“NSCC”) ceases to act for a member, or the member’s clearing firm, and NSCC determines not to guarantee the settlement of the member’s trades;

[(2)](B) for regulatory purposes or to comply with an order of an arbitrator or court; or

[(3)](C) on risk management reports provided to the member’s contra parties each day after 4:00 p.m., which disclose trading activity on an aggregate dollar value basis.

[(d)](4) The Association will reveal to a member, no later than the end of the day on the date an anonymous trade was executed, when the member’s Quote/Order has been decremented by another Quote/Order submitted by that same member.

[(e)(i)](5)(A) In order to satisfy members’ record keeping obligations under SEC Rules 17a-3(a)(1) and 17a-4(a), Nasdaq shall, with the exception of

those circumstances described in subparagraph [(ii)](B) below, retain for the period specified in Rule 17a-4(a) the identity of each member that executes [an] a fully anonymous transaction described in paragraph [(a)](b) of Rule 4719. The information shall be retained in its original form or a form approved under Rule 17a-6.

[(ii)](B) In the situations described in paragraphs [(b)(1)](b)(2) or [(d)](b)(4) of Rule 4719, and solely with respect to the member that submits, and receives an execution of, a fully anonymous Non-Attributable Quote/Order that is a Preferred Order, the member retains the obligation to comply with Rules 17a-3(a)(1) and 17a-4(a) because it possesses the identity of its contra party.

#### 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 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

In response to requests from members, Nasdaq is proposing to restore the pre-trade only anonymity option for orders submitted to SuperMontage. Pre-trade anonymity will be an option in addition to the full anonymity feature.<sup>4</sup> With respect to anonymity, members will now have the choice to submit orders that will preserve their anonymity on a pre-trade basis only or through

<sup>4</sup> An attributable Quote/Order is the default for a market maker or Electronic Communication Network (“ECN”). If a market maker or ECN wants to trade in anonymous fashion (*i.e.*, a non-attributable Quote/Order), it must indicate either pre-trade anonymity or full anonymity. The default for Order Entry (“OE”) Firms is different because an OE Firm is not allowed to display Quote/Orders under its own market participant identification. If an OE Firm submits an Immediate or Cancel (“IOC”) order (*i.e.*, no chance of the order being displayed on the book), the default is no anonymity. However, if the OE Firm submits something other than an IOC order, the default is full anonymity. An OE Firm must affirmatively choose pre-trade anonymity. See e-mails from Peter Geraghty, Associate Vice President and Associate General Counsel, Nasdaq, to Marc McKayle, Special Counsel, Division, Commission, dated February 4 and February 12, 2004.

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Peter Geraghty, Associate Vice President and Associate General Counsel, Nasdaq, to Marc McKayle, Special Counsel, Division of Market Regulation (“Division”), Commission, dated February 4, 2004 (“Amendment No. 1”). In Amendment No. 1, Nasdaq amended the proposal rule change for consideration under Section 19(b)(3)(A) of the Act, and Rule 19b-4(f)(6) thereunder, as opposed to Rule 19b-4(f)(5).

settlement (*i.e.*, full anonymity). Pre-trade anonymity is the functionality that existed in SuperMontage prior to the Commission approving the full anonymity feature on September 23, 2003.<sup>5</sup>

Pre-trade only anonymity will function in the same manner as it did prior to full anonymity becoming available, with one exception discussed below. A member seeking pre-trade anonymity will submit a Non-Attributable Quote/Order indicating it is seeking pre-trade anonymity. If the order is not marketable immediately, the order will be placed in the SuperMontage book and reside under the SIZE acronym. Once the order is executed, whether immediately upon submission to SuperMontage or when an incoming order matches against the anonymous order as it resides in SIZE, the identity of the member that submitted the order will be revealed to its contra party on the SuperMontage and Automated Confirmation Transaction Service ("ACT") reports.<sup>6</sup> Both members that are a party to the trade will know the identity of their contra party.<sup>7</sup> In addition, the members' identities will be revealed on the contract sheets issued by the National Securities Clearing Corporation.

The one difference between how pre-trade only anonymous orders will be processed under this proposal, compared to the processing that occurred prior to full anonymity being implemented, occurs when an order seeking pre-trade only anonymity matches against an order seeking full anonymity. In such instances, the trade will be processed on a fully anonymous basis consistent with NASD Rule 4719(b), as amended.

<sup>5</sup> See Securities Exchange Act Release No. 48527 (September 23, 2003), 68 FR 56361 (September 30, 2003).

<sup>6</sup> Presently, anonymous orders submitted to SuperMontage can reside on the book under SIZE, however, with certain exceptions described in NASD Rule 4719, the identities of the members who executed the anonymous order are not revealed. Similarly, the members remain anonymous today when an anonymous order is executed immediately upon submission to SuperMontage.

<sup>7</sup> Because members will know the identities of their contra-parties when a pre-trade only anonymity order is executed, members must comply with the recordkeeping obligations under SEC Rules 17a-3(a)(1) and 17a-4(a) to record and maintain the identities of their contra-parties. See NASD Rule 4719.

Similarly, the exemption the Commission issued with respect to SEC Rule 10b-10 relieving members of their obligation to provide customers with the identities of their contra-parties is not available because members will know the identities of their contra-parties. See letter from Brian A. Bussey, Assistant Chief Counsel, Division of Market Regulation, Commission, to Edward S. Knight, Executive Vice President and General Counsel, Nasdaq, dated September 23, 2003.

## 2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,<sup>8</sup> in general, and with Section 15A(b)(6) of the Act,<sup>9</sup> in particular, in that it is designed to foster coordination and cooperation with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities. The proposal is consistent with this obligation because it provides members an additional option for submitting anonymous orders and it is functionality that previously existed in SuperMontage.

### *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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act,<sup>10</sup> and subparagraph (f)(6) of Rule 19b-4,<sup>11</sup> thereunder because it does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate. At any time within 60 days of the filing of the 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.<sup>12</sup>

<sup>8</sup> 15 U.S.C. 78o-3.

<sup>9</sup> 15 U.S.C. 78o-3(b)(6).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>11</sup> 17 CFR 240.19b-4(f)(6).

<sup>12</sup> The pre-trade only anonymity feature will be available on or after April 19, 2004; the exact date of implementation has not been finalized. Nasdaq will issue a Head Trader Alert informing members of the exact date when this feature will be available again. For the purposes of determining the effective date and calculating the 60-day abrogation period, the Commission considers the proposed rule change to have been filed on February 5, 2004, the date Nasdaq filed Amendment No. 1.

## 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](mailto:rule-comments@sec.gov). All comment letters should refer to File No. SR-NASD-2004-015. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, comments should be sent in hard copy 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 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-2004-015 should be submitted by March 16, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

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<sup>13</sup> 17 CFR 200.30-3(a)(12).