

Barbara Z. Sweeney
Senior Vice President
and Corporate Secretary

November 21, 2003

Ms. Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: **File No. SR-NASD-2003-145, Amendment No. 1**

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed please find Amendment No. 1 to the above-numbered rule filing. At the request of the staff of the Division of Market Regulation, this amendment is intended to replace the original rule filing in its entirety. Also enclosed is a 3-1/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Philip A. Shaikun, Office of General Counsel, Regulatory Policy and Oversight, NASD at (202) 728-8451; e-mail philip.shaikun@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Barbara Z. Sweeney

Enclosures

cc: John Polise

File No. SR-NASD-2003-145
Consists of 18 Pages
November 21, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

Form 19b-4

Proposed Rule Change

by

NASD

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act” or “Act”), the National Association of Securities Dealers, Inc. (“NASD”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend Rules 4300A and 4619A(g) to give jurisdiction to NASD’s Market Regulation Committee (“MRC”) to review system outage determinations under Rule 4300A(f) and excused withdrawal denials under Rule 4619A, respectively.

The proposed rule change would apply during the time that the NASD Alternative Display Facility operates on a pilot basis. The Commission previously approved the ADF as a nine-month pilot to quote and trade only Nasdaq-listed securities.¹ The Commission subsequently approved an extension of the pilot until January 26, 2004.² As further discussed below, NASD is filing the proposed rule change for immediate effectiveness.

The text of the proposed rule is set forth below. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

4300A. Quote and Order Access Requirements

(a) through (e) No change.

(f) Procedures for Reviewing System Outages

(1) through (4) No change.

¹ Exchange Act Release No. 46249 (July 24, 2002), 67 Fed. Reg. 49822 (July 31, 2002).

² Exchange Act Release No. 47633 (April 10, 2003), 68 Fed. Reg. 19043 (April 17, 2003).

(5) A Market Participant may appeal a determination made under paragraph (e)(3) to a three-member subcommittee comprised of current or former industry members of NASD's Market Regulation [Alternative Display Facility Market Operations Review] Committee in writing, via facsimile or otherwise, by the close of business on the day a determination is rendered pursuant to paragraph (e)(3). An appeal to the subcommittee[Committee] shall operate as a stay of the determination made pursuant paragraph (e)(3). Once a written appeal has been received, the Market Participant may submit any additional supporting written documentation, via facsimile or otherwise, up until the time the appeal is considered by the subcommittee[Committee]. The subcommittee[Committee] shall render a determination by the close of business following the day a notice of appeal is received. The subcommittee's[Committee's] determination shall be final and binding.

* * * * *

4619A. Withdrawal of Quotations and Passive Market Making

(a) through (f) No Change

(g) A three-member subcommittee comprised of current or former industry members of NASD's [Alternative Display Facility Operations Review] Market Regulation Committee shall have jurisdiction over proceedings brought by market makers seeking review of a denial of an excused withdrawal pursuant to this Rule, or the conditions imposed on their reentry.

* * * * *

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) The proposed rule change was approved by the Executive Committee of the Board of Governors of NASD on September 15, 2003 and authorized for filing with the SEC. No other action by NASD is necessary for the filing of the proposed rule change. Section 1(a)(iii) of Article VII of NASD By-Laws permits NASD Board to adopt amendments to NASD Rules without recourse to the membership for approval.

(b) Questions regarding this rule filing may be directed to Philip A. Shaikun, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, NASD, at (202) 728-8451.

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

(a) Purpose

Background

On July 24, 2002, the Commission approved SR-NASD 2002-97, which authorizes NASD to operate the ADF on a pilot basis for nine months, pending the anticipated approval of SR-NASD-2001-90, which proposes to operate the ADF on a permanent basis.³ On April 10, 2003, the Commission approved SR-NASD-2003-53, authorizing extension of the ADF pilot period until January 26, 2004.⁴ As described in detail in SR-NASD-2001-90, the ADF is a quotation collection, trade comparison, and trade reporting facility developed by NASD in accordance with

³ Exchange Act Release No. 46249 (July 24, 2002), 67 Fed. Reg. 49822 (July 31, 2002).

⁴ Exchange Act Release No. 47633 (April 10, 2003), 68 Fed. Reg. 19043 (April 17, 2003).

the Commission's SuperMontage Approval Order⁵ and in conjunction with Nasdaq's anticipated registration as a national securities exchange.⁶

For the duration of the pilot period, ADF will provide ADF market participants (market makers and ECNs) the ability to post quotations in Nasdaq securities and will provide all members that participate in the ADF the ability to view quotations and report transactions in Nasdaq securities to the Exclusive Securities Information Processor ("SIP") for Nasdaq-listed issues⁷ for consolidation and dissemination of data to vendors and ADF market participants. The facility also will provide for trade comparison through the Trade Reporting and Comparison Service ("TRACS"). The facility further will provide for real-time data delivery to NASD for regulatory purposes, including enforcement of firm quote and related rules. It is anticipated that the ADF will operate on a pilot basis until the effective date of SR-NASD-2001-90, the approval of which would provide for the operation of the ADF on a permanent basis and an expansion of ADF-eligible securities to include all exchange-listed securities.

Order Access Rule

The ADF does not provide an order routing capability. Instead, pilot Rule 4300A requires market participants to provide direct electronic access to other market participants and to provide to all other NASD members direct electronic access or allow for indirect electronic access to the individual market participant's quote. This rule provides the means for ADF market participants

⁵ Exchange Act Release No. 43863 (January 19, 2001), 66 Fed. Reg. 8020 (January 26, 2001) (File No. SR-NASD-99-53).

⁶ Exchange Act Release No. 44396 (June 7, 2001), 66 Fed. Reg. 31952 (June 13, 2001) (File No. 10-131).

⁷ Nasdaq initially will be the designated SIP for all transactions and quotations in Nasdaq securities. During the pilot period, the SIP will distribute individual quotations for both ADF and Nasdaq market makers and ECNs.

and other broker/dealers to access ADF quotes and, among other things, to meet the firm quote and locked and crossed quotation requirements.

System Outage Determinations

Pursuant to NASD Rule 4300A(e)(2), NASD may suspend a market participant from quoting for 20 business days if the market participant experiences three unexcused, confirmed system outages during any period of five business days. The Rule defines system outages as (1) an inability to quote or (2) an inability to respond to orders. The Rule gives officers of NASD authority to review an outage and determine whether the outage should be excused. An officer may deem a system outage excused based on the specific facts and circumstances surrounding the outage. Most significant consideration is given to whether the system outage resulted from circumstances beyond the market participant's control and whether the market participant voluntarily brought the matter to the attention of NASD before it otherwise learned of the outage. Other factors that may be considered include, but are not limited to, the extent and duration of the system problem.

Rule 4300A provides for a review and appeal process of a determination of whether an outage is excused or unexcused. Currently, Rule 4300A(f)(5) gives authority for such reviews to NASD's Alternative Display Facility Market Operations Review Committee. The proposed rule change would amend that provision to give review authority to a three-member subcommittee comprised of current or former industry members of NASD's MRC to take advantage of that committee's expertise. It would be NASD's intention to draw first from current MRC members and resort to former members only when conflicts or availability problems exist with current members.

Denial of Excused Withdrawals

Rule 4619A generally provides that NASD Alternative Display Facility Operations may, under certain circumstances, grant excused withdrawal status to an ADF Market Maker that withdraws its quotations from a security. Rule 4619A(g) provides for review of a denial of an excused withdrawal and gives authority for such reviews to NASD's Alternative Display Facility Market Operations Review Committee. The proposed rule change would amend that provision to give review authority to a three-member subcommittee comprised of current or former industry members of the MRC, as would be the case for system outage proceedings described above.

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that NASD rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the MRC is the appropriate committee to review ADF system outage and denial of excused withdrawal determinations.

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

NASD 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.

5. 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.

6. Extension of Time Period for Commission Action

NASD does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

NASD requests the Commission to find good cause pursuant to Section 19(b)(2) for approving the proposed rule change prior to the 30th day after its publication in the Federal Register. The proposed rule change will result in more effective administration of the ADF pilot program, which has already been approved by the Commission and is in operation. Further, the proposed rule change does not change the review process previously approved by the Commission, but only changes the Committee responsible for that process. Accordingly, good cause exists for the Commission to accelerate the effectiveness of the proposed rule change prior to the 30th day after its publication in the Federal Register.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD

BY: _____
Barbara Z. Sweeney
Senior Vice President and Corporate Secretary

Date: November 21, 2003

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-

; File No. SR-NASD-2003-145)

Self-Regulatory Organizations; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change To Give Authority to NASD's Market Regulation Committee To Review Alternative Display Facility System Outage and Denial of Excused Withdrawal Determinations

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act" or "Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on _____, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. NASD has designated the proposed rule change as concerned solely with administration of the self regulatory organization under Section 19(b)(3)(A)(iii) of the Act³ and Rule 19b-4(f)(3) thereunder,⁴ which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act" or "Act"), the National Association of Securities Dealers, Inc. ("NASD") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. § 78s(b)(3)(A)(iii).

⁴ 17 CFR § 240.19b-4(f)(3).

change to amend Rules 4300A and 4619A(g) to give jurisdiction to NASD's Market Regulation Committee ("MRC") to review system outage determinations under Rule 4300A(f) and excused withdrawal denials under Rule 4619A, respectively.

The proposed rule change would apply during the time that the NASD Alternative Display Facility operates on a pilot basis. The Commission previously approved the ADF as a nine-month pilot to quote and trade only Nasdaq-listed securities.⁵ The Commission subsequently approved an extension of the pilot until January 26, 2004.⁶ The text of the proposed rule is set forth below. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

4300A. Quote and Order Access Requirements

(a) through (e) No change.

(f) Procedures for Reviewing System Outages

(1) through (4) No change.

(5) A Market Participant may appeal a determination made under paragraph (e)(3) to a three-member subcommittee comprised of current or former industry members of NASD's Market Regulation [Alternative Display Facility Market Operations Review] Committee in writing, via facsimile or otherwise, by the close of business on the day a determination is rendered pursuant to paragraph (e)(3). An appeal to the subcommittee[Committee] shall operate as a stay of the determination made pursuant paragraph (e)(3). Once a written appeal has been received, the Market Participant may

⁵ Exchange Act Release No. 46249 (July 24, 2002), 67 Fed. Reg. 49822 (July 31, 2002).

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submit any additional supporting written documentation, via facsimile or otherwise, up until the time the appeal is considered by the subcommittee[Committee]. The subcommittee[Committee] shall render a determination by the close of business following the day a notice of appeal is received. The subcommittee's[Committee's] determination shall be final and binding.

* * * * *

4619A. Withdrawal of Quotations and Passive Market Making

(a) through (f) No Change

(g) A three-member subcommittee comprised of current or former industry members of NASD's [Alternative Display Facility Operations Review] Market Regulation Committee shall have jurisdiction over proceedings brought by market makers seeking review of a denial of an excused withdrawal pursuant to this Rule, or the conditions imposed on their reentry.

* * * * *

II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its original rule filing with the Commission, NASD 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. NASD 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

(a) Purpose

Background

On July 24, 2002, the Commission approved SR-NASD 2002-97, which authorizes NASD to operate the ADF on a pilot basis for nine months, pending the anticipated approval of SR-NASD-2001-90, which proposes to operate the ADF on a permanent basis.⁷ On April 10, 2003, the Commission approved SR-NASD-2003-53, authorizing extension of the ADF pilot period until January 26, 2004.⁸ As described in detail in SR-NASD-2001-90, the ADF is a quotation collection, trade comparison, and trade reporting facility developed by NASD in accordance with the Commission's SuperMontage Approval Order⁹ and in conjunction with Nasdaq's anticipated registration as a national securities exchange.¹⁰

For the duration of the pilot period, ADF will provide ADF market participants (market makers and ECNs) the ability to post quotations in Nasdaq securities and will provide all members that participate in the ADF the ability to view quotations and report transactions in Nasdaq securities to the Exclusive Securities Information Processor ("SIP") for Nasdaq-listed issues¹¹ for consolidation and dissemination of data to vendors and ADF market participants. The facility also

⁷ Exchange Act Release No. 46249 (July 24, 2002), 67 Fed. Reg. 49822 (July 31, 2002).

⁸ Exchange Act Release No. 47633 (April 10, 2003), 68 Fed. Reg. 19043 (April 17, 2003).

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will provide for trade comparison through the Trade Reporting and Comparison Service (“TRACS”). The facility further will provide for real-time data delivery to NASD for regulatory purposes, including enforcement of firm quote and related rules. It is anticipated that the ADF will operate on a pilot basis until the effective date of SR-NASD-2001-90, the approval of which would provide for the operation of the ADF on a permanent basis and an expansion of ADF-eligible securities to include all exchange-listed securities.

Order Access Rule

The ADF does not provide an order routing capability. Instead, pilot Rule 4300A requires market participants to provide direct electronic access to other market participants and to provide to all other NASD members direct electronic access or allow for indirect electronic access to the individual market participant’s quote. This rule provides the means for ADF market participants and other broker/dealers to access ADF quotes and, among other things, to meet the firm quote and locked and crossed quotation requirements.

System Outage Determinations

Pursuant to NASD Rule 4300A(e)(2), NASD may suspend a market participant from quoting for 20 business days if the market participant experiences three unexcused, confirmed system outages during any period of five business days. The Rule defines system outages as (1) an inability to quote or (2) an inability to respond to orders. The Rule gives officers of NASD authority to review an outage and determine whether the outage should be excused. An officer may deem a system outage excused based on the specific facts and circumstances surrounding the

¹¹ Nasdaq initially will be the designated SIP for all transactions and quotations in Nasdaq securities. During the pilot period, the SIP will distribute individual quotations for both ADF and Nasdaq market makers and ECNs.

outage. Most significant consideration is given to whether the system outage resulted from circumstances beyond the market participant's control and whether the market participant voluntarily brought the matter to the attention of NASD before it otherwise learned of the outage. Other factors that may be considered include, but are not limited to, the extent and duration of the system problem.

Rule 4300A provides for a review and appeal process of a determination of whether an outage is excused or unexcused. Currently, Rule 4300A(f)(5) gives authority for such reviews to NASD's Alternative Display Facility Market Operations Review Committee. The proposed rule change would amend that provision to give review authority to a three-member subcommittee comprised of current or former industry members of NASD's MRC to take advantage of that committee's expertise. It would be NASD's intention to draw first from current MRC members and resort to former members only when conflicts or availability problems exist with current members.

Denial of Excused Withdrawals

Rule 4619A generally provides that NASD Alternative Display Facility Operations may, under certain circumstances, grant excused withdrawal status to an ADF Market Maker that withdraws its quotations from a security. Rule 4619A(g) provides for review of a denial of an excused withdrawal and gives authority for such reviews to NASD's Alternative Display Facility Market Operations Review Committee. The proposed rule change would amend that provision to give review authority to a three-member subcommittee comprised of current or former industry members of the MRC, as would be the case for system outage proceedings described above.

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that NASD rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the MRC is the appropriate committee to review ADF system outage and excused withdrawal determinations.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD 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

Written comments were neither solicited nor received.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

NASD has requested that the Commission find good cause pursuant to Section 19(b)(2) for approving the proposed rule change prior to the 30th day after publication in the Federal Register. The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to NASD and, in particular, the requirements of Section 15A and the rules and regulations thereunder. The Commission finds good cause for approving the proposed rule change prior to the 30th day after the date of publication of notice of filing thereof in that accelerated approval will result in more effective

administration of the ADF pilot program, which has already been approved by the Commission and is in operation. Further, the proposed rule change does not change the review process previously approved by the Commission, but only changes the Committee responsible for that process.

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 self-regulatory organization 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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. 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 the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act, that the proposed rule change be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland
Deputy Secretary